Collateral Protection Insurance / Blanket Vender Single Interest

Financial Institutions have three options to manage their Risk related to their Auto or Rolling Stock collateral. These are:

- Self Insure
- Blanket VSI
- Forced place Auto or Collateral Protection Insurance

A considerable analysis and discussion is needed to determine the best strategy for a Financial Institution. Each method will carry advantages and disadvantages. Noted below is a brief description of each.

I. Self Insure

A Financial Institution simple assumes “all Risk” associated with this loan portfolio. Tracking is not generally done. If a customer wrecks their vehicle and quits making payments, the Bank assumes all losses.

II. Collateral Protection Insurance / Lender Placed Insurance

The third option available to Lenders is to actually force place coverage to the Borrower as the Lenders Loan Contract allows them to do. These are written on a Master Policy that provides Physical Damage (Comprehensive and Collision) as the Primary Coverage. Various Endorsements can be used as noted below:

- Waiver of Repossession – eliminates the need for a Lender to repossess covered collateral before filing a comprehensive or collision claim; essentially making the coverage dual interest (Lender and Borrower).
- Waiver of ACV – eliminates the ACV loss settlement option in most cases to allow loss settlement to either cost of repair or loan balance.
- Automatic coverage – provides coverage in the event that tracked collateral in notice cycle or administrator has not recognized the need for placement of CPI.
- Pro Rata Coverage – insures that refunds of unearned premium will be calculated on a daily Pro Rata basis.

The Borrowers auto insurance is tracked under this system and letters are sent to communicate to those customers who have yet to provide adequate coverage. If the customer fails to respond to letters then the system will eventually force place auto coverage to protect the Bank’s interest.

III. <u>Blanket VSI</u>

Generally a premium is charged by the carrier per each covered loan. The Bank will identify each loan made monthly and charge that premium per loan and submit report to carrier. Another method is to charge a rate per outstanding balance of the portfolio total. Some states allow this premium to be charged to customers and some do not. Texas does not allow this charge to be passed on to the bank customers.

Tracking is generally not done. The Financial Institution is required to have insurance at the time the loan is made. Coverage typically includes:

A. **<u>Physical Damage Losses</u>:** This applies to collateral the institution ***repossessed***, had physical damage at the time repossession occurred, and where no primary insurance was in effect for the borrower or lienholder.

B. **<u>Non-Filing Losses</u>:** This includes losses the institution suffered due to its inability to obtain possession, or enforce their rights under the title, because of ***unintentional*** failure to perfect their lien.

C. **<u>Skip Losses</u>:** This includes losses suffered because the institution is unable to locate any maker, co-maker, or the collateral.

D. **<u>Repo Collateral Losses</u>:** This All-Risk coverage is intended for vehicles that sustain damage in the first sixty (60) days ***following*** repossession, while in the institution's care.

G. **<u>GAP (Waiver of ACV Settlement Option)</u>:** The standard VSI policy settles claims on the lesser of 3 options: the Actual Cash Value (ACV) of the collateral, the Net Balance, or the Repair Estimate, whichever is less. The GAP Endorsement (Waiver of ACV Option) is intended to protect the lender's interest in the event of a total loss under Coverage A – All Risk Physical Damage or Coverage C - Skip or Confiscation, and is valid up to $5,000 per occurrence.

<u>Physical Damage Scenario</u>:
An institution has a valid Coverage A claim that is a total loss (it would cost more to repair collateral than it is worth), there is an ACV of $5,000.00 and a Net Balance of $9,000.00. If they did not have the GAP endorsement, we would settle the claim on the $5,000.00 ACV, which is the lesser of our 2 remaining options. If they had the GAP endorsement, we would issue 1 draft for the $5,000.00 ACV and a second draft for $4,000.00, to cover the GAP between the ACV and the Net Balance.

<u>Skip Scenario</u>:
Once we have accepted liability for a Skip claim, we have 60 days to find any obligee of the note. If we do not locate any obligee of the note within that period, we will settle on the lesser of the ACV and the Net Balance. In this case, there is an ACV of $2,000.00 and a Net Balance of $7,000.00. If they did not have the GAP endorsement, we would

settle the claim on the $2,000.00 ACV, which is the lesser of our 2 remaining options. If they had the
GAP endorsement, we would issue 1 draft for the $2,000.00 ACV and a second draft for $5,000.00, to cover the GAP between the ACV and the Net Balance.

It should be noted that we will never pay more than the balance due the lender.

The previous explanations are a synopsis only. All coverages are subject to exclusions and conditions that are outlined in the policy.

COMMON VSI QUESTIONS

1. **IF THERE IS MORE THAN ONE PIECE OF COLLATERAL ON THE NOTE, DO WE CHARGE EACH PIECE OF COLLATERAL?**
   No. There is only one charge per note, regardless of how many pieces of collateral are listed.

2. **WHAT IS THE BANK'S RESPONSIBILITY IN TRACKING THE CUSTOMER'S PRIMARY INSURANCE?**
   As condition # 15 of the policy states, the financial institution must require all borrowers to obtain insurance on their collateral at the time the loan is made, and the borrower must agree to do this.

