Mortgage Insurance Companies of America

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Office of the Comptroller of the Currency
250 E Street, SW
Mail Stop 2-3
Washington, DC 20219
Docket No: OCC-2009-0007

Robert E. Feldman, Executive Secretary
Attention: Comments/Legal ESS
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429
Attention: RIN 3064-AD42

Jennifer J. Johnson, Secretary
Federal Reserve Board of Governors
20th Street and Constitution Avenue
Washington, DC 20551
Docket No: R-1361

Regulation Comments
Chief Counsel's Office
Office of Thrift Supervision
1700 G Street, NW
Washington, DC 20552
Attention: OTS-2009-0007

Ladies and Gentlemen:

The Mortgage Insurance Companies of America (MICA) is pleased to comment on the interim final rule (IFR) issued by the banking agencies to address regulatory-capital impediments to mortgage loan modifications [74 Fed. Reg. 31,160]. MICA strongly supports efforts by the banking agencies and the Treasury Department to prevent unnecessary foreclosures, which result in untold harm to homeowners, neighborhoods, the financial system and even the global economy. MICA thus supports the IFR as a necessary measure, but we urge regulators not to lose sight of the critical discipline provided by risk-based capital that is in fact tied to risk. As has been amply and disastrously demonstrated by the current crisis, any regulatory capital requirement that creates a perverse incentive to risk taking will be quickly exploited, exacerbating procyclicality and exposing banks to

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unanticipated risk. MICA thus recommends that the capital relaxation provided in the IFR be clarified to ensure it applies only to reasonable loan modifications. We also urge that the rules be replaced in connection with the broader rewrite of U.S. regulatory capital standards now under way.

In this letter, MICA will do the following:

- Detail the role mortgage insurance has played in ongoing efforts to reduce mortgage foreclosures, and reiterate the industry's commitment to work with the banking agencies in all efforts in this regard;

- Support the IFR as a temporary measure required in light of the current crisis. MICA believes that capital relief should apply only to loans modified through the Making Home Affordable Program.[1] This program has essential controls in it to ensure long-term borrower ability to repay that limits the risk of defaults that are costly to borrowers, neighborhoods and the financial system that may not be included in other mortgage loan modifications. As detailed below, MICA also recommends additional clarifications to protect the borrowers long-term ability to repay; and

- Summarize considerations for regulators with regard to mortgage loan-to-value (LTV) and other credit risk criteria as the broader rewrite of regulatory capital rules commences. MICA suggests that the regulators clarify in the preamble to the final rule that its reduced regulatory capital requirements are provided solely due to the current crisis and set no precedent for subsequent regulatory capital standards for residential mortgages. Credit risk is directly linked to LTV and risk-based capital under normal circumstances should similarly be closely aligned with it and rise sharply in tandem to prevent risky lending practices based on house price appreciation.

The private mortgage insurance industry has existed since 1957. Since that time, it has helped more than 25 million families buy homes. Today, the MI industry's capital stands behind over 900 billion dollars of mortgage loans. That is almost 9% of all home mortgage debt outstanding.

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[1] Press Release, U.S. Department of the Treasury, Relief for Responsible Homeowners One Step Closer Under New Treasury Guidelines, (March 4, 2009).

According to the 2007 Home Mortgage Disclosure Act (HMDA) data (the most recent data available), 51% of the borrowers who received mortgages insured by private mortgage insurers made less than area median income and 35% made less than 90% of area median income. The income distribution of mortgage insurers customers combined with the fact that numerous studies have determined that the lack of a substantial down payment is the major barrier to homeownership leads us to believe that a substantial share of our purchase business is comprised of first-time homebuyers who would not be able to get into an affordable home without the benefit of mortgage insurance.

MICA Supports Loan-Modification Efforts

As noted, MICA strongly endorses the efforts under way by the banking agencies and the Treasury Department to prevent avoidable foreclosures. Having their own capital at risk means that mortgage insurers have very clear incentives to mitigate their losses if a loan is in default. The best way to do that, of course, is to avoid foreclosures altogether by working with borrowers to keep them in their homes.

Mortgage insurers have a history of partnering with lenders, investors and community groups to work with borrowers in default. In today's devastating mortgage market, they continue to play a leadership role in working with all parties, including with the Obama Administration. In 2008 alone, MICA members were able to save almost 100,000 people from losing their homes.

MICA Comments on the IFR

As noted above, MICA supports the interim final rule as an appropriate temporary measure to prevent unavoidable foreclosures. However, we recommend the clarifications to the final rule discussed below that are, we believe, fully consistent with the IFR and promote its goals of preventing unnecessary foreclosures without creating additional risk to financial institutions already experiencing significant strain and capital pressure.

