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October 22, 2012

Office of the Comptroller of the Currency
250 E Street, S.W., Mail Stop 2-3
Washington, D.C. 20219
Docket ID: OCC-2012-0009
RIN: 1557-AD46

Ms. Jennifer J. Johnson, Secretary, Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, D.C. 20551
Docket No.: R-1442
RIN: 7100 AD 87

Mr. Robert E. Feldman, Executive Secretary, Federal Deposit Insurance Corporation
Attention: Comments/Legal ESS
550 17th Street, N.W.
Washington, D.C. 20429
RIN: 3064-AD96

VIA FEDERAL E-RULEMAKING PORTAL
http://www.regulations.gov

RE: Comments on Non-Recognition of Private Mortgage Insurance in in the Proposed Capital Rules: Standardized Approach for Risk-Weighted Assets

Dear Sir or Madam:

National Mortgage Insurance Corporation (National MI) appreciates this opportunity to comment on the proposed Regulatory **Capital Rules: Standardized Approach for Risk-Weighted Assets; Market Discipline and Disclosure Requirements** (Standardized Version) issued by the respective bank regulatory agencies (Agencies).

National MI, headquartered in Emeryville, CA, has been created to offer private mortgage insurance to help homebuyers purchase and finance residential housing. National MI is a newly formed company that will bring a half billion dollars in private capital to the housing market. National MI (www.nationalmi.com) intends to offer mortgage insurance on a national basis after receiving the necessary approvals from Fannie Mae, Freddie Mac and state regulators. National MI is committed to delivering high quality customer service and strong investor results.

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National MI believes it important that bank regulators recognize the important role of private mortgage insurance in the sound operation of the housing market, and that private mortgage insurance can be offered safely and without excess risk to banking organizations.

In these comments, National MI will (1) address the importance of Private Mortgage Insurance (Private MI) to the residential housing market, (2) review the structure of Private MI, (3) discuss the regulation of private mortgage insurers, and (4) discuss the economic performance of the industry.

In specific response to the agencies' request for comments on private mortgage insurance's role in the standard risk model, we will point out (1) the benefits of Private MI to banking organizations and the communities they serve and (2) the adverse consequences of failing to include Private MI in banking organization's risk weighted capital calculations. Finally we will address the question of the criteria banking regulators can use to ensure mortgage insurers are sound.

I. BACKGROUND

1. The Importance of Private Mortgage Insurance to the Residential Housing Market

Mortgage lending is the foundation of the United States housing market. Without an effective mortgage lending system, homebuilding and the many industries associated with it would come to a near standstill. Private mortgage insurance is an integral part of our mortgage lending system.

Private MI plays a specific role in mortgage lending. In broad terms mortgage lending works as follows. Loans are originated by banks, by mortgage companies or by loan originators. The may be held in the portfolio of the originator or, as has happens frequently, they are sold. These loans are aggregated together into packages (securitized) and sold to the end user investor who wishes to own the stream of payments promised by the bundled individual notes. These end users may be pension funds, insurance companies, or other financial investors.

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The largest buyers of residential mortgages are the government chartered Fannie Mae and Freddie Mac (the GSEs), which along with the FHA and the VHA currently account for more than 90% of the mortgage purchase market. The GSEs' loan purchasing standards require a loan-to-value ratio of at least 80%, unless the loan is insured by Private MI, or the lender retains either full recourse on the loan or a participation interest in the loan.

Most borrowers cannot make a down payment equal to 20% of the appraised value of a property. The median existing home sales price in August 2012 was $187,000, which would require a 20% down payment of $37,480. Few families or individuals have liquid assets available to make such a payment.

Private mortgage insurance is often, though not always, utilized by first time home buyers who often have the income required to service a mortgage, but lack the savings to make a 20% down payment. A number of studies have shown that this set of circumstances will be especially true for the generation that will be entering the peak home buying years of the early to mid-30's over the next decade. So the need for mortgage insurance will be increasing, and should remain at a sustained level for a number of years into the future in order to meet first time buyer demand. To function effectively, the residential mortgage market must have some mechanism for addressing the difference between the loan-to value ratio mandated by the GSEs and the realities of the marketplace. Private mortgage insurance is one such mechanism.

Private mortgage insurance insures the difference between the 80% requirement and the amount of the actual loan. Private MI makes it possible for a person to acquire a mortgage with a down payment as low as 5% of appraised value, something that is far more within reach of most borrowers. Private MI is funded by private capital, and provides another buffer against loss to the owner of the mortgage.

Private mortgage insurance is not the only mechanism available to mitigate mortgage-lending risks. Lenders could refrain from making high loan-to-value loans, which would exclude many would-be homebuyers from the housing market. This in turn would depress the recovery of the housing market even further.

Alternately, the GSEs could assume the risk of high loan-to-value mortgages. This is not currently a viable alternative, since the GSEs are in conservatorship and prohibited by law from bearing the additional risk of high LTV mortgages.

