


NAIC

August 9, 2012

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LPI: Purpose

- Mortgage contract (and NFIA as to Flood) requires coverage at all times.
- LPI provides dwelling coverage when the borrower does not maintain required insurance.
- Typically issued under a master policy – mortgage company is named insured; borrower additional insured or certificate holder.
- Coverage is limited to the dwelling and other structures. Contents and liability risks are not covered automatically.
- Coverage is not individually underwritten – guaranteed insurance for all uninsured properties, regardless of insurable condition, vacancy, etc.

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LPI: Tracking and Placement Process

- Most lenders engage third parties to monitor insurance for the portfolio, due to:
 - Economies of scale
 - Technology required
 - Expertise in insurance matters
- Monitoring: notices to borrowers on exposed properties, customer service calls, coverage placement
- Typically, three or more notices – at expiration/cancellation of coverage, 30 days thereafter and 60 days after 2nd notice:
 - 1st letter (at exposure) – 7.5% of portfolio
 - 2nd letter (30 days later) – 4.2% of portfolio
 - 3rd letter (and coverage document – 30 days later) – 2.7% of portfolio
 - Of the 2.7%, approximately 10% cancel flat, as insurance confirmations are received.

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Borrower Disclosures

- Letters disclose:
 - Insurance requirement in the mortgage contract
 - Records show property is uninsured
 - How to comply with insurance requirement – contact information for lender/service provider
 - Encouragement to call insurance agent
 - LPI will be purchased if evidence of insurance not received
 - LPI is more expensive than homeowners and covers only the dwelling
 - Servicer affiliate will receive a commission (if applicable)
- Additional information – agency name and number to contact for a dwelling or homeowner underwritten policy quote (QBE FIRST).
- Pre-expiration phone calls to borrower's agent or insurer to confirm payment and coverage.

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Federal Developments

- CFPB (created by Dodd-Frank) – to issue proposed rules and regulations concerning LPI aspects of mortgage servicing. Expected August 2012, effective January 2013.
 - Borrower letters and disclosures
 - Refund timelines
 - Premium disbursement rules

- FNMA Service Guidelines
 - Issued March 2012
 - Put on indefinite “hold” May 2012, but servicers instructed to implement as soon as practicable.

- National Flood Insurance Act
 - Renewed, with some changes to September 2017.

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LPI: Questions

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| <ul style="list-style-type: none"> • Coverage Placement <ul style="list-style-type: none"> – Duplicate coverage – “Retroactive” placement
 • Borrower Communications <ul style="list-style-type: none"> – Letter content | <ul style="list-style-type: none"> • Broker Compensation – Affiliates and Non-Affiliates <ul style="list-style-type: none"> – Commissions – Expense Reimbursements
 • Rates and Rating <ul style="list-style-type: none"> – Expenses – Is this a catastrophe book? |
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LPI: Coverage Placement

- Coverage amount – typically replacement cost. Some discussion (FNMA Servicer G/L of March 2012) of requiring unpaid balance if loan is delinquent.
- Duplicate coverage – occurs when information is incomplete. LPI designed to cover only uninsured or underinsured risks.
- Retroactive coverage – occurs when exposure is discovered after the fact. Losses are paid whenever the property is uninsured, whether or not insurer is aware of exposure.

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LPI: Borrower Communications

- Servicer letter – provides all information the consumer needs to fulfill insurance requirement.
- Letter content – designed to answer relevant questions and provide additional information.
- We look forward to working with CFPB and other state and federal agencies to ensure communications are prompt, thorough and informative.

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LPI: Broker Compensation

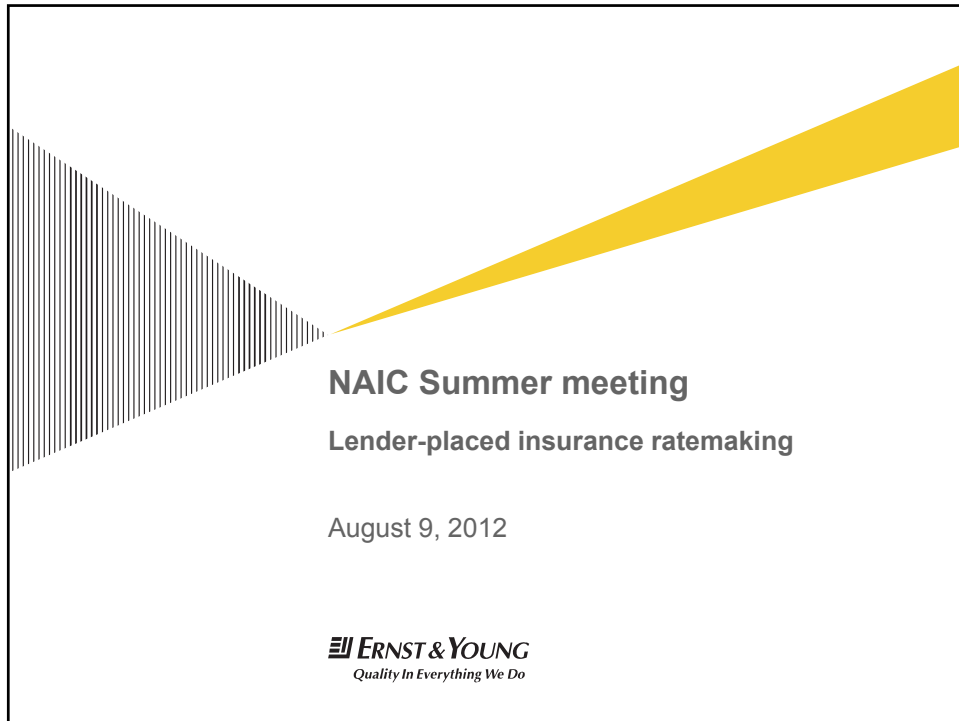
- Broker represents mortgage company, whether or not affiliated with the mortgage company.
- Affiliated and non-affiliated brokers provide similar services, in some cases, the affiliated broker is more active.
- Lender-affiliated brokerage or agency commissions expressly allowed by NAIC Model Act, so long as reasonable (see NAIC Model Act, §12.D(2), excerpted in the Appendix)