First, as noted, MICA urges regulators to retain provisions in the IFR that limit capital relief only to loans under the Making Home Affordable Program. As you know, this Program includes numerous controls – for example, debt-to-income tests – that are designed to limit default risk. The program is also limited to primary residences, which targets government assistance and capital relief only to mortgages that promote home ownership. Many other mortgages were intended for investment or second home purposes and should not be granted any

regulatory capital relief because these loans are and will remain high-risk ones for which borrowers should not receive federal support. If these loans are delinquent or face foreclosure, lenders should work with borrowers on a case-by-case basis as has long been done and recognize any losses as quickly as possible to strengthen the financial system and promote economic recovery.

In addition, MICA recommends that the final rule be clarified so that any mortgage modified under the program that receives preferential capital treatment and that had mortgage insurance in place prior to the modification has such coverage on the modified loan if the LTV exceeds 90%. This coverage may come from the Federal Housing Administration (FHA) or private mortgage insurers, and it provides following two critical elements that protect borrowers and limits risk to the modifying insured depository institution:

- First, insured loans are subject to eligibility criteria and, in the case of loans backed by private mortgage insurance, a second underwriting done solely to ensure the long-term ability of the borrower to repay. Because the private mortgage insurer's interests are fully aligned with those of the borrower, this underwriting ensures that Making Home Affordable Program -- an essential risk-management tool for the federal government -- criteria in fact have been met.

- Second, mortgage insurance provides credit risk mitigation for the lender or investor. It is for this reason that the banking agencies' rules have long provided reduced regulatory capital requirements for loans with coverage by regulated, capitalized providers of private mortgage insurance. This principal should be retained and the rule should thus be clarified to urge lenders to seek mortgage insurance for the modification when it was in place on the original mortgage obligation. The greater the mortgage insurance coverage, the less credit risk to lenders and investors and, thus, the more appropriate the reduced risk-based capital requirements provided in the IFR.

Regulatory Capital Reform

Finally, MICA would like to provide forward looking comments on residential-mortgage regulatory capital. We have been pleased to comment extensively on all of the U.S. proposals to rewrite these rules and are grateful that the final version of the U.S. advanced rules[2] and the proposed standardized capital standards[3] reflect the

[2] 72 Fed. Reg. 69,288.

significant impact LTV has on mortgage credit risk. In our prior comments, MICA emphasized that underwriting factors such as credit score – while useful – have only some bearing on probability of default and none at all on loss given default, which is driven by the initial LTV and cannot be affected by any house-price appreciation scenarios or similar factors built into loan underwriting. We have deplored the mortgage instruments based principally on house price appreciation, not long-term ability to repay, and urged regulators in the capital rules to ensure that speculative structures with high LTVs are given punitive capital charges and that the important role of regulated, capitalized forms of credit risk mitigation like mortgage insurance are recognized and rewarded.

With this background, we urge the banking agencies to make clear that the reduction in risk-based capital for high-LTV loans is a temporary measure designed only to promote mortgage modifications in the current crisis. It cannot and should not be seen as a precedent that will be reflected in the pending rewrite of U.S. regulatory-capital standards now under way to address the hard, costly lessons of the crisis and the role uninsured high-LTV mortgage lending played as a cause and ongoing contributor to the financial market melt-down.

MICA understands that the banking agencies are considering not only the appropriate risk weighting for high-LTV mortgages in the new capital rules, but also broader changes to ensure that, going forward, regulatory capital standards are not procyclical. In this respect, we draw your attention to the capital requirements applicable to private mortgage insurance, which in fact have long been structured to ensure the "dynamic provisioning" regulators are now considering for banks and bank holding companies.

Mortgage insurers are required to keep three types of reserves, the most important of which is the contingency reserve. Half of each premium dollar earned goes into the contingency reserve and generally cannot be touched by the mortgage insurer for a ten-year period. It ensures that significant reserves are accumulated during good times not only to handle claims under stress, but also to avoid boom-bust cycles. Therefore, unlike other financial institutions that may pay high dividends during profitable periods, mortgage insurance companies build their contingency reserves during these periods in order to have the capital ready to pay the higher claims that inevitably occur during periods of market corrections such as the one the U.S. is now experiencing.

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[3] 12 C.F.R. Part 3 (1997).

MICA would be pleased to provide any additional information to support the final rule based on this IFR. We also look forward to working with the banking agencies as broad reforms to the regulatory-capital regime begins.

Sincerely,

Suzanne C. Hutchinson