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A third option would be for lenders themselves to assume the additional risk. Given the present regulatory views on risk weighting, it is doubtful that regulated lenders would move significantly into this area. Further, regulated lenders' capital is not structured to cover insurance risks. They do not have requirements or operating models that call for large reserves in good times. To the extent that the lenders were local or regional, they would have geographic concentration risk, the effect of which bank regulators have observed all too painfully during the recent crisis.

Private mortgage insurance offers a way to bridge the LTV gap with private capital and under conditions that can satisfy regulatory concerns.

2. Structure of Private Mortgage Insurance

The terms of coverage of private mortgage insurance are set forth in the master policy, which must be acceptable to the insurance beneficiary (the GSE or private owner of the mortgage). Private mortgage insurance may take several forms:

- Flow insurance covers an individual loan at the time of its origination.
- Bulk insurance covers each loan in a larger group that has already been originated.
- Pool insurance covers multiple mortgages up to an aggregate loss.

Mortgage insurance risks may be reinsured either by independent or by captive reinsurers. Mortgage insurance policies typically cover losses suffered by the lender up to a maximum of 25% of the balance of the mortgage. Most states have laws that restrict the mortgage insurer's risk exposure to 25% of the loan balance. Mortgage insurers do offer coverage amounts in excess of 25% of the loan balance and they reinsure the additional risk exposure, typically with an affiliated company. Coverage generally takes effect upon foreclosure. The typical claim will include a percentage of the outstanding principal and interest on the loan as well as expenses incurred by the owner during the foreclosure process, such as legal expenses and property taxes. Private MI is automatically terminated when a homeowner's equity through mortgage payments reaches 22% of the original sales price or original appraised value. Thus, homeowners do not pay for unneeded coverage.

3. Regulation of Private Mortgage Insurers

Mortgage insurance, like insurance in general, is primarily regulated by the states. Individual states' regulatory frameworks establish reserve requirements, capital requirements and imposes investment and concentration restrictions. While state laws differ in some details, the essential requirements are substantially similar among the jurisdictions that have enacted specific statutory requirements relating to mortgage insurers.

Reserve Requirements. Mortgage insurers have several forms of reserves. The first category is "contingency" reserves. Mortgage insurers must retain 50% of net earned premiums, which cannot be released for 10 years unless the insurer has very high losses during a given year. In that case, the insurer can draw down its contingency reserve temporarily to pay claims. In addition to "contingency" reserves, insurers must hold "loss" reserves, to cover expected claims and losses on known delinquent loans.

Insurers must also retain the amount of premiums paid before the coverage period as "unearned premium" reserves.

Capital Requirements. The standard risk-to-capital ratio for private mortgage insurers has been 25-1. In view of the significant reserve requirements, this capital ratio has not been an issue except in severely adverse economic conditions. In some cases, state regulators have granted temporary waivers so that the insurers could continue to write new insurance in order to generate revenue.

Investment Restrictions. Private mortgage insurers must follow state insurance law restrictions on investments. These include mandates that exposures must be limited geographically and prohibitions against real estate investments. Common permitted investments are stocks, bonds and notes.

4. Performance of Private Mortgage Insurance

The U.S. housing market underwent a series of recessions in the 1980s and the early 1990s. While several insurers went out of business and others were recapitalized or sold, with one exception (Ticor) all were able to repay policyholders in full. The industry as a whole met its claims-paying obligation, paying out over $14 billion during this period.

The current crisis in the housing market has been the most serious since the Great Depression. It has been nationwide in scope, infused with questionable products and outright fraud. Nevertheless all of the active private mortgage insurers continue to satisfy all of their claims, paying obligations despite operating at a loss since 2007. The mortgage insurance industry has paid more than $28 billion since 2007, and continues to respond to claims. Private mortgage insurance has unquestionably buffered losses to both homeowners and lenders.

II. RESPONSE TO QUESTION 6

The NPR requested specific comment with respect to private mortgage insurance. Question 6 asks (a) whether banking organizations should be allowed to recognize private mortgage insurance for calculating loan-to-value ratios and (b) what criteria could be used to ensure private mortgage providers are sound.

1. Banking organizations should be allowed to recognize private mortgage insurance for calculating loan-to-value ratios.

The better policy is to permit banking organizations to recognize private mortgage insurance when calculating loan-to-value ratio for a number of reasons.

First, insurance that covers the banking organization in the event of the default on a loan in its portfolio reduces the risk to the banking organization holding that loan. It is an additional buffer against loss. It is part of an overall structure of good lending. It is a useful tool in the lender's toolkit when making a loan. The bank is certainly better for having the insurance than not.

Second, private mortgage insurance can improve the quality of lending. Private MI underwriting represents a second set of eyes on a loan. Because of their experience with underwriting, with claims management and with loss mitigation, private mortgage insurers often better understand the risks associated with high loan-to-value loans. This can be particularly valuable to community and smaller banks that may not have deep experience with loans of this type.

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Third, private mortgage insurance will help a banking organization meet its CRA and community goals. As a matter of policy, banks are encouraged to make sure that they serve their minority and other underserved communities. In terms of mortgage finance needs, access to affordable, low down payment mortgage financing is important for these communities and private mortgage insurance will help banks to better serve the housing needs of these communities.

