October 15, 2009

The Honorable Barney Frank
Chairman, Financial Services Committee
United States House of Representatives
Washington, DC 20515

The Honorable Spencer Bachus
Ranking Member, Financial Services Committee
United States House of Representatives
Washington, DC 20515

Re: Urge Opposition to Moore Amendment to Strip Credit Insurance Authority from CFPA

Dear Chairman Frank, Ranking Member Bachus and Committee Members:

The undersigned national consumer organizations[1] write to urge you to strongly oppose an amendment to be offered by Representative Gwen Moore to remove regulatory authority of the proposed Consumer Financial Protection Agency (CFPA) for credit-related insurance products: credit insurance[2], title insurance and mortgage guaranty insurance.

The Moore amendment is a "green light" to lenders to continue to use credit insurance as a primary tool for predatory lending and equity skimming in the refinance mortgage market, auto financing, and personal loans. Moreover, we conservatively estimate that Americans have been overcharged by at least $17.5 billion since 2004 for credit insurance alone.

The goal behind Chairman Frank's legislation to create a single agency responsible for consumer protection of financial products is to ensure an institutional focus on consumer protection and stop the regulatory arbitrage that has prevented existing agencies from effectively protecting

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1 The undersigned groups have broad expertise on the impact of credit based insurance on consumers. For example, the Consumer Federation of America and Center for Economic Justice have issued several reports over the last 20 years describing the poor regulatory oversight of credit insurance. Mr. Birnbaum is a nationally-known expert on title insurance. Both Mr. Hunter and Mr. Birnbaum have served as insurance regulators as well as consumer advocates on insurance, testifying in the states and before the NAIC on credit-related insurance issues.

2 Credit insurance includes credit life, credit disability, credit involuntary unemployment, credit personal property, credit family leave, credit GAP, credit nonfiling and creditor-placed (force-placed) insurance.

insurance consumers. Credit-related insurance products are precisely the type of products for which the CFPA is needed to protect consumers.

- Providing the CFPA with authority to set minimum standards that cannot be skirted is appropriate because credit-related insurance products are already subject to both state and federal regulatory requirements. The sale of credit insurance is typically inseparable from the sale or servicing of a credit product. In fact, credit insurance is often "packed" into a loan product and not chosen voluntarily by consumers;
- Lenders often use "regulatory arbitrage" to seek out the weakest regulator of credit-related insurance products at the federal or state level;
- Credit-related insurance product markets are characterized by reverse competition – competition which drives up prices to consumers – which requires strong regulatory oversight to protect consumers;
- Credit insurance has historically been a primary tool for predatory lending and equity skimming in the refinance mortgage market, auto financing, and personal loans, and they remain so;
- State and federal regulators have done a very poor job of protecting consumers of credit-related insurance products and their banking counterparts' debt cancellation contracts and debt suspension agreements. We conservatively estimate that Americans have been overcharged by at least $17.5 billion since 2004 for credit insurance alone.
- Regulatory oversight of credit-related insurance products is biased towards insurers, lenders, and auto dealers because consumers have no institutionalized advocate to counter the lobbying of those who benefit from excessive prices.

Credit-related insurance products are already subject to both state and federal regulatory requirements. Credit-related insurance is primarily regulated at the state level. State insurance regulators approve the credit insurance products and rates – but do a very poor job of protecting consumers, as explained below. State regulators also regulate title and mortgage guaranty insurers. At the federal level, credit insurance sales are restricted by the Truth in Lending Act (TILA) which has requirements for disclosures and the Home Ownership and Equity Protection Act (HOEPA). The Department of Housing and Urban Development's (HUD) recent revision to mortgage disclosure forms – the good faith estimate (GFE) and HUD 1 – include credit-related insurance products. The Real Estate Settlement Procedures Act (RESPA) regulates key aspects of title insurance and mortgage guaranty insurance. The federal banking regulators (Office of Comptroller of Currency, Office of Thrift Supervision, and National Credit Union Administration) regulate the credit insurance substitutes called debt cancellation contracts (DCC) and debt suspension agreements (DSA).

Differing federal and state standards for credit-related insurance result in regulatory arbitrage, where lenders seek out the most favorable regulator to maximize lender profits at the expense of consumers.

