COMMISSIONER OF FINANCIAL REGULATION

LICENSEE ADVISORY

October 25, 2017

REGULATORY ALERT

PROPERTY INSURANCE COVERAGE LIMITS UNDER MARYLAND LAW

Background

Maryland law imposes limits on the amount of property insurance coverage that a mortgage lender or servicer may require a borrower to provide or purchase as a condition of receiving or maintaining a loan secured by a first mortgage or deed of trust. *See* Md. Code Ann., Commercial Law (CL) Article, § 12-124 (full text here). The Maryland General Assembly codified the limitation on property insurance coverage amount to prevent mortgage lenders from compelling borrowers to purchase property insurance in excess of the amount necessary to protect a creditor's interest in the collateral. In addition, insurers and insurance producers are reminded that it is a violation of Maryland insurance law to knowingly participate in writing or issuing substantial over-insurance of property risks. *See* Md. Code Ann., Insurance Article, §§ 10-126(a)(9) and 27-216.

Property Insurance Coverage Amount May Not Exceed Replacement Cost

Mortgage lenders and servicers may not require a borrower to provide or purchase property insurance coverage that exceeds the property's replacement cost, defined as the amount needed to repair damage to or rebuild improvements on real property to restore the improvements to their pre-loss condition. *See* CL § 12-124(a)(2). In determining the replacement cost of improvements, the mortgage lender may either accept the value placed on the improvements by the insurer, or use the value placed on the improvements by the lender's appraisal of the improvements. *See* CL § 12-124(a)(4). A violation of Commercial Law section 12-124 entitles a borrower to seek an injunction and obtain attorney's fees and damages directly resulting from the violation. *See* CL § 12-124(b).

Use of Unpaid Principal Balance to Determine Coverage Amount Not Permitted

Staff from the Office of the Commissioner of Financial Regulation (OCFR) has encountered situations where mortgage lenders and servicers that are licensed under the Maryland Mortgage Lender Law (MMLL) are utilizing unpaid principal balance (UPB) to determine the amount of property insurance coverage. **This practice is not permitted under Maryland law**. MMLL licensees should ensure that UPB is not being used to determine property insurance coverage amounts in lieu of an insurer's valuation of the improvements or an appraisal. Licensees that utilize UPB to determine the amount of property insurance coverage could be subject to enforcement actions from the OCFR as well as from state and federal authorities including the Consumer Protection Division of the Maryland Attorney General's Office and the Consumer Financial Protection Bureau. If the OCFR discovers that UPB is or has been used as the basis for determining property insurance coverage amounts, the OCFR can order the licensee to come into compliance with Maryland law and provide an adequate remedy to all impacted consumers in situations where the UPB exceeds the replacement cost of the property. Licensees will also be subject to such further disciplinary action as the OCFR deems appropriate.

Use of Last-Known Coverage Amount to Determine Value of Improvements

The OCFR has encountered situations where a MMLL licensee has relied on its insurance vendor to determine the amount of lender placed insurance (LPI) coverage, and the insurance vendor has utilized last-known coverage amount (LKCA) to determine the value of improvements and the amount of LPI coverage. The statute allows a lender or servicer to accept the value placed on the improvements by the insurer, but does not specify how an insurer shall place value on the improvements. For that reason, the OCFR will permit MMLL licensees, through a provider of LPI insurance, to use LKCA as the basis for determining the value of improvements and the amount of LPI coverage. However, if LKCA is not known, MMLL licensees are not permitted to utilize UPB to determine LPI coverage. Instead, if LKCA is not known, LPI providers may utilize a commercially available reconstruction cost estimator to determine the value of improvements and the amount of LPI coverage.

Compliance Reviews

OCFR monitors MMLL licensee compliance with the applicable sections imposing property insurance coverage limits. In particular, OCFR's examiners review licensees' policies and procedures for determining property insurance coverage limits and conduct loan-level reviews of property insurance coverage amounts to ensure that the policies and conduct of MMLL licensees are in compliance with Maryland law. In order to facilitate OCFR's loan-level review, MMLL licensees should retain and make available all document(s) that set forth the value placed on the improvements by the lender, servicer, or insurer.

For more information, please contact the Non-Depository Supervision Unit at: mortgage.examination@maryland.gov.

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