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Chairman of the Board
President and Chief Executive Officer

The Honorable Melvin L. Watt
Director
The Federal Housing Finance Agency
400 7th St. SW
Washington, DC 20024

September 8, 2014

Dear Director Watt:

Thank you for giving us the opportunity to comment on the newly proposed Private Mortgage Insurer Eligibility Requirements (PMIERs). We hope you find our comments constructive and helpful in moving this important initiative forward.

We are generally supportive of the proposed PMIERs and the framework for their implementation. However, we believe some changes should be made to better position the PMIERs to meet the goals of mitigating future Enterprise losses and ensure that Approved Insurers maintain sufficient financial strength to withstand a stress macroeconomic scenario. The changes we suggest would affect the calculation of both Required Assets and Available Assets and would, we believe, more effectively encourage Approved Insurers to adopt and adhere to prudent credit risk and pricing policies, and ensure Approved Insurers are able to meet their claims obligations.

We suggest the following Financial Requirement changes:

- Add credit for future premium to the calculation of Available Assets in the form of two years credit for monthly premiums and 50% credit for unearned premium reserves, subject to limitations detailed in our response below;
- Explicitly include seasoning factors for performing loans that reduce Required Assets as a book year ages through a non-stress economic environment. In the absence of a severe economic decline, the Required Asset factors should decrease as a book year ages; and
- Apply Table 3A to all loans and add risk multipliers for additional layered risk components (e.g., ARMs, cash-out refinances, manufactured homes and multi-unit properties), including multipliers less than 1.0 to recognize characteristics that reduce risk (e.g., 15 year term).

The most important change we propose to the PMIERs is to recognize some credit for future premium in the calculation of Available Assets. We would note that the credit we propose is considerably less than an MI in runoff would likely collect over time. Future premium streams can be and have been counted on as a source of claims-paying resources.

An MI's coverage is effective only as long as premiums are paid. As recent history has shown, even in cases of regulatory action, an MI may be able to meet all of its claims obligations due to premiums collected after runoff begins.

In addition, giving credit for future premium provides a meaningful incentive for Approved Insurers to properly price their premiums, and thus helps create a self-regulating set of requirements. If an Approved Insurer receives no credit for future premium income, there is little disincentive to cut pricing in order to gain market share. The market share gain is immediate and the impact of lower returns is slowly realized over the ensuing years.

However, if an Approved Insurer receives credit for future premium income, a price cut would result in a reduction in its Available Assets which will immediately and negatively affect its returns.

We believe that the request for changes to the Financial Requirements that we and others have made should not be used as a reason to delay the implementation of the PMIERs. The two year transition period currently contemplated is sufficient time to make adjustments to the Financial Requirements.

Below we provide specific responses to each of the questions you have posed.

Sincerely,

Bradley M. Shuster

cc: Bob Ryan
Prasant Sar
Garret Hartzog
(Separate letters to Rob Schaefer and Gina Healy)

A. Business Requirements

1. *Scope of Business:*

   a. *How can the PMIERs ensure that Approved Insurers have long-term access to staff, services and technology that meet their operational needs for administering their insurance book of business?*

   We feel the PMIERs will help ensure Approved Insurers have long-term access to staff, services, and technology, by restoring credibility to the industry through ensuring Approved Insurers operate in a safe and sound manner and are sufficiently capitalized to survive economic shocks. Removing uncertainty regarding the financial strength of Approved Insurers, and creating well defined requirements, helps attract resources.

   b. *How can the PMIERs ensure that potential losses from insuring high-risk loan concentrations do not jeopardize an Approved Insurer's financial ability to pay claims on its lower risk portfolio?*

   The PMIERs should be designed to ensure Approved Insurers can pay all claims, not just those on low risk loans. Also, insured loans are not bifurcated into low and high risk – Approved Insurers insure loans across a continuum of risk.

   However, in their present form, we are concerned the PMIERs will not achieve the goal of ensuring all claims are paid, but instead could set improper incentives for the industry to take undue risk in some areas, while backing away from acceptable risks in other areas. We believe that a few small but important changes to the PMIERs will greatly increase the likelihood that Approved Insurers will have adequate claims paying ability moving forward.

   Whether or not this is intended or desired, the Financial Requirements will not only be used by the Enterprises to measure financial strength, but also internally by the Approved Insurers to determine pricing/premium adequacy. As such, the requirements will influence pricing behavior in the industry.

