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2nd Circ. Filed-Rate Insurance Decision Is In The Minority

Adam M. Moskowitz

Law360, New York (October 13, 2015, 4:33 PM ET) -- The filed-rate doctrine is a century-old common law doctrine that requires entities that are required to file tariffs to adhere strictly to those terms. The purpose of the doctrine is to appropriately forbid regulated entities from charging rates other than the one on file with the appropriate state or federal regulatory authority, but a few courts have extended this doctrine to insulate defendants from alleged illegal conduct. The Second Circuit Court of Appeals recently held that the filed-rate doctrine applied to bar all claims by GMAC mortgagors against Balboa Insurance Co., the insurer that contracts with GMAC to provide lender-placed or force-placed insurance to cover lapses in homeowners' voluntary coverage for the mortgage servicer. In Rothstein v. Balboa Insurance Co., 794 F.3d 256 (2d Cir. 2015), the court held that the plaintiffs' claims offended both the nonjusticiability principle and the nondiscrimination principle underlying the filed-rate doctrine because Balboa's rates for LPI were filed with state regulators and GMAC had invoiced borrowers for the amount that GMAC had initially paid Balboa for the insurance coverage.

The Rothstein decision was certainly decided based upon the specific facts alleged in that litigation. For example, the Second Circuit's holding applied only to claims against the lender-placed insurer and not the mortgage lender/servicer. In considering application of the filed-rate doctrine, the focus in most other lender-placed litigation has been on the liability of the servicer for its specific acts directly towards the homeowner. Because of the Second Circuit's narrow focus in Rothstein, its analysis overlooked key aspects of the relationships between major mortgage lenders and servicers and their LPI providers, leading it to a result that conflicts with dozens of district court opinions from across the country. Indeed, the Second Circuit now stands with the minority in holding that the filed-rate doctrine applies to claims challenging the inflated charges that mortgage lenders and servicers impose on consumers as it related to the insurer.

The market for LPI is controlled by just two insurance groups — Assurant Inc. and its subsidiaries and QBE Insurance, formerly known as Balboa. Together, Assurant and QBE have consistently controlled more than 95 percent of the American LPI market since 2004. Today, QBE has left the lender placed market, so it is Assurant alone that controls this arena. These insurers' arrangements with all of the major mortgage lenders/servicers are materially uniform across all relationships: the mortgage lender purchases a master policy from the LPI provider to cover its entire portfolio of mortgage loans, then outsources the mortgage servicer's obligation to "track" the portfolio for lapses in coverage to the insurance provider. The master policy is a commercial insurance policy between the mortgage lender and the insurance company; the mortgage lender is the named insured and certificates of coverage are issued to individual homeowners when a lapse in coverage is detected. Pursuant to the borrower's mortgage contract, the borrower is then responsible for reimbursing the mortgage lender for the "cost" of the insurance coverage.

The major mortgage lenders' LPI practices have come under both state and federal regulatory and judicial scrutiny in the past five years because, among other things, the mortgage lenders and their LPI providers had developed intricate contractual arrangements by which the insurers would pass financial incentives back to the mortgage lenders to keep the cost of LPI high and the insurers' and lenders' dealings exclusive. Through these arrangements, after the mortgage lender or servicer had paid the full LPI premium amount under its commercial master policy with the insurer, the insurer would give the mortgage lender a rebate, sometimes termed a "kickback," based on a percentage of the premium paid. Regulators and litigants challenged these practices because although consumers' mortgage contracts obligated them to reimburse the lender for only the "cost of coverage", the mortgage lenders and servicers did not give consumers the benefit of this rebate/kickback. Mortgage lenders ultimately paid their insurers *less* than the full premium amount, which, in turn, had been calculated based on a filed rate and then charged the borrower an amount equal to the premium amount *prior* to the rebate.

In class action litigation, mortgage lenders and LPI providers have routinely raised the filed-rate doctrine as a defense to borrowers' claims. They contend that the amounts paid by the borrower are insurance premiums that are based on filed rates — the rates that the LPI insurers file for their *commercial* master policies. But the majority of district courts to have considered the issue have rejected the defense, reasoning most convincingly that the borrower is not the ratepayer precluded from challenging the filed rate. In the LPI context, the mortgage lender pays the LPI insurer a premium for a commercial master policy. As the district court observed in Rothstein, the rates for these policies are set *and approved* for lenders purchasing insurance and were designed to protect the lender's interest in mortgagors' properties. The rates set for LPI policies, that is, "were not meant to be directly applicable to individual residential mortgage loan borrowers ... and ... these rates were not approved for direct application to such individuals." Rothstein v. GMAC Mortg. LLC, 2013 U.S. Dist. LEXIS 141034, at *24-25 (S.D.N.Y. Sept. 30, 2013); see also, e.g., Jackson v. U.S. Bank, NA, 44 F. Supp. 3d 1210, 1217 (S.D. Fla. 2014) ("U.S. Bank, not plaintiffs, is the alleged ratepayer barred from challenging the other defendants' rates.")