Credit insurance and DCC/DSA – so-called "payment protection" products – provide textbook examples of regulatory arbitrage. DCC and DSA are substitutes for credit insurance, as both sets of products are identical in appearance and function to consumers. But federal banking regulators have declared DCC/DSA to be banking products and, therefore, not subject to state insurance regulation. Because federal banking regulators have very lax regulatory oversight of DCC/DSA, lenders migrated from the credit insurance (for which states have done a poor job protecting consumers) to DCC/DSA (for which federal regulators have done an even worse job).

Just as lenders migrated to the more favorable federal regulator when DCC/DSA effectively became an unregulated alternative to credit insurance, so will lenders migrate back to credit insurance if the CFPA provides meaningful consumer protection for the DCC/DSA banking product. The regulatory arbitrage of state-regulated credit insurance and federally-regulated DCC/DSA is precisely the type of regulatory failure the CFPA is being created to fix.

Credit-related insurance markets are characterized by reverse competition and, consequently, require strong regulatory oversight to protect consumers. Reverse competition refers to a market structure in which the insurer does not sell directly to the borrower, but sells a group insurance policy to a lender who, in turn, sells the insurance to individual borrowers. Because the insurers require the lender to sell the insurance product, the insurers market their products to lenders and not to consumers. The competition among insurers to get the lender to purchase the credit-related insurance is based on providing more compensation to the lender: bidding up the price of the insurance product to include more commission and compensation for the lender. Reverse competition means a market in which the competition drives up the price to individual consumers.

While state insurance regulators recognize the problem of reverse competition,[3] the majority of states fail to protect consumers of credit-related insurance. The attached tables show the loss ratios for various types of credit insurance. The loss ratio is the ratio of claims paid by the insurer on behalf of the borrower divided by premiums collected by the insurer. It should be pointed out that the lender is the primary beneficiary of credit insurance because the insurance protects the lender's loan and eliminates the lender's need for collection activities from heirs or disabled or unemployed workers. Yet, the low loss ratios indicate that lenders not only benefit from the loan protection, but receive significant compensation, often in amounts greater than those paid out as benefits for the consumer. Consumer groups, and even the National Association of Insurance Commissioners, have called for credit insurance to provide benefits that are reasonable in relation to premiums collected and have set a minimum 60 percent loss ratio as that standard.

As tables 1 through 9 show,[4] consumers have been overcharged by billions of dollar a year as the overall nationwide credit insurance loss ratios and credit insurance loss ratios in most states are well below 60 percent.

Table 1 shows that nationwide credit insurance loss ratios have hovered in the low 40's for the past ten years. Table 1 shows the states with the lowest loss ratios, the highest loss ratios and the most

[3] For example, the New York State Department of Insurance credit insurance regulation 27A describes the problem in Section 185.0:
(b) In the marketing of credit insurance, the inferior bargaining position of the debtor creates a captive market in which, without appropriate regulation of such insurance, the creditor can dictate the choice of coverages, premium rates, insurer, agent and broker, with such undesirable consequences as: excessive coverage (both as to amount and duration); excessive charges (including payment for nonessential items concealed as unidentifiable extra charges under the heading of insurance); failure to inform debtors of the existence and character of their credit insurance and the charges therefore, and consequent avoidance of the protection provided the debtor by such coverage.
(c) In the absence of regulation, premium rates and compensation for credit insurance tend to be set at levels determined by the rate of return desired by the creditor in the form of dividends or retrospective rate refunds, commissions, fees, or other allowances, instead of on the basis of reasonable cost. Such reverse competition, unless properly controlled, results in insurance charges to debtors that are unreasonably high in relation to the benefits provided to them.
[4] Tables 1 though 9 are compiled from data reported by credit insurers in the Credit Insurance Experience Exhibit of the Statutory Annual Statement filed annually with state insurance regulators. The data was obtained from the National Association of Insurance Commissioners, which is not responsible for the analysis.

premium written. Several states with large amounts of credit life premium show five-year loss ratios lower than 30 percent.

Table 2 shows the credit life loss ratios for individual insurers for the five-year period 2004-2008. The table shows loss ratios ranging from 23.2 to 55.6 percent. The very low loss ratios for most insurers show that state insurance regulators have not enforced state laws requiring that benefits be reasonable in relation to premium.

