Mortgage Insurance Companies of America

Suzanne C. Hutchinson
Executive Vice President

May 22, 2009

Alfred M. Pollard, General Counsel
Attention: Comments/RIN 2590–AA25
Federal Housing Finance Agency
Fourth Floor, 1700 G Street, NW.
Washington, DC 20552

Re: Regulatory Information Number (RIN) 2590-AA25

Dear Mr. Pollard:

The Mortgage Insurance Companies of America (MICA) is pleased to comment on the revised affordable-housing goals proposed by the Federal Housing Finance Agency (FHFA) for the government sponsored enterprises Fannie Mae and Freddie Mac (together the GSEs).[1] The private mortgage insurance (MI) industry is dedicated to promoting affordable housing. Indeed, MI is critical to ensuring that first-time buyers and others who lack a large down payment can become homeowners when disciplined underwriting demonstrates their long-term ability to repay a mortgage. It is an unfortunate fact that far too many affordable housing loans – including those purchased by Fannie Mae and Freddie Mac – were not prudent and their performance contributed to the profound housing crisis now gripping the GSEs, U.S. mortgage finance and even the global economy. MICA urges FHFA not only to proceed with the proposed affordable housing framework, but to build on it to ensure that going forward all GSE-purchased affordable housing loans in fact promote home ownership by low-and moderate-income individuals and support neighborhood development through responsible underwriting.

Specifically, MICA would make the following comments discussed below in more detail:

- FHFA should not only finalize the proposed affordable housing goals, but also reserve the right – as proposed – to revise them further through 2009 as needed. In doing so and establishing the next round of more permanent affordable housing goals for 2010 and beyond, FHFA should consider ways to create incentives to promote sustainable affordable housing lending. These could, for example, include penalties for loans that go into early default, such as subtracting them from those that qualify for

[1] 74 FR 20236.

1425 K Street, NW
Suite 210
Washington, DC 20005
(202) 682-2683
Fax (202) 842-9252

affordable housing consideration and, perhaps, even requiring subtraction of a multiple of any such early-payment default loans to ensure that the goals promote sound GSE practice.

- In the 2009 goals and beyond, MICA urges FHFA to stipulate that all qualifying loans must meet appropriate underwriting standards that ensure borrower protection. These should at a minimum ensure compliance with the Federal Reserve's recent Homeownership and Equity Protection Act (HOEPA) rules,[2] but also go beyond them to ensure that the GSEs can both fulfill their statutory mission and comply with all charter and prudential requirements.

- MICA notes that FHFA cites as causes for the new approach capital pressures in the MI industry and tougher underwriting standards. MICA deeply appreciates Director Lockhart's recent calls for support of MI capitalization through the Troubled Asset Relief Program (TARP) authorized in the Emergency Economic Stabilization Act.[3] As Mr. Lockhart and FHFA understand, private mortgage insurers are adequately capitalized to meet expected claims but seek federal support to ensure MIs play a full role in the mortgage market's recovery and in foreclosure prevention. MIs are review underwriters and have a depth of experience in underwriting low-down payment mortgages. This second set of eyes ensures that borrowers can in fact repay their loans. We urge FHFA to require the GSEs to purchase only affordable housing loans that are prudently underwritten and support long-term homeownership and neighborhood stability.

I. MICA Supports the Proposed Goals and Future Flexibility

MICA supports FHFA's proposed approach both with regard to the adjusted goals and the criteria on which these will be judged. In particular, MICA supports the inclusion of loan modifications in the purchase goals because these loans ensure ongoing home ownership and are thus not comparable to loan refinancings executed only to realize home-equity appreciation, promote consumption spending or for other goals not directly related to maintaining home ownership. MICA also supports subtracting jumbo loans from the denominator against which the goals are judged because these loans are authorized for GSEs

[2] 73 FR 44521.
[3] Public Law No. 110-343.

to support market recovery, not meet mission requirements. Including them in the goals would make them overly difficult to meet and thus create undue incentives to risk taking.

Overly stringent goals do nothing to support affordable housing, as is now all too evident in foreclosures, neighborhood blight and the GSEs' serious related problems. As GSEs, it is wholly appropriate that Fannie Mae and Freddie Mac meet affordable housing goals and use their federal charters to support this critical national priority. However, they must lead the market with a prudent, disciplined approach that promotes the intent of these goals rather than undermining them by creating a secondary market for high-risk loans. Thus, in addition to easing the goals, MICA recommends that FHFA also expressly mandate prudential standards governing qualifying loans, doing so as discussed in more detail below either in conjunction with finalizing the 2009 goals now or in future revisions to these goals and forward-looking standards governing years to come.

Because of the risk resulting from inappropriate affordable housing goals, MICA endorses FHFA's proposed reservation of the right to revise the 2009 goals. Current market conditions remain volatile and uncertain, making any estimate of obtainable, prudent affordable housing goals now at best an informed guess. Reserving this right will also provide FHFA with time to make substantive changes, including consideration of penalties related to early default suggested above.

