

Office of Inspector General (OIG) Urges Federal Housing Finance Agency (FHFA) To Sue Over Force-Placed Insurance

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The Office of Inspector General (“OIG”) for the Federal Housing Finance Agency (“FHFA”) is *urging the FHFA to sue* its servicers and lender-placed insurance (“LPI”) providers because Fannie Mae and Freddie Mac have suffered considerable financial harm in the LPI market, possibly as much as \$158 million in 2012 alone from excessively priced insurance coverage. FHFA has been conservator of the two government sponsored entities (“GSEs”) since August 2008.

LPI, commonly called “force-placed” insurance, exists because the GSEs require their borrowers to maintain hazard insurance for their homes, thereby protecting the GSEs’ interests in those properties. LPI is ordered by the servicer when it identifies a lapse in the hazard insurance a borrower is required to carry on a mortgaged property. Apparently, the GSEs are in this predicament by paying its servicers the allegedly excessive premiums when borrowers refused to pay the GSEs.

In the *report* released by the FHFA OIG June 25, 2014, two companies and their subsidiaries are identified as providing 90% of the nation’s LPI coverage, *Assurant* and *QBE Holdings*. The FHFA report claims that several state financial regulators, including in the large population states of New York, California and Florida, found that the LPI rates in their states were excessive. According to the report, the excessive costs were driven up by “profit-sharing arrangements under which servicers were paid to steer business to LPI providers. Such arrangements often took the form of commission structures and reinsurance deals.”

Last November, *FHFA directed the GSEs* to prohibit their servicers from receiving such LPI-related commissions or entering into reinsurance arrangements with providers, and both *Fannie Mae & Freddie Mac* subsequently issued new servicing guidelines that took effect on June 1, 2014. In addition, in 2012 and 2013, New York, California and Florida, which together accounted for 48% of earned LPI premiums nationwide in 2012, accused Assurant and QBE of charging excessive LPI rates and began to enter into consent orders to settle the claims. In 2013, the two companies agreed to pay \$24 million to New York and provide restitution to the affected borrowers. In Florida and California, the companies were forced to lower their rates after the states found that the LPI rates did not comply with state law. Moreover, mortgage borrowers have also begun filing class-action lawsuits against their servicers and LPI providers over excessive rates, resulting in out of court settlements

totaling at least \$674 million to date.

These developments may go a long way toward resolving the issue of excessive LPI rates going forward, but the OIG recommended that the FHFA assess the merits of litigation by the GSEs against their servicers and LPI providers to remedy potential damages caused by past abuses in the LPI market and take appropriate action in this regard. The OIG's report noted that the FHFA's general counsel has not yet considered lawsuits over the LPI rates: "An official from that office said that it had not yet done so, citing competing priorities, such as finalizing pending legal claims. The official said, however, that FHFA's Office of General Counsel would consider undertaking such an assessment." The OIG stated that it believes that "FHFA—as the Enterprises' conservator—has a responsibility to conduct such an assessment because the failure to do so could result in potentially forgoing significant financial recoveries."

FHFA accepted OIG's recommendation and will complete its litigation assessment within 12 months.

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National Law Review, Volume IV, Number 182

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