   With this in mind, while the Required Asset tables in the PMIERs are a step in the right direction toward risk-based Financial Requirements, we feel a bit more complexity would add a lot more security. Specifically, on newly insured loans covered by Table 3, we feel it would be prudent to add additional required asset multipliers based on loan-level risk features in addition to FICO and LTV. To be specific, we would recommend that the PMIERs apply Table 3A to all newly insured loans, including those sold to the Enterprises, after appropriate adjustments are made.

   Table 3A should be modified so that it contains risk multipliers (which may be less than or greater than 1.0) consistent with the underlying performance characteristics and excluding any punitive or judgmental add-ons. Table 3A should be modified to include variables the Enterprises themselves price for and exclude any variables they do not price for. Besides non-Full Doc, non-owner occupied, and not fully amortizing loans, additional asset multipliers should be applied for ARMs, cash-out refinances, manufactured homes, multi-unit properties and for loans that are not subject to Independent Validation (as defined in each MI's post 10/1/2014 master policy). A multiplier less than 1.0 should be applied for loans with 15 year terms.

DTI should be excluded from the multipliers because it is not included in Enterprise or MI pricing.

Although the Financial Requirements already require that some of these risk features lead to higher required assets for loans not sold to the Enterprises, the additional risk from these features is no less present in loans that are sold to the Enterprises. Evidence of this additional risk is reflected by the Loan Level Pricing Adjustments / Delivery Fees charged by the Enterprises themselves for such risk features. Presumably these additional charges are borne from the additional risk these features present to the Enterprises.

Prior to the crisis, the MI industry's capital was largely governed by the Rating Agencies, specifically by Standard and Poor's MI capital model. The S&P capital model was not without its merits, but its major weakness was its lack of appropriate adjustments for stress losses for additional risk features. As the MI industry insured loans with additional risk features, such as those with Limited Documentation, or Interest Only features (some of which were sold to the Enterprises), the S&P model did not increase the stress loss estimate for those features, instead assuming they would perform under stress like an equivalent loan without those additional risk features. History has shown that assumption was incorrect. It would be unfortunate if the PMIERs Financial Requirements repeated the mistakes of the past by ignoring risk features on insured loans.

The new Financial Requirements should not only measure financial adequacy to support a given amount of risk-in-force today, but also create appropriate incentives for Approved Insurers taking on new risk. The added complexity of adding a few additional asset multipliers for risk features, and applying them to all newly insured loans will, we believe, create benefits far exceeding the minimal additional compliance cost to the industry, and will discourage the industry from taking on excessive amounts of high risk loans. This in turn will ensure that Approved Insurers can pay all claims, regardless of the relative risk level of the loans they insure.

c. *Should Approved Insurers have separately funded affiliates for insuring higher-risk products?*

If the PMIERs are properly designed, we do not feel it is necessary, nor desirable, for Approved Insurers to have separately funded affiliates for insuring higher-risk products. Regardless of where risk is held, there should be sufficient sources of funds available to pay claims in a stress scenario. Adding granularity to the required asset calculation for new production, as we recommend in our response to Question 1b, will ensure required sources of funds will be sufficient regardless of the risk profile of the insured book.

2. *Should the adequacy of each Approved Insurer's risk-adjusted rates of return be measured? If so, what would be the appropriate calculation method for this measure?*

While we understand the Enterprises' concern with inadequate risk-adjusted rates of return, we believe that directly regulating returns is a near-impossible task. Returns are a function of not just required capital/assets, but also premium rates, expected frequency of claims, expected severity of claims, expenses (both direct and allocated), prepayment rates, investment income, and expected tax rates, among other things. Any one of these assumptions could be altered by an Approved Insurer in a number of ways, and it would be difficult for the Enterprises to question those assumptions and thereby question the adequacy of returns.

However, we believe that with small adjustments to the PMIERs as we suggest, the need to monitor returns directly would be diminished, if not eliminated.

As we mention in our response to Question 1 b., designing the PMIERs so required assets for new production reflect all risks of all insured loans, whether or not sold to the Enterprises, is an important step in ensuring adequacy of risk-adjusted returns.

Additionally, we feel there should be credit given to future premiums as a source of funds / available assets. The exclusion of any credit for future earned premiums for newly insured loans is puzzling to us. Recent experience shows that in runoff, the premium generated by a mortgage insurer is a significant source of claims paying ability.

For example, Triad Guaranty Insurance Corporation (NAIC #24350) was forced to cease accepting new business as of 7/15/2008. At that time, Triad had roughly $930M in available assets, as defined in the PMIERs. From 7/15/2008 through 12/31/2013, Triad has collected over $860M in premiums, a source of funds that has gone to help pay all claimants, including the Enterprises.