II. Prudent Underwriting Must Be Mandated in Conjunction with These Goals

Flexibility also will permit FHFA to consider specific underwriting standards for affordable housing qualified loans if time does not permit doing so in conjunction with finalizing the current proposal. As noted, MICA recommends that FHFA expressly require that all loans purchased by the GSEs and used to qualify for these goals meet underwriting standards at least as stringent as those mandated by the Federal Reserve's HOEPA rules. MICA understands that the FRB's rules are mandatory and thus might be assumed to apply to all loans sold to Fannie Mae and Freddie Mac. However, mandating compliance with these standards not only at origination, as done by the Federal Reserve, but also at purchase – as only FHFA can do – provides a critical safeguard to reinforce the important borrower and investor protection stipulated by the Federal Reserve.

However, MICA believes that FHFA should mandate additional safeguards to ensure that the GSEs at all times comply with their mission and charter – issues not considered by the Federal Reserve in the HOEPA rule. Of particular concern here are loans with simultaneous second liens, which are structured loans with first and second liens issued at the same time to a borrower who cannot or chooses not to make the down payment required under the Fannie Mae and Freddie Mac charters.[4] Through these mortgages the borrower avoided the second underwriting that a private mortgage insurer would have provided to assure that the loan amount and loan terms were prudent for the particular borrower.

As FHFA well knows, the charter requirements dictate one of three forms of credit enhancement, including MI, for mortgages that have loan-to-value (LTV) ratios above eighty percent. Borrowers and lenders sought to evade these prudential requirements by splitting loans into pieces with combined LTVs of as much as 100 percent or even more. Fannie and Freddie are now exposed to losses in the first liens that comprised portions of these loans, often called piggyback mortgages, but often without the protection of credit risk mitigation, thus validating the taxpayer-protection rationale that led Congress to mandate credit enhancement for loans with initial high LTVs. Further, borrowers with these piggyback mortgages are having particular difficultly obtaining loan modifications to prevent foreclosure because of the obstacle created by the second lien. Borrowers were being steered into these piggyback mortgages and the piggyback mortgages facilitated by the GSEs through their purchase of either the first or second lien have had a net negative and serious adverse impact on the nation's housing market and borrowers.

As a result, going forward we think it critical that the FHFA stipulate that any mortgage loan that qualifies for the affordable housing goals meet all applicable GSE charter requirements, including those governing third-party credit enhancement. This will not only ensure borrower protection, but also – as Congress intended – put private capital at risk on higher-risk, high-LTV loans. As FHFA knows, bank regulators and Congress have determined that the absence of capital-at-risk was a profound contributing factor to the crisis created by the originate-to-distribute approach to mortgage securitization. FHFA should ensure that all of its rules going forward, including those governing affordable housing, reflect this hard lesson and correct for it.

III. Private MI Seeks a Greater Role Supporting GSE Affordable Housing

Finally, MICA would like to address the comments throughout the proposal that directly deal with private mortgage insurance. These fall

[4] 12 USC 1717 and 12 USC 1454 respectively.

into two parts: suggestions that the industry is under capital pressure and that tighter underwriting standards adversely affect the GSEs' ability to meet affordable housing requirements.

First, on the capital issue, as noted at the outset of this letter, private MIs are adequately capitalized to meet anticipated claims. This results in part from the contingent reserve required by state regulators to ensure that MIs have capital even under catastrophic risk conditions such as those now gripping the nation's housing market. This capital requirement – which puts aside fifty percent of each premium dollar generally for a ten year period – is precisely the type of counter-cyclical capital that global and U.S. regulators are now seeking for the banking industry. For example, a recent document from the International Financial Stability Board[5] suggests precisely this "dynamic provisioning" approach to capital to ensure that, going forward, banks are as well prepared as private MIs to handle stress scenarios. Chairman Bernanke has also frequently called for this approach to counter-cyclical capital.[6]

While rigorous, MI regulatory capital is not designed both to bear catastrophic risk, and also to support significant new business. However, this new business is a critical need as the FHFA, Treasury and other policy-makers seek ways to provide liquidity to the mortgage market that supports housing prices and helps to prevent foreclosures.

To ensure that MIs can fully participate in the market's recovery, individual MIs may require additional capital support. Director Lockhart has played a leadership role in discussing this with other decision-makers, and MICA is grateful for all his hard work on this critical issue. With regard to MI underwriting practices, it is critical to note that these provide essential borrower protection. Because MIs are of course at risk if a mortgage is foreclosed, MI's underwriting is a disciplined process to evaluate long-term ability to repay.

Conclusion

MICA endorses the proposed 2009 affordable housing goals, but urges FHFA to remain flexible both with regard to them and the shape of the goals to come. Going forward, we think it critical to ensure that all loans that qualify for the goals meet stringent prudential requirements that protect borrowers, the GSEs and the mortgage-

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[5] Financial Stability Forum, *Report of the Financial Stability Forum on Addressing Procyclicality in the Financial System* (April 2, 2009).
[6] Ben Bernanke, Chairman of the Federal Reserve Board, Address at the Federal Reserve Bank of Chicago Conference on Bank Structure and Competition, Chicago, Illinois (May 7, 2009).

finance system more generally. Private mortgage insurance will be critical to promoting these affordable housing goals, as well as to broader stabilization of U.S. housing finance. The industry is now adequately capitalized to meet current claims, but does require additional support to play the larger role in affordable housing for the GSEs contemplated by FHFA.

Sincerely,

Suzanne Hutchinson

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