Tables 3 and 4 include loss ratios for states and companies for credit disability and show that states have done a worse job with credit disability than credit life. Nationwide, loss ratios have dropped by an average of more than 10 percent over the past ten years, meaning billions more in unwarranted compensation to lenders. Loss ratios for many states and companies are in the 20's, demonstrating that regulators have allowed very excessive rates.

Tables 5 and 6 include loss ratios for states and companies for credit involuntary unemployment. The nationwide average loss ratio for ten years has been 10.9 percent: the overcharges for credit unemployment have been unconscionable.

Table 7 shows the combined credit life, credit disability and credit unemployment results for all states for the 2004-2008 period. **The nationwide loss ratio of less than 38 percent means consumers were overcharged $7.5 billion compared to the minimum consumer protection standard of a 60 percent loss ratio for just three lines of credit insurance.** The table also shows that some states were able to do a good job regulating credit insurance – Maine, Vermont and New York stand out – but the vast majority of states fail to protect consumers.

Table 8 includes the nationwide premiums and loss ratios for credit family leave insurance. The chart shows that state regulators have essentially allowed the sale of a bogus product. Insurers have collected almost $150,000,000 in premium and paid out less than $300,000 in claims, a loss ratio of 0.2 percent. The Center for Economic Justice alerted regulators to the credit family leave problem in 2005, but regulators continued to allow this "product" to be sold.

Table 9 shows the explosion in amounts of force-placed insurance. Force-placed or creditor-placed insurance is insurance forced on the consumer by the lender – and paid for by the consumer – when the consumer fails to maintain the required insurance for the auto or mortgage loan. Consumers forced to pay for force-placed insurance are among the most vulnerable of consumers as they have no say in the purchase of insurance. Here, again, state regulators have failed to protect vulnerable consumers, as demonstrated by creditor-placed home owners' loss ratios in the low 20's in 2007 and 2008, as the amount of this insurance almost tripled from just a few years earlier. **The overcharges for creditor-placed insurance since 2004 was another $10 billion, bringing the total credit insurance overcharges to over $17.5 billion.**

The low loss ratios for credit insurance do not describe the entire failure of state insurance regulators to protect credit insurance consumers. State regulators did not, and to this day still have not, taken any action to stop the abuses of financed single premium credit insurance. These products are not only overpriced, but are part of predatory lending practices in which insurance is packed into the loan and consumers are robbed of their equity.

As poor a job as state insurance regulators do protecting consumers of credit-related insurance, federal regulators have done an even worse job protecting consumers of DCC/DSA. DCC/DSA products typically have fewer benefits and cost much more than credit insurance with loss ratios estimated to be in the single digits.[5]

Title insurance loss ratios are also truly dismal. Over the 20 years prior to 2007, title insurance paid out benefits averaging 6.1 percent of premium. Over the decade prior to 2007, the number dropped to 4.9 percent.[6] In 2008, the loss ratio "jumped" to 11.7 percent.[7]

State and federal regulators' failure to protect consumers of credit-related insurance products is a result of the fragmented regulatory structure which encourages regulatory arbitrage by lenders and insurers. But the failure of regulators to protect consumers is also a result of the lobbying power of the insurers, lenders and auto dealers who benefit mightily from weak consumer protection. While insurers can use policyholder-supplied funds to lobby regulators, consumers of credit-related insurance products have no institutionalized advocate. Just as business interests hold disproportionate influence in state legislatures and Congress, so do the same business interest with state and federal regulatory agencies. The CFPA is essential to start leveling the playing field. There is no area where consumers need the help of the CFPA more than credit-related insurance products.

We strongly urge you to oppose this amendment that will be very damaging to credit and insurance consumers. For more information, please contact Travis Plunkett at the Consumer Federation of America at 202-387-6121.

Sincerely,

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Director of Insurance
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Birny Birnbaum
Executive Director
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5 Center for Economic Justice, "The Impact of Debt Cancellation Contracts on State Insurance Regulation,"July 2003. See pages 26-29. Available at www.cej-online.org/dccdsamainpage.htm.

6 Source: "U.S. Title – 2007 Market Review, A. M. Best Special Report," October 13, 2008, Page 4.

7 Missouri Department of Insurance, Financial Institutions and Professional Regulation, at http://www.insurance.mo.gov/reports/lossratio