The stated goal of the PMIERs is "to mitigate future Enterprise losses, ensure that Approved Insurers maintain sufficient financial strength to withstand a stress macroeconomic scenario and, to the extent possible, create a common set of eligibility requirements for Approved Insurers". The Enterprises have stated that an additional goal is to ensure Approved Insurers avoid state regulatory action; specifically, to avoid the imposition of Deferred Payment Obligations. We respectfully question the appropriateness of this goal since preventing state regulatory action is outside the control of the FHFA or the Enterprises. The Financial Requirements should, we believe, be designed to ensure that an MI will be able to pay all of its claims over a reasonable timeframe if it is subject to regulatory action.

Also, even assuming an Approved Insurer becomes subject to regulatory action, there is a significant lag between the appearance of financial distress, and corrective actions that may result in a deferred payment obligation. Substantial premiums are generated during that lag, premiums that can be used as a source of funds to pay claims.

For example, Triad was clearly in financial distress prior to 7/15/2008. From a level of $56 in early 2007, its parent company's stock price declined to under $7 by November 2007. By April 2008 its rating had been downgraded from AA to BBB. Finally, in July 2008 it stopped accepting new business. But even after it ceased accepting new business, the Corrective Order from the Illinois Director of Insurance ordering Triad to institute a deferred payment obligation was not effective until 6/1/2009. So nearly two years after financial distress was evident, Triad was finally ordered to defer claim payments. Just in the period between 7/15/2008 and 6/1/2009, Triad collected premiums of roughly $230M, roughly 25% again of its available assets as of 7/15/2008.

We also note that Triad Guaranty was an extreme example of a severely weak industry participant. PMI Mortgage Insurance Co. and Republic Mortgage Insurance Company took much longer to fail after financial distress first became evident. PMI lost its AA rating in April 2008, and RMIC in July 2008, but neither company was placed into runoff until mid-2011, over three years later. In the interim both companies continued to collect premiums, and of course both continue to collect premiums today.

Even in the case of regulatory action that curtails claims payments in the short term, the Enterprises may be made whole eventually. RMIC is now paying 100% of each approved claim, and has paid all of their deferred claims. Triad started paying 60% of each claim; it is now paying 75%. PMI started paying 50%, and is now paying 67% (and in both cases, past curtailments were trued-up to the new percentage). It is possible that both Triad and PMI will increase this payment in the future. This ability to increase claims payments is due primarily to the premiums these companies have collected in runoff.

Mortgage insurance companies are not banks. They are not subject to bank runs. Their sources of funding are secure for the intermediate to long term. They don't collapse suddenly, but rather run off over many years. Their financial strength should not be measured as if they are banks. Mortgage insurers can count on contractually mandated premium income to pay contractually mandated claims, long after regulatory action becomes necessary.

There is another important reason to include some level of future earned premium as an available asset, directly related to the question at hand, and that is to create a disincentive for Approved Insurers to accept inadequate returns. It appears the Enterprises are concerned with ensuring Approved Insurers price their insurance to generate adequate returns, but as we stated, regulating returns directly is a near impossible task. However, including future earned premium as an available asset can provide the PMIERs with an important self-regulating mechanism.

As an example, envision a situation where all Approved Insurers have the same filed premium rates, and assuming similar expense structures and identical Financial Requirements, all returns should be roughly equal. Now imagine, in an attempt to capture market share, one of the Approved Insurers reduces its premium rates by 10%.

Under the proposed Financial Requirements, this Insurer would suffer no immediate impact to its returns; the impact would only be felt as premiums were earned over time. In the meantime, this now-weaker counterparty could improve its market share and further increase the counterparty risk to the Enterprises.

In contrast, assume the PMIERs do recognize future premiums on new production as a claims paying resource. An insurer reducing premium rates will experience an immediate reduction in return on new business, as its minimum required assets would need to increase as a result of lower future premium.

We feel that the inclusion of some level of future premium is a better solution to regulating returns than trying to monitor returns directly. Even the lowest returns can be justified by altering assumptions, and different Approved Insurers may naturally have different return targets. We propose the calculation of Available Assets includes i) two years of monthly premiums (measured by {written premiums from the most recent quarter} x 8), and ii) 50% of the non-refundable unearned premium reserve (UPR), which is approximately two years' worth and therefore equivalent to the amount of monthly premium credit.

