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Essent Announces Limited Rescission Waiver Program for Delegated Mortgage Underwriting

Essent Guaranty has enhanced its master policy for private mortgage insurance with language designed to reduce exposure to mortgage insurance claims arising from misrepresentations, underwriting errors and missing loan documents.

The enhancement, Clarity of Coverage, is an endorsement to the company's new master policy that applies to all home loans insured by the company. Essent entered the MI market in 2010 but has so far declined to report how much business it has done.

The Clarity of Coverage endorsement is a written commitment to lenders and policy beneficiaries that claims will be handled in a transparent, predictable and fair manner, the company said. It aims to assure lenders that claims investigations will be fair and not immediately result in rescission.

Essent executives clarified that the endorsement is not a guarantee against loan repurchases or MI cancellation risk. "It is all about restoring lender confidence that legitimate MI claims will be honored and treated fairly, which ought to greatly minimize the number of rescissions, especially when you combine [such assurances] with the good-quality loans originated in today's market," said Adolfo Marzol, vice chairman of Essent.

Recent irregularities in foreclosure documents submitted to courts in various cases have led to the suspension of foreclosure proceedings, causing delays in foreclosures in judicial foreclosure states. Mortgage insurance contracts typically allow the MI to curtail claim payments when there are foreclosure delays.

Private MIs' high levels of rescinded policies and claim denials in the past few years have led to an increased risk of litigation, according to a new study by Standard & Poor's. Rescission occurs when the MI determines that the loan did not meet underwriting guidelines from the outset. In such cases, the MI returns the premiums paid and does not pay the lender claims.

By contrast, claim denials could be disallowed for a variety of reasons and further information might be needed to support the claim. "When an MI denies a claim, it does not refund the premiums paid," S&P pointed out.

Rescissions have cut MI paid losses by more than $8 billion since 2008, said S&P. Some MIs rescinded insurance on more than 24 percent of the mortgages for which claims were submitted in 2009, although in the first half of 2010 this share had eased somewhat. S&P analysts say lenders are using litigation and arbitration to reverse these rescissions since lenders have little to lose by suing MIs in court.

“Mortgage insurers could find it difficult to justify all of the policies rescinded, particularly in cases where in the past they might have paid or settled claims represented under similar circumstances,” said S&P analyst Ron Joas. “As a result, legal proceedings could focus on MI’s processes and procedures.”

Rescissions have mostly happened on 2005-2007 vintage loans, which are showing signs of burnout. Consequently, the benefits from rescission will likely drop in coming quarters, said Joas. However, claim denials could increase, though denials are more susceptible to push-back from the claimants. “So denying claims might provide only temporary relief for MIs,” he said.

Under Clarity of Coverage, Essent will not rescind coverage for delegated lenders for any underwriting errors or non-compliance “when the borrower has made 36 months of timely payment” unless there are factors that would have rendered the loan ineligible for Essent insurance.

In addition, delegated lenders will not be subject to outside investigation for fraud or misrepresentation after 36 months of consecutive timely payments by the borrower except where there is evidence of fraud or that “regulators or law enforcement” is involved.

Coverage will not be rescinded if the appraised value of the property is more than 15 percent above its market value when the loan was made unless there is evidence the appraiser acted improperly. Absent any hard evidence, Essent will not assume that a lender or its representative was involved in a borrower’s fraud. Documents that have little bearing on the loan’s eligibility or risk assessments and later found missing from the loan file will not constitute grounds for rescinding MI coverage.

Marzol said only “professional and fair investigative approaches will be used in determining if a loan has met the MI’s requirements. No unreliable investigative techniques – hearsay evidence, for example – will be used as the sole basis to determine misrepresentation,” he added.

On the other hand, lenders that agree to use Essent’s own underwriting guidelines will be fully protected because the MI is essentially taking full responsibility for the loan’s outcome, said Marzol.

Meanwhile, Radian is also planning to announce a similar initiative. “Radian will be releasing a 24-month limited rescission waiver program shortly for our delegated underwriting customers,” said a company spokesperson. “We continue to work closely with our mortgage servicing partners in managing defaulted loans and identifying solutions to keep borrowers in their homes.”

A spokesperson for Mortgage Guaranty Insurance Corp. declined to comment on Essent’s master policy enhancement but noted that MGIC’s claims process “includes steps to help the insured understand how we arrived at a claim settlement amount, and provides an opportunity for the insured to appeal our decision.” ♦