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LPI: Rates and Rating

- QBE writes on an admitted basis in 47 states.
- Surplus Lines in Florida, Louisiana and Texas – admitted filings pending
- Surplus lines for some or all states or coverages not atypical.
- Expenses in filing are consistent with general insurance practice.
 - NAIC Model Act (see Appendix):
 - Tracking fees and acquisition expenses – see § 8.E., Alt. 1, §12.D(2)
 - Commissions to Broker, including lender affiliates are also acquisition expenses see §12.D(2)
- Absence of catastrophic loss activity contributes to lower than expected losses.

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NAIC Summer meeting
Lender-placed insurance ratemaking

August 9, 2012

ERNST & YOUNG
Quality In Everything We Do

Agenda

- Introduction
- Actuarial discussion topics
 - QBE rate modification process
 - Loss history and rate of return
 - Catastrophe exposure concentration (2007 to 2011)

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Discussion Topics

QBE rate modification process

- We have reviewed the Company's rate modification process by:
 - Reading the Rate Modification Workbook documentation
 - Discussing the process with Management

- Based on our review, we found the process to be consistent with the following Actuarial Standards of Practice ("ASOP") as promulgated by the American Academy of Actuaries ("AAA")
 - ASOP #30: Expense provision in rates
 - ASOP #31: Profit and contingencies
 - ASOP #39: Catastrophe losses

Discussion Topics

Loss history and rate of return

- We have reviewed the QBE Specialty's historical experience in the states of Florida, Texas, and Louisiana. Based on their claims experience, reinsurance costs, and underwriting expenses, we have calculated the historical pre-tax return-to-surplus ratio for years 2000 to 2010, and have found this amount to be within reasonable industry expectations.

Discussion Topics Catastrophe exposure concentration (2007-2011)

- Reviewed progression of QBE First/Balboa catastrophe exposure over the last 5 years
- Policy count and Insurance in Force (“IIF”) in hurricane-prone areas increasing at much higher pace than in other areas

Policy Count Distribution - % of total by area

Coverage Period	Florida & Louisiana	Florida Texas	All States Distance to Coast < 0.5 mi	All States Distance to Coast < 2 mi
2007	13.6%	25.7%	2.5%	6.5%
2011	21.5%	30.5%	4.3%	10.6%

- Metrics used: Florida Only, FL/TX/LA, DTC <0.5 mile, DTC < 2 mi
- Same trends
- Company now much more exposed to wind peril than in 2004, 2005 or 2008, the most recent years where industry faced significant hurricane losses

APPENDIX

Creditor-Placed Insurance Model Act (Model 375)

NAIC - Model Laws

Insurance Monitoring Expenses

Model 375 s 8

Filing, Approval and Withdrawal of Forms and Rates

E. Alternative 1:

The schedules of premium rates shall not be excessive, inadequate or unfairly discriminatory. In determining whether a schedule of premium rates are excessive, inadequate or unfairly discriminatory, the commissioner shall take into account past and prospective loss experience, general and administrative expenses, loss settlement and adjustment expenses, *reasonable creditor compensation and other acquisition costs including insurance tracking costs*, reserves, taxes, licenses, fees and assessments, reasonable insurer profit and other relevant data. Rates are not unfairly discriminatory because different premiums result for different policyholders, including group policyholders, with similar loss exposures but different expense factors or similar expense factors but different loss exposures, nor are rates unfairly discriminatory if they are averaged broadly among all persons insured in this state or all persons insured under a group insurance policy. (Emphasis Supplied.)

Producer/Broker Commission

Model 375 s 12

Remittance of Premiums and Payment of Compensation

D. Prohibited rebates or inducements do not include:

- 1) The *providing of insurance tracking and other services incidental to the creditor-placed insurance program*;
- 2) The *paying of commissions and other compensation to a duly licensed and appointed insurance producer, whether or not affiliated with the creditor*;
- 3) The *paying to the creditor policyholder of group experience rated refunds or policy dividends*; and
- 4) The *paying to the creditor of amounts intended to reimburse the creditor for its expenses incurred incidental to the creditor-placed insurance program* (such as costs of data processing, mail processing, telephone service, insurance tracking, billing, collections and related activities); provided that these payments are approved in a manner consistent with the procedures in Section 8 and are calculated in a manner that does not exceed an amount reasonably estimated to equal the expenses incurred by the creditor. (Emphasis Supplied.)