Correspondingly, district courts nationwide, including the district court in Rothstein, have observed that government regulators review neither the contracts between the borrower and the mortgage lender nor mortgage lenders' conduct with respect to their borrowers. The charges that the lender chooses to pass on to the borrower are not calculated based on a filed rate. See, e.g., Jackson, 44 F. Supp. 3d at 1217 ("U.S. Bank is not subject to administrative oversight by state insurance commissions; as a result, its authority to regulate and approve insurers' rates does not touch the plaintiffs' claims that U.S. Bank, a lender and servicer, included impermissible costs in the amounts it charged borrowers for force-placed insurance."); Rothstein, 2013 U.S. Dist. LEXIS 141034, at *23 ("the court cannot conclude that the amounts billed to the plaintiffs for the cost of an insurance agreement between [the mortgage lender and the LPI insurer] are 'subject to the regulatory scheme in the same way that insurance rates are'") (quoting Gallo v. PHH Mortgage Corp., 916 F. Supp. 2d 537, 546 (D.N.J. 2012)); Simpkins v. Wells Fargo Bank NA, (S.D. Ill. Aug. 26, 2013) ("Plaintiffs should not be barred under the filed-rate doctrine from challenging conduct which is not otherwise addressed by a governing regulatory agency[.]"); Abels v. JPMorgan Chase Bank NA. 678 F. Sup. 2d 1273, 1277 (S.D. Fla. 2009) (adopting plaintiff's argument that "because the bank is not subject to the extensive administrative oversight that insurance companies are, applying the filed-rate doctrine in this instance would not serve either purpose" of the doctrine).

The reasoning offered by these courts makes sense because a holding that the mortgage lender is only permitted to charge its borrowers the actual cost of LPI coverage, and thus must give the borrower the benefit of any rebate that it receives from the insurer, would not require LPI insurers to adjust their rates or otherwise interfere with regulators' oversight of the insurers' *commercial* rates. The LPI provider would remain free to charge mortgage lenders the full premium calculated using the filed and approved rate, but mortgage lenders would be bound by their mortgage contracts to charge borrowers only the cost of actual coverage. Such a holding, therefore, would not offend the

nonjusticiability prong of the doctrine, which "precludes any judicial action which undermines agency rate-making authority." Marcus v. AT&T Corp., 138 F.3d 46, 61 (2d Cir. 1998).

Nor would such a holding violate the nondiscrimination principle underlying the filed-rate doctrine, under which challenges to the filed rate "would undermine the ... scheme of uniform rate regulation" Rothstein, 794 F.3d at 263. This is true first and foremost because borrowers challenging the amounts charged by their mortgage lenders beyond the cost of coverage are not challenging filed rates in the first instance. See, e.g., Laffan v. Santander Bank NA No. 13-cv-4040, 2014 U.S. Dist. LEXIS 79915, at *7-10 (E.D. Pa. June 12, 2014) (complaint could not "fairly be read as challenging the actual rates of the force-placed insurance" because plaintiff "challeng[ed] the manner and methods used by the defendant in purchasing force-placed hazard insurance"); Ellsworth v. U.S. Bank NA, 908 F. Supp. 2d 1063, 1082-83 (N.D. Cal. 2012) ("Just because the damages are based on increased costs incurred as a result of the alleged kickback scheme does not transform a challenge to conduct and practices into a challenge to the premiums.")

The Second Circuit overlooked these distinctions in Rothstein, finding that plaintiffs' claims "invite[d] judicial meddling in issues of insurance policy," thus offending the nonjusticiability principle and would "result in plaintiffs paying preferential rates for LPI[,]" offending nondiscrimination. See Rothstein, 794 F.3d at 263-64. Ultimately, the court viewed the mortgage lender as a mere "go-between" for the borrower and insurer, passing LPI rates on to the borrower, whose demand for reimbursement from the borrower could not be "decoupled" from its own purchase of LPI. See id. at 265. This analysis disregards the very nature of LPI policies, which are commercial contracts between lender and insurer, as well as the grounds on which LPI rates are reviewed and approved. In any event, the reality is that numerous lender placed class actions have been actively litigated during the past five years, mainly in the Southern District of Florida, and significant changes and reforms regarding these rates have already been agreed to by most of the insurers and banks/servicers involved in this industry. See Hamilton v. SunTrust Mortgage Inc., No. 13-cv-60749 (S.D. Fla.); Hall v. Bank of America, No. 12-cv-22700 (S.D. Fla.); Fladell v. Wells Fargo Bank NA, No. 13-cv-60721 (S.D. Fla.); Diaz v. HSBC Bank (USA) NA, No. 13-cv-21104 (S.D. Fla.); Pulley v. JPMorgan Chase Bank NA No. 12-cv-60936 (S.D. Fla.); Saccoccio v. JPMorgan Chase Bank NA, No. 13-cv-21107 (S.D. Fla.); Williams v. Wells Fargo Bank NA, 280 F.R.D. 665 (S.D. Fla.); Jackson v. U.S. Bank, Case No. 1:14-cv-21252-FAM (S.D. Fla.); Wilson v. Everbank NA, No. 14-cv-22264 (S.D. Fla.); Lee v. Ocwen Loan Servicing LLC, No. 14-cv-60649 (S.D. Fla.); Braynen v. Nationstar Mortgage LLC, No. 14-cv-20726 (S.D. Fla.); Montoya v. PNC Bank NA, No. 14-cv-20474 (S.D. Fla.); Almanzar v. Select Portfolio Servicing, No. 14-cv-22586 (S.D. Fla.); Circeo-Loudon v. Greentree, No. 14-cv-21384 (S.D. Fla.).

—By Adam M. Moskowitz and Rachel Sullivan, Kozyak Tropin & Throckmorton LLP

Adam Moskowitz is a partner in Kozyak Tropin's Miami office and is an adjunct professor at the University of Miami School of Law teaching class action litigation. Rachel Sullivan is of counsel in Kozyak Tropin's Miami office.

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