GAO Highlights

Highlights of GAO-15-631, a report to the Ranking Member, Subcommittee on Financial Institutions and Consumer Protection, Committee on Banking, Housing, and Urban Affairs, U.S. Senate

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LENDER-PLACED INSURANCE

More Robust Data Could Improve Oversight

Why GAO Did This Study

Mortgage servicers use LPI to protect the collateral on mortgages when borrower-purchased homeowners or flood insurance coverage lapses. The 2007-2009 financial crisis resulted in an increased prevalence of LPI. Because LPI premiums are generally higher than those for borrower-purchased coverage, state insurance regulators and consumer groups have raised concerns about costs to consumers.

This report addresses (1) the extent to which LPI is used; (2) stakeholder views on the cost of LPI; and (3) state and federal oversight of LPI. GAO examined documentation, studies, and laws and regulations related to LPI, and interviewed stakeholders including state insurance and federal financial regulators, consumer advocates, insurers, servicers, and industry associations. GAO selected interviewees based on their involvement in the LPI market and other factors to obtain a diverse range of perspectives. GAO selected the seven state insurance regulators to interview based on a number of factors including LPI premium volume and involvement in the LPI market.

What GAO Recommends

GAO recommends that NAIC work with state insurance regulators to collect sufficient, reliable data to oversee the LPI market. This includes working with state insurance regulators to develop and implement more robust policies and procedures for LPI data collected annually from insurers and to complete efforts to obtain more detailed national data from insurers. NAIC said it would consider the recommendations as part of its ongoing work in the area.

View GAO-15-631. For more information, contact Alicia Puente Cackley at (202) 512-8678 or cackleya@gao.gov.

What GAO Found

Mortgage servicers purchase lender-placed insurance (LPI) for mortgages whose borrower-purchased insurance coverage lapses, most often because of nonpayment by the borrower or cancellation or nonrenewal by the original insurer. The limited information available indicates that LPI generally affects 1 percent to 2 percent of all mortgaged properties annually and has become less prevalent since the 2007-2009 financial crisis as foreclosures have declined. Although used more often when borrowers without escrow accounts (about 25 percent to 40 percent of borrowers) stop paying their insurance premiums, servicers also use LPI when an insurer declines to renew a policy. LPI insurers often provide services such as tracking properties to help servicers identify those without insurance and confirming coverage. LPI insurers said they must refund premiums if a borrower provides evidence of coverage, which occurs on about 10 percent of policies. The Federal Emergency Management Agency offers flood LPI, but industry officials said most servicers prefer private coverage because of more comprehensive coverage and lower rates, among other things.

LPI premium rates are higher than rates for borrower-purchased insurance, and stakeholders disagreed about whether the difference is justified. Insurers pointed out that they provide coverage for any property in a servicer's portfolio without a rigorous underwriting process, and the limited information requires higher rates. They added that LPI properties tended to have higher risk characteristics, such as higher-risk locations (along the coast) and higher vacancy rates because of foreclosures. But some consumer advocates and state regulators said that the factors that insurers cite for higher rates, as well as the insurers' limited loss histories, do not justify the magnitude of the premium differences. They also said borrowers have little influence over the price of LPI and that some insurers competed for the servicers' business by providing commissions to the servicer that passed the costs on to the borrower through higher premium rates. Insurers, however, said that LPI premium rates were filed with and approved by state regulators and that commissions were a standard industry practice, but their use had decreased.

State insurance regulators have primary responsibility for overseeing LPI insurers, but federal financial regulators generally oversee the servicers that purchase LPI coverage for their portfolios. However, a lack of comprehensive data at the state and national levels limits effective oversight of the LPI industry. For example, regulators lack reliable data that would allow them to evaluate the cost of LPI or the appropriateness of its use. The National Association of Insurance Commissioners (NAIC), which helps coordinate state insurance regulation, requires insurers to annually submit state-level LPI data, but the data were incomplete and unreliable. NAIC provides guidance for the reporting of these data and shares responsibility with state regulators for reviewing and analyzing the data, but neither has developed policies and procedures sufficient for ensuring their reliability. State and federal regulators have coordinated to collect more detailed national data to better understand the LPI industry, but insurers failed to provide them all of the requested information, and whether and when they will is unknown. Without more comprehensive and reliable data, state and federal regulators lack an important tool to fully evaluate LPI premium rates and industry practices and ensure that consumers are adequately protected.