

## Lender-Placed Insurance

### *Protecting American Homeownership and the Mortgage Process*

Lender-placed insurance serves a necessary and valuable role in American homeownership. It is utilized only when homeowners do not maintain their own insurance coverage on their properties. Claims due to events such as fire and severe weather could be devastating for homeowners who, for whatever reason, had failed to carry insurance.

Lender-placed insurance is a safety net for homeowners, lenders, and mortgage investors alike.

### **Lender-placed insurance: the basics**

Lender-placed insurance has been part of the mortgage process for decades, with its origins rooted in the modernization of the banking system beginning in the 1960s.

When a home loan is approved, the mortgage servicer (usually a bank) requires the borrower, under the terms of the mortgage, to carry the proper amount of hazard insurance on the property to insure it against fire and other perils. It's crucial for the lender to make sure that the property is insured against loss because it's part of the collateral that secures the loan. This is one of a homebuyer's primary responsibilities under a mortgage, and it is disclosed in the lending documents signed by the borrower.

Homeowners can fail to maintain the required coverage for a variety of reasons - cancellation, a withdrawal by their existing insurer, or even just a simple oversight. But if a homeowner does fail to maintain proper insurance on the property, the lender will purchase insurance to cover the property until the homeowner obtains coverage, in accordance with terms of the mortgage. This is known as lender-placed insurance.

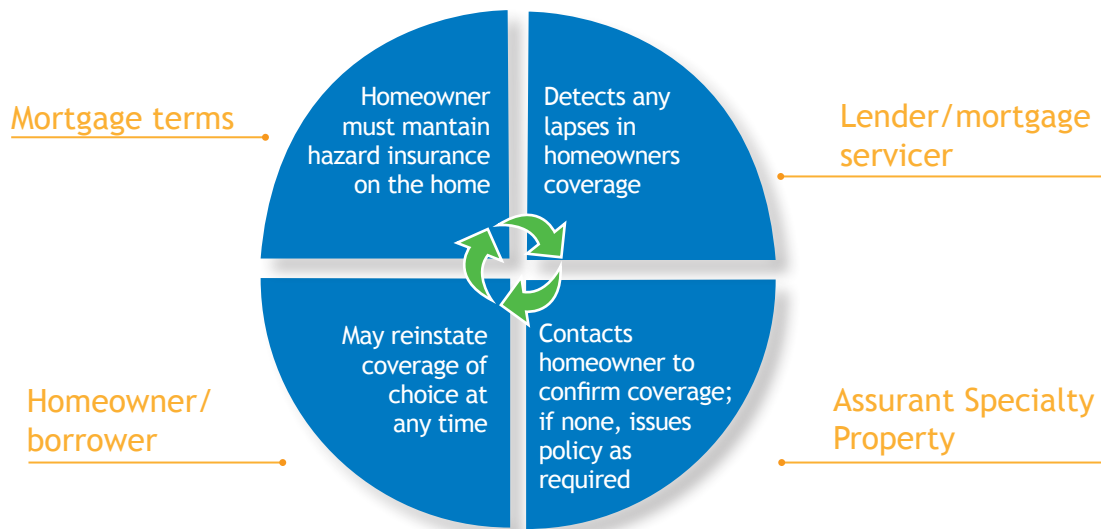
Lender-placed insurance is a critical component of virtually every mortgage. Lenders and mortgage servicers aren't the only party with a vested interest in a homeowner's property. Investors who buy mortgages, such as through residential mortgage-backed securities, also have a stake.

Once the lender has established a possible lack of insurance or inadequate coverage, an effort begins to confirm coverage, and arrange for the issuance of a lender-placed policy if necessary. This insures that the property remains protected against damage or financial loss - safeguarding the interests of the bank and the homeowner alike.

Lenders and servicers have a responsibility to ensure continuous insurance coverage on mortgaged properties, to protect their interests and those of other investors. This coverage is called for under guidelines promulgated by the government-sponsored mortgage organizations Fannie Mae and Freddie Mac, and under most security

agreements supporting the issuance of mortgage-backed securities. Because continuous insurance coverage is required by lenders and other stakeholders, the policy becomes effective at the time of the lapse. It then can cover losses that may occur after the date of lapse.

The lender pays the premiums on the lender-placed policy, which is then collected back from the borrower - usually by an adjustment to the monthly payment. If it's determined later that adequate coverage was in place after all and no lapse occurred, the lender-placed policy is canceled fully. The homeowner is then refunded any premiums paid on the lender-placed policy. In cases where a lapse in coverage does occur, the borrower is charged only for the period of the lapse.



## What's covered?

Lender-placed insurance provides coverage for the structural property. It typically does not extend to liability coverage or a homeowner's personal contents, as the lender has no collateral interest in these items. The value of the policy is typically based on the last known insured value, as established by the homeowner and their previous insurance carrier.

Lender-placed insurance is not merely limited to the outstanding loan balance; it provides structural coverage, similar to that of a standard homeowners policy. The lender-placed policy is based on replacement cost, to make sure the property is repaired or rebuilt completely in the event of damage, and is dual-interest. The homeowner and the lender each have an interest in the property, and they are both protected in the event of a claim.

