

- SUBJECT:** Revising requirements for collateral protection insurance
- COMMITTEE:** Financial Institutions — committee substitute recommended
- VOTE:** 8 ayes — Averitt, Solomons, Denny, Ehrhardt, Elkins, Grusendorf, Pitts, Juan Solis
- 0 nays
- 1 absent — Marchant
- WITNESSES:** For — Karen Neely, Independent Bankers Association of Texas
- Against — None
- On — Rob Schneider, Consumers Union
- BACKGROUND:** Some lenders using real property as collateral to secure loans require the borrower to obtain insurance on the collateral and list the lender as the beneficiary of the insurance. Collateral protection insurance differs from most other forms of insurance on real property in that it only protects the value of the collateral for the lender, not the borrower.
- Sec. 341.302, Finance Code, requires creditors who require collateral protection insurance to notify a borrower of the type of insurance obtained, the extent of coverage, the identity of the beneficiary, the coverage period, the total cost of the policy, the interest rate on the policy, and the options by which the borrower can pay the premium.
- DIGEST:** CSHB 3714 would create a new subchapter F within sec. 341, Finance Code, retaining existing statutory requirements and adding new provisions on obligations of creditors and borrowers regarding collateral protection insurance. The insurance could protect the interests of the creditor only or both the creditor and the debtor.
- The bill would define collateral protection insurance as coverage that:
- ! is purchased by a creditor after the date of a credit agreement;

- ! protects the creditor against loss or damage to the collateral or against liability arising from ownership; and
- ! is purchased as a result of the debtor's failure to provide evidence of insurance or maintain adequate coverage, with costs payable by the debtor.

A creditor would be able to require this insurance for a credit transaction if the credit agreement or separate document provided at the time of the agreement so stated. Notice in the credit agreement would declare the borrower would have to name the creditor as beneficiary. It would be purchased from an insurer authorized to do business in Texas or an eligible surplus lines insurer. If the borrower failed to meet requirements, CSHB 3714 would allow creditors to obtain collateral insurance on behalf of the borrower at the borrower's expense.

Notice in the credit agreement would specify deadlines for mailing notice from the creditor about purchase of collateral insurance, with details on the policy including cost and premium options. Repayment terms for such a policy would have to include either a final balloon payment at the end of the credit agreement or a full amortization over the term of the agreement.

CSHB 3714 would allow the borrower to cancel the creditor's policy at any time by providing proof that the borrower had obtained insurance required by the credit agreement. The insurer would refund to the creditor the amount of unearned premiums. The creditor would distribute a refund of unearned premiums directly to the borrower.

If the borrower provided evidence that the borrower had insurance in effect before the creditor's policy became effective, the creditor could not charge the borrower any costs, interest, or other charges associated with the canceling the creditor's policy.

The bill would establish that a creditor, the creditor's insurer, or the insurer's agent placing collateral protection insurance in compliance with the credit agreement would not be liable to the borrower or any other person. The bill would expressly indicate that the sole purpose of this insurance would be to protect the creditor's interest if the debtor failed properly to insure the collateral.

The bill would provide that a creditor was not required to insure collateral. The bill would not create a cause of action for damages on behalf of the borrower in connection with the placement of collateral protection insurance.

CSHB 3714 would repeal the existing provisions concerning collateral insurance in the Finance Code.

The bill would take effect on September 1, 1999, and apply only to credit agreements entered into, on, or after that date. Current law would remain in effect for credit agreements entered into before that date.

**SUPPORTERS
SAY:**

CSHB 3714 would help clear up a number of questions that have arisen since the current requirements for collateral insurance were enacted in 1993. It also would offer consumers a number of protections that are, at best, only implied under current law. These include:

- ! requiring that collateral insurance required by creditors be purchased only from authorized insurers or eligible surplus lines insurers;
- ! specifying what constitutes collateral insurance and what would be excluded from the definition;
- ! clarifying that the sole purpose of this insurance would be to protect creditors against the loss of value of the collateral used to secure a credit transaction;
- ! specifying the rights of borrowers to terminate policies bought by creditors by obtaining proper policies themselves, plus the requirements for refunding unearned premiums; and
- ! clarifying notification requirements.

The bill also would protect creditors and insurers from lawsuits that may arise from the vagueness of the current statute.

**OPPONENTS
SAY:**

No apparent opposition.

NOTES:

The substitute would change the deadline for the creditor to notify a borrower about the purchase of the insurance to within 60 days before or 10 days after the proposed purchase by the creditor, instead of from within 30 days after. The substitute would eliminate a number of provisions requiring specified

notification language and instead would use requirements based more on current law. The substitute also would make the bill prospective.

The companion bill, SB 1273 by Wentworth, has been referred to the Senate Economic Development Committee.