3. **OUR CUSTOMER HAS WRECKED THEIR VEHICLE, BUT HAS NOT DEFAULTED ON THEIR NOTE. CAN WE FILE A CLAIM UNDER THE VSI INSURANCE?**
   No. As condition #16 of the policy states, the customer must default and the financial institution must suffer an impairment of interest before a claim can be filed.

4. **DO I HAVE TO REPOSSESS THE COLLATERAL IN ORDER TO FILE A CLAIM?**
   Yes. Before the financial institution can file a claim, they must legally repossess <u>all</u> <u>listed</u> collateral on the note and be in position to convey good title to the insurance company, if necessary.

5. **HOW LONG DOES IT TAKE TO PROCESS A CLAIM?**
   All claims are handled, from start to finish, within our office. The single biggest delay, in claims processing, is the failure to receive all the necessary information, from the financial institution, when the claim is submitted.

   If all necessary data is received in the beginning, the claim is assigned, that day, to either the appraiser or the skip tracer.

   As respects a physical damage claim, the turn around time for the appraiser's report (which varies some depending on the geographical location) is seven (7) to ten (10) days, after which the information is verified and the draft is issued from our office.

As respects skip claims, when all required information is received, they are assigned to the investigator that same day. The policy provides for sixty (60) days location time. At the end of that period, if we fail to locate, the claim will be settled.

6. **WHAT IS THE DEFINITION OF PERSONAL PROPERTY?**
Personal property is intended to include those items that can be identified by make, model, and serial number, at the time of the loss, so that we can determine the actual cash value when necessary.

7. **WHAT IS COVERED UNDER MACHINERY & EQUIPMENT?**
Machinery and equipment is intended to include, but is not limited to, such collateral as farm tractors and their equipment, mowers, landscaping equipment, portable mixers, bobcats and similar types, which are not licensed for road use.

8. **HOW IS MY SETTLEMENT DETERMINED ON A DAMAGED REPOSSESSION?**
We will pay the lesser of three options which include: (1) The Actual Cash Value (ACV), less salvage; (2) The net payoff (Gross balance less interest and carrying charges) not more than 90 days past due, less salvage; or (3) The estimate to repair.
Note!: Only the ACV and balance are options for a skip.

9. **WHAT IS GAP COVERAGE?**
This coverage applies when either a total loss occurs under Physical Damage (Coverage A), or in the case of a Skip (Coverage C), and the financial institution's net balance exceeds the ACV of the collateral. This coverage is limited to $5,000.00 per claim.

10. **DO YOU OFFER A DIVIDEND PLAN?**
No, we do not. Complete information and code interpretations are available from our office.

11. **WHEN THERE ARE TWO OR MORE PIECES OF COLLATERAL, ON A NOTE, AND ONLY ONE VEHICLE HAS BEEN DAMAGED, CAN WE FILE A CLAIM ON JUST THE WRECKED VEHICLE?**
Yes you can, but all collateral listed on the note must be repossessed before any claim can be filed.

12. **ARE DEALER LOANS COVERED?**
Only if they are not covered under a separate full recourse agreement.

13. **IS MECHANICAL BREAKDOWN OR DAMAGE COVERED?**
Mechanical breakdown or damage is only covered when it directly results from an insured peril.

14. **ALTHOUGH WE 'VE REPOSSESSED THE VEHICLE, OUR CUSTOMER STILL HAS PRIMARY INSURANCE IN FORCE. AM I ELIGIBLE TO FILE A VSI CLAIM?**
Possibly, after the primary insurance is settled. We are excess coverage over any primary that can be collected, subject to policy limits.

15. **CAN WE SELL OUR CAR WHILE AWAITING A VSI PAYMENT?**
We strongly discourage selling the collateral until we have settled your claim. If you do sell the collateral, before we can inspect the damage, your claim could be jeopardized.

16. **HOW DO I KNOW IF I HAVE A SKIP CLAIM?**
The bank must be unable to locate the collateral, the borrower or any obligee of the note. Once it has been determined that the borrower has skipped, and is not merely delinquent, you have 180 days from the delinquency date to file a claim under Coverage C.

17. **IS THEFT COVERED?**
Yes, both total and partial thefts. Theft is considered a covered loss under Coverage A.

18. **WHAT INFORMATION DO I NEED TO SEND, IN ORDER TO FILE A CLAIM?**
There is a checklist provided in the blue Executive notebook you receive with your policy. Simply consult the list to see what we require for the type of claim you wish to file.

19. **HOW LONG DO I HAVE, AFTER REPOSSESSING A CAR, TO FILE A CLAIM WITH YOUR OFFICE?**
You have 90 days from the date of loss, (by definition), under Coverages A, B, and D.

20. **WHAT IS THE POLICY TERM AND WHAT TERM LOANS ARE ELIGIBLE FOR COVERAGE?**
The policy term is from the effective date until cancellation. After cancellation, coverage ceases. This is a continuous contract with no fixed expiration date.

Loan Terms in the basic policy include installment loans up to 60 months in length, or 62 months including extensions. This can be extended, if necessary, to accommodate most needs. Also, single payment (commercial) notes are eligible up to 12 months in length.