Therefore, lender-placed insurance protects both the lender's interest and the borrower's interest and equity.

## Insurance lapses: flirting with disaster

A homeowner might allow his or her homeowners insurance policy to lapse for any number of reasons: a carrier cancellation, missed premiums, an oversight, or lost paperwork, just to name a few. However, not having homeowners insurance could spell disaster if an unforeseen event occurs.

Consider Joplin, Missouri's devastating tornado on May 22, 2011. The National Weather Service declared it one of the nation's deadliest in history. The tornado's toll was staggering: 159 people died and more than 1,000 were injured. It leveled much of what stood in its 22-mile-long, 1-mile-wide path.

Assurant Specialty Property handled **78 claims**, totaling more than **\$2.2 million**, from the Joplin storm alone. Most of these were cases where the homeowner originally had insurance through another carrier, but their policies had lapsed. Assurant Specialty Property was there to step in and "bridge the gap" in coverage, allowing these homeowners to rebuild.

Assurant is on the scene time and again in response to catastrophes. A more widespread storm was Hurricane Irene, which soaked the eastern U.S. coast in August 2011. Assurant incurred more than **\$75 million in claims** from Irene, from more than 10,000 homeowners. Again, their insurance enabled them to rebuild in the wake of serious storm damage.

### Quick facts:

- 99 major disasters were declared in the U.S. in 2011

- More than \$185 million in 2011 catastrophe claims by Assurant policyholders

*Sources: FEMA.gov, the National Weather Service, Assurant*

## Protecting the mortgage system

Lender-placed insurance is a critical part of the lending process. By protecting collateral, it supports lenders' ability to continue to lend.

Many of the nation's leading banks and lenders hire Assurant to help monitor their portfolio of home loans to make sure that borrowers are maintaining adequate insurance coverage. Assurant has invested heavily in developing robust, proprietary technology that monitors the insurance coverage on millions of homes where our clients' mortgages are in place, checking millions of data points in real time from more than 20,000 different insurance forms. Assurant receives more than 100,000 pieces of paper correspondence each day, along with electronic data feeds providing millions of inputs. All this information helps banks control risk. Without this service, banks and other lenders could find themselves extremely vulnerable if their collateral interests are underinsured or uninsured.



*Lender-placed insurance quite simply makes home mortgages possible. It's like this: When you get a mortgage, one of those papers you sign promises you'll keep insurance on your house, and if you don't, the bank will. That's because they've got an investment in that house too. Without that safety net, you'd find it extremely difficult to ever get a loan to buy a home."*

*-Gene Mergelmeyer, President and CEO, Assurant Specialty Property*

## **Assurant's commitment to transparency and protecting customers**

Over the course of its 100-year history, Assurant has developed products and processes designed to be fair, transparent, and beneficial to all parties involved.

Assurant works hard to protect the interests of homeowners and lenders alike. The company follows a detailed process of notification, disclosure, and checks and balances.

### **Notification to homeowners**

Assurant believes that lender-placed insurance should be a last resort. Under the direction of our clients, we work to notify customers about suspected lapses so that they have adequate time to remedy the issue on their own.

If a potential lapse in coverage is detected, an extensive process of outreach and notification through phone calls and written correspondence begins. This process usually takes at least 75 days to complete. During this time, the homeowner has ample opportunity to confirm that proper coverage exists. Even if a lapse is confirmed, the homeowner is strongly encouraged to reinstate his or her own coverage. If Assurant customer service professionals are unable to verify insurance, after 75 days and multiple points of contact with the homeowner and the last known insurance carrier or agent, a lender-placed policy from Assurant is put in place. Clear disclosure is important. Under Assurant's process, the homeowner receives a full copy of the insurance policy so that they know exactly what coverage has been purchased on their behalf.

The homeowner always maintains the option of obtaining or renewing the insurance of his or her choice. Even after a lender-placed insurance policy is put in place, they can obtain other coverage, and the lender-placed policy will be canceled at the point voluntary coverage is effective.

Assurant maintains a strong track record of accuracy. However, sometimes a homeowner may change homeowners insurance carriers without notifying the lender or loan servicer. If the required insurance is actually in place, the homeowner simply has to show proof of continuous coverage. The lender-placed policy is then canceled at no charge.

## An uncommon occurrence

Of the millions of loans monitored annually by Assurant, approximately 13 percent will be identified with a potential lapse in insurance. With the effectiveness of Assurant's extensive customer notification processes, most of these lapses will be resolved with the homeowner renewing or replacing coverage on their own. Only about 2 percent will proceed to protection by a lender-placed policy.

## Pricing

Assurant works hard to maintain fair pricing on its policies, even though it operates under a very different business model than standard homeowners carriers.

### Unlike conventional carriers, Assurant:

- Contractually agrees to insure all lapsed properties in a lender's portfolio
- Puts policies in place with no individual risk underwriting, inspection or evaluation of a property's condition
- Accepts all risks; offers coverage sight unseen

Many properties covered by Assurant have negative factors from an insurance standpoint: a history of multiple losses; aging, poor, or vacant condition; or risk for certain hazards based on location and other issues (e.g. hurricane-prone states, which make up more than half of Assurant's lender-placed inventory). As the level of risk increases, so do costs. As a result, Assurant's average lender-placed policy will cost from 1.5 to 2 times the cost of the prior insurance policy in place.

