NAIC
National Association of Insurance Commissioners
Consumer ALERT

Protecting An Investment:
What Consumers Need to Know About Lender-Placed Insurance

Today, consumers use credit to purchase almost everything from appliances to cars. For smaller purchases, like a new TV or washing machine, most credit lenders do not insist that a consumer buy insurance coverage. But for major purchases like a new home or car, however, the lender expects the consumer to insure the property against losses. Many consumers do not realize if they fail to purchase the necessary insurance, the lender can buy a policy on their behalf and charge the consumer. This type of coverage is referred to as lender-placed insurance. The National Association of Insurance Commissioners (NAIC) recently began reviewing lender-placed insurance as the practice has became more common in this weakened economy. The NAIC offers this information to help consumers understand these practices and offers tips to avoid having insurance placed on their property.

What is Lender-Placed Insurance?

Lender-placed insurance is a group policy where an insurer issues certificates of insurance to a bank or mortgage servicer when the consumer's own insurance policy may have lapsed or if the lender deems the consumers' insurance to be insufficient.

When a loan agreement is made with a bank or a lender, generally the lending document includes a stipulation requiring property insurance, often referred to as hazard insurance, on the property. The contract will spell out specifically what must be covered and how proof of coverage is to be submitted to the lender or the company servicing the loan. This is why, when insurance is purchased for a home or car, the insurance agent asks if there is a lienholder and the lender's name appears on a declarations page. If a consumer cannot provide proof of coverage, a lender can ask the insured to place insurance on the property in accordance with the terms of the lending contract.

Consumers may not realize, but a mortgage for a home located in a National Flood Insurance Program Special Flood Hazard Area will require flood insurance. If this is a requirement of the mortgage contract and it is not purchased, the lender can purchase the coverage and require the consumer to pay for it.

Why is it Important to Understand Lender-Placed Insurance?

Lender-placed insurance premiums are higher than the property insurance a borrower can purchase on their own and consumers are billed by the lender for the cost of a lender-placed policy.

A lender will try to verify coverage before it acts to insure a collateral property and it will also notify the consumer of the action to insure the property. Be aware the standard mortgage loan contract allows a lender to secure property insurance back to the date they last show it was covered by the consumer's personal policy. This could result in a large bill for a more expensive insurance policy.

In addition to being more expensive, the lender-placed insurance policy also has limited coverage. For example, these policies generally do not cover personal items or owner liability. If a borrower does not pay the lender-placed insurance policy premium, they could be at risk of foreclose.

Why Are Regulators Reviewing this Type of Business?

"Reverse competition" is the key regulatory concern, because the consumer is forced to pay the premium on a policy selected by the lender. Under this practice the lender is not motivated to select the lowest price for coverages driving up prices for consumers. The NAIC, as well as regulators in Florida, California, New York and Texas, recently held public hearings to learn more about these products and practices.

What Can Consumers Do To Avoid Lender-Placed Insurance?

Consumers fail to maintain the required coverage for a variety of reasons — cancellation, a lapse in coverage or even just a simple oversight. Paying insurance premiums on time and reviewing the paperwork received from the insurance company and the lender is the most important protection from lender-placed insurance.

In the case of a mortgage, the premium for lender-placed insurance can be taken directly from an escrow account. Any change in payment should be an alert to a possible insurance-related issue.

Many lenders use third-party companies to process payments and insurance information. If paperwork is not processed in a timely manner, or if verification of coverage is mistakenly sent to the wrong address, the lender may not realize the property is adequately covered and secure lender-placed coverage. It is important to check lender information on a policy's declarations page, and carefully review all statements received from the lender.

If changing insurance companies, it is important that there is no interruption between policies. It is also a good idea to notify the lender of any change and provide proof of coverage directly, instead of waiting for a copy to be mailed from the new insurance company.

Contact the Kentucky Department of Insurance with any questions about the use of lender-placed insurance.

Consumers looking for a way to control insurance costs can get smart about their insurance coverages. The NAIC Insure U education program has more about the choices available when it comes to coverage and how to evaluate their needs to find ways to save money on their premiums.

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About the NAIC

The National Association of Insurance Commissioners (NAIC) is the U.S. standard-setting and regulatory support organization created and governed by the chief insurance regulators from the 50 states, the District of Columbia and five U.S. territories. Through the NAIC, state insurance regulators establish standards and best practices, conduct peer review, and coordinate their regulatory oversight. NAIC staff supports these efforts and represents the collective views of state regulators domestically and internationally. NAIC members, together with the central resources of the NAIC, form the national system of state-based insurance regulation in the U.S. For consumer information, visit insureUonline.org.