We have reviewed the report, Putting Mortgage Insurers on Solid Ground, released by Moody's Analytics in August and we believe that the following two limitations on credit for future premiums suggested in the report are reasonable:

- **Future premiums should not count for more than one-third of a MI's Available Assets, and**
- **Future premiums should not be counted at all if an MI's non-premium Available Assets falls below $400 million.**

While we do recognize that giving credit to future premiums would lead to a reduction in required on-balance sheet assets, the impact would be partially mitigated by adding the risk feature asset adjustments we recommend in Question 1b above.

Taken in concert, these changes would add minimal complexity, and if properly calibrated would leave the measurement of financial strength little changed, but would create both a more accurate assessment of Approved Insurer financial strength and a set of self-regulating Financial Requirements.

3. *If the Enterprises, in the interest of establishing strong counterparty financial requirements, expect an Approved Insurer to maintain "adequate" risk-adjusted rates of return for New Insurance Written (NIW), what might be benchmarks for the Enterprises to establish a reasonable range of such expected returns? Should the new benchmark also be inclusive of the Approved Insurer's entire portfolio of Insurance in Force (IIF), or only a defined portion?*

As we have mentioned above, we are of the view that the GSEs should not regulate risk-adjusted rates of return; rather, the Financial Requirements should be adjusted to not only better reflect an Approved Insurer's true claims paying ability, but also to create the proper incentives to discourage risk-seeking behavior that may jeopardize the Approved Insurers' ability to pay claims. By including additional required assets for risk attributes beyond FICO and LTV for all newly insured loans, and including some provision for future earned premiums, Approved Insurers will have a much greater incentive to adequately price for the risk they are taking.

4. *What counterparty risks might be raised by an Approved Insurer maintaining inadequate risk-adjusted rates of return on capital across its expected business profile?*

The counterparty risks of an Approved Insurer maintaining inadequate risk-adjusted rates of return are material. Besides the obvious risk that the Approved Insurer participating in this conduct would in and of itself represent an increased counterparty risk through the generation of inadequate resources to pay claims, it may also lead other Approved Insurers, in attempts to maintain market share, to accept inadequate risk-adjusted rates of return. This risk is not just theoretical; we observed such behavior during the recent housing bubble.

Also, as recent history also shows, should other Approved Insurers exercise restraint and not lower risk-adjusted returns in response to a competitor, they risk losing market share, and the offending Insurer will increase market share, which also exacerbates the risk to the Enterprises. Clearly some measures should be taken by the Enterprises to minimize this behavior.

However, as we have mentioned above, we do not believe that directly regulating returns is an achievable goal. The Enterprises should be concerned with ensuring their claims can be paid in a stress environment. By assessing appropriate multipliers for all new production with additional risk features, and giving credit for future earned premiums, the PMIERs will be better designed to deter Approved Insurers from unjustifiably reducing premiums or taking uncompensated risks.

5. *Should an Approved Insurer be required to validate a third-party AUS prior to using the recommendations from these systems? If so, what type of analysis would be appropriate to sufficiently validate that the credit decisions from the AUS are in line with the Approved Insurer's credit underwriting requirements?*

   No. When a model is validated, it is to determine how well it 1) segregates good risks from bad risks and 2) rank orders risk.

   We do not use the recommendations from any third-party AUS as a substitute for our own credit policy and underwriting decision making. We refer to decisions rendered by the AUS to confirm to lenders that our credit policy and underwriting guidelines are currently closely aligned to the credit policy and underwriting guidelines embedded in each GSE's AUS. We then direct the originating lender to the appropriate National MI underwriting guidelines which must be met in order for a loan to qualify for our mortgage insurance . For loans that qualify under our AUS eligible guidelines, National MI will accept GSE documentation and soft guideline eligibility with specific overlays.

   We believe that the other MI industry participants have a similar policy. Therefore, each MI must be aware of any changes to the policy or guidelines embedded in an AUS system which could lead to a divergence of its credit policy from that of the particular AUS. The most efficient way to ensure that this divergence doesn't occur is for an MI to underwrite every loan it insures. This is National MI's policy which gives us the immediate ability to observe any changes that occur to DU or LP.

6. *Are there other Approved Insurer operational performance scorecard metrics that should be considered?*

   We have no additional suggestions at this time.