Assurant uses its scale and technology to manage expenses so that the costs of its policies are not vastly out-of-line with other policies. In fact, Assurant's rates are among the lowest in the lender-placed industry. Customers are always welcome to cancel their Assurant policy at any time and restore coverage through a different carrier simply by showing proof of insurance.

Amid America's housing crisis, consumers in some areas may wonder why insurance rates have not declined as property values have. This is because insurance rates are based on the cost of repairing or rebuilding the protected home, not the market value of that house or others in the area. A study by the Insurance Institute revealed that the cost to rebuild a home may not significantly decline even if the market values do. In fact, the study found that in recent years, labor, building and material costs were only 10% off their peak. Regulators want to ensure that homeowners suffering damages receive the actual resources necessary to rebuild their home. For this reason, when establishing a new policy in the event of a coverage lapse, Assurant factors in the coverage amount set by the homeowner's previous insurance carrier.

## Checks and balances

- **Regulations**

The lender-placed insurance industry operates in a carefully regulated environment. Assurant has opted to be what is known as a “filed and admitted” carrier in 49 of the 50 states. This means that the company voluntarily submits to the highest level of scrutiny and agrees to file its rates and forms for approval in each state.

Assurant is monitored by state insurance departments and complies with applicable laws and regulations in all 50 states, as well as federal statutes and regulations.

- **Transparency and ethic**

In addition to providing outsourced monitoring services that help mortgage servicers track their borrowers’ home insurance coverage, Assurant also furnishes lender-placed policies if such coverage becomes necessary. These two services are separate business models and operations, with several factors that distinguish the two groups, and eliminate any potential for conflicts of interest.

MONITORING SERVICES GROUP	INSURANCE GROUP
<ul style="list-style-type: none"> <li>• Focuses solely on monitoring activities and obtaining insurance coverage information; no “sales”</li> <li>• Uses highly developed technology and expertise in complicated aspects of property insurance</li> <li>• Can monitor for insurance gaps more effectively than lenders themselves</li> </ul>	<ul style="list-style-type: none"> <li>• Supplies policies for lenders on mortgaged properties</li> <li>• Acts in accordance with loan documents and applicable insurance laws</li> </ul>
<ul style="list-style-type: none"> <li>• No incentive to erroneously report or falsely place a policy; doing so creates unnecessary work and expense if customer cancels or doesn’t need coverage</li> </ul>	

- **Compensation**

Assurant also wants to ensure fair dealing when it comes to compensating those licensed agents who manage insurance programs and refer business to the company. Like other programs in the general property and casualty industry, Assurant follows the standard practice of paying commissions to licensed agents who generate policies. It is fair and reasonable to pay some form of compensation because financial institutions offering insurance programs also have expenses such as advancement of funds, billing and collection of premiums, and systems costs. Commissions are generally comparable to the general insurance market, and lenders disclose any such compensation to borrowers.

## Customer service focus

Mortgage servicers, through Assurant, extensively reach out to customers to inform them of what they need to do to avoid lender-placed insurance. Whether it's a letter, phone call, or locating the most recent carrier or agent, exhaustive steps are taken to accurately diagnose the situation and install the necessary safety net to protect homeowners and lenders alike. About 98 percent of the homes we monitor ultimately hold, renew or obtain new insurance of their choice; only about 2 percent proceed to lender-placed protection. There is no incentive to place policies in error, because it results in unnecessary work and the refunding of premiums. As a result, accuracy is key.

The company adheres to the highest levels of service and claims standards. Assurant field adjusters across the United States mobilize quickly to respond and settle claims fast. Assurant's claims organization also can look at coverage patterns during major disasters such as hurricanes, and start the claims process early. In some cases, work starts on claims even before a claim has been filed.

In the case of the 2011 Joplin tornado, Assurant immediately dispatched a special team following the disaster to assess damages on the scene, provide first-person observations to the Risk Assessment Center, and actively seek out Assurant-insured households that had suffered damage. The team went door to door to answer questions and provide information about filing claims. This level of responsiveness can be a huge help for homeowners after weathering an emotionally devastating event and losing a home.

## Summary

Lender-placed insurance is a service to homeowners, lenders, and investors alike. Customers always have the opportunity to carry insurance of their choice, but lender-placed insurance acts as a safety net when other insurance has lapsed. Assurant works every day to assist homeowners who were under lender-placed policies when misfortune struck. Without this coverage, homes and collateral are lost – a serious consequence not only for the individual, but also for America's banking system.

### About Assurant Specialty Property

Assurant Specialty Property is the nation's leader in lender-placed insurance, serving clients and their customers in all 50 states and the District of Columbia.

Assurant Specialty Property is part of Assurant, a premier provider of specialized insurance products and related services in North America and selected other markets, with more than a century of industry experience. Assurant is traded on the New York Stock Exchange under the symbol AIZ.