Fourth, private mortgage insurance is a source of capital support for banks. Private MI shifts some of the risk of residential lending from the banking institution to other sources of private capital.

2. Consequences of the Failure to Recognize Private Mortgage Insurance

Failing to recognize private mortgage insurance in the capital rules will discourage banking organizations from making higher loan-to-value loans, which will have its greatest impact on the less affluent. The decision not to recognize Private MI will affect credit allocation by making the extension of higher LTV loans more expensive if they are held in the banking organization's portfolio. The natural economic consequence is to direct lending away from transactions that adversely affect capital and toward transactions that do not.

One of the criticisms of the mortgage system during the recent crisis was that institutions had no stake in the loans they originated and so were less concerned with the quality of the underwriting than they might otherwise be. Non-recognition of private mortgage insurance will mean that banks have even less incentive to hold higher LTV loans in their portfolios and more incentive to pass them on.

The disincentives to making and holding higher LTV loans do not fall evenly on all banking organizations. Community banks and regional banks have proportionally more of such loans on their books. They tend to be closer to individuals in the community, and may thus be more committed to addressing their needs. If private mortgage insurance is not recognized it will be that much more difficult for them to extend such credit.

Private mortgage insurance is an additional means of risk mitigation. It provides an additional source of capital for the mortgage market. It is a non-governmental source of additional strength to support residential mortgages in the portfolios of banking organizations. Discouraging it will have a negative effect on capital available to the banking organization.

Private mortgage insurance, as noted, can be helpful in the mortgage origination process. It serves as a second set of eyes in the underwriting process. This is particularly important for institutions that are not regularly in the business of making residential loans. Creating a disincentive to use Private MI will take this expertise out of the banking organization's process.

We understand banking regulators' concerns about high LTV lending, but these loans serve an important function in the housing market. Our goal should be to make this type of lending safer, rather than to restrict it or eliminate it altogether, by providing banks with a source of loss protection on these loans.

III. CRITERIA TO ENSURE THAT PRIVATE MORTGAGE INSURERS ARE SOUND

We understand that bank regulators need confidence in mortgage insurance companies' ability to respond to financial demands when called upon to do so. We further understand that regulators need a reliable method in which they have confidence to make the determination that the insurer will be able to respond.

We believe that a stress test specifically tailored for mortgage insurers can give banking regulators the assurance they need that the companies that stand behind mortgage insurance are capable of fulfilling their obligations. Regulators are familiar with the concept of stress tests, and use them in other areas as part of current regulatory practices.

The stress test we envision would include the key elements listed below, which we believe would the agencies the information necessary to identify and recognize only financially sound private mortgage insurers.

(1) The test would analyze, on an annual basis, whether the Private MI would have resources to pay all anticipated claims, focusing on claims paying capacity in even the most highly stressed conditions.
(2) For purposes of the test, all Private MIs within the same insurance holding company system, or providing or receiving substantial services from another Private MI, would be consolidated and treated as a single Private MI.

(3) The baseline of the analysis would be the actual performance of actual high LTV mortgages between 2007 and 2012. This would capture mortgages originated during the most stressful time in the history of the U.S. mortgage market.
(4) The baseline would be static. It would not change over time, and would thus ensure the measurement of stress levels at their most extreme point.
(5) An independent third party such as an auditing or actuarial firm would administer the test.
(6) The test would assume that the company ceases writing new business at year-end so that the results do not depend on income from future business, but would include premium income on loans insured on or before the end of the year.
(7) The bank regulatory agencies themselves should set the standards and criteria for the test with input from a mortgage insurance industry advisory panel.

Private mortgage insurance underwritten by companies that pass a stress test containing these elements should qualify for full credit under the new risk weightings, and lenders should receive at least partial credit for all private mortgage insurance tied to the results of these tests.

IV. CONCLUSION

Private mortgage insurance is an important and valuable financial product, making access to housing and mortgage loans possible for millions of deserving persons. Private mortgage insurance helps bridge the gap between the 80% loan-to-value requirement of the lending market and most borrowers' financial reality.

Private MI supports banking organizations by using private, not public funds to provide an additional buffer against loan loss. It can strengthen bank underwriting and make it easier and less burdensome for banks to carry out their CRA and community responsibilities.

Regulatory guidance and risk weightings should encourage private MI, rather than discouraging it, as the proposed risk weighting would do. Allowing bank regulators to set and enforce reliable stress tests for private MI providers would ensure that only financially sound private mortgage insurance qualifies for full credit under the new risk weighting.

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We respectfully request that the final rule provide that private mortgage insurance qualify for full credit under the new risk weightings when underwritten by companies that pass a stress test approved and overseen by banking regulators, and that lenders receive at least partial credit for all private mortgage insurance tied to the results of the appropriate test.

We appreciate this opportunity to comment on the proposed rulemaking, and would be happy to provide additional information if needed.

Sincerely,

Bradley M. Shuster
Chairman and CEO
National Mortgage Insurance Corporation