7. *How should Operational Performance Scorecard thresholds be determined?*

   Thresholds should only be set for scorecard metrics with corresponding requirements established within the PMIERS (e.g., pay/deny/rescind within 180 days of claim perfection per Section 309 or use statistical QC sampling with a 95% confidence/2% margin of error/annual confidence per Section 503). Target expectations should mirror the minimum requirements established within the PMIERS and the threshold should be that the target is met 95% of the time (with the calculation as described in our response to question A.9).

8. *How should Approved Insurers be rated under the Operational Performance Scorecard?*

   For each metric contained in the Operational Performance Scorecard where there is an

established threshold, the MI should be rated as "pass" or "fail". Each fail should then be rated as low risk, medium risk or high risk based on how the failure is likely to affect the MI's ability to pay claims over the lifetime of the insured portfolio.

9. *How should Operational Performance Scorecard thresholds be applied?*

   The scorecard metrics consist primarily of percentage calculations. This works well when large numbers are involved, but less well when percentages are calculated on a small number of observations where a single observation can cause a significant percentage change or fluctuation. To address this shortcoming, we suggest that an MI be measured against a threshold once a sufficient number of observations are present and subsequently, using a trailing 3 quarter average. The remediation process proposed within the PMIERs is reasonable.

B. Newly Approved Insurer Requirements

10. *What would be the impact of the $500 MM requirement for newly Approved Insurers? Should the requirement reflect the start-up costs to scale a competitive mortgage insurance business? Are there other appropriate requirements or controls that should be established to ensure that start-ups are held to more stringent requirements?*

    We believe the $500 MM requirement is appropriate for Newly Approved Insurers and that the amount is adequate to cover operational costs and initial capital requirements of a new mortgage insurance company.

C. Settlements and Changes to Enterprise Rights

11. *Section 307 contains requirements relating to the ability of Approved Insurers to enter into agreements with servicers or originators. Should the PMIERs contain provisions relating to agreements entered into between Approved Insurers and originators or servicers? If so, what provisions should be in place?*

    We believe the requirements in Section 307 are appropriate. As the Insured on Mortgage Insurance policies covered by Approved Insurers, the Enterprises should have the right to approve any agreements affecting their benefits under those policies.

D. Claims Processing and Loss Mitigation

12. *Should the Enterprises impose pricing adjustments for acquired loans where an Approved Insurer does not provide a full delegation of loss mitigation? Does a lack of full delegation unnecessarily expose the Enterprises to foreseeable costs? Should there be exceptions to what constitutes full delegation of loss mitigation?*

    The Enterprises should be free to impose pricing adjustments for loans acquired or guaranteed that do not have delegated loss mitigation from a mortgage insurer. The lack of full delegation exposes the Enterprises to additional time to negotiate and wait for responses from an MI and the extra time amounts to extra costs. The lack of full delegation could also result in missed opportunities regarding loan modifications or property sales which could result in additional costs

or foregone recovery. We don't believe there should be an exception to full delegation of loss mitigation.

E. Policies of Insurance

13. Should self-insurance be an appropriate method for Approved Insurers to meet the requirements for Fidelity Bond and E&O insurance?

No.

F. Quality Control

14 What are the relative costs and benefits for Approved Insurers to implement the draft quality control requirements in the PMIERs?

The QC requirements are generally consistent with best practices and could be implemented with minimal incremental costs, provided the following items are addressed:

a) The timeline for completing the quality control process for loans that have been independently validated should not begin until the independent validation is complete. Therefore, the QC file review completion period of 120 days in section 502 should be modified to begin from the month end during which insurance coverage becomes effective for non-delegated loans (underwritten by National MI) and from the month end during which the independent validation is completed for delegated loans.

b) Section 504 requires "immediate reporting to senior management in the event that fraud is suspected" and the glossary defines senior management as the CEO, President, etc. It is not useful or practical to conduct such reporting every time fraud is suspected (i.e., "red flags" are present, but have yet to be investigated). PMIERs should remove this requirement and replace it with one that states the MI must have and adhere to an appropriate policy governing the evaluation of suspected fraud and its investigation to a final determination. (We note that as an insurance company National MI is required to adopt and file an anti-fraud policy in several states).

Additionally, in several places the PMIERs are very specific about the timing of reporting to senior management. Given how senior management is defined, it is recommended that more general terms (such as "appropriate") be used rather than the proposed specific timelines.

15. Do the draft quality control standards present any unintended consequences?

We do not believe so.

G. Financial Requirements

Grids

16. *What comments or suggestions are there related to the grid framework for performing loans in calculating the Financial Requirements?*

    We feel the grid framework for performing loans is a good foundation for achieving the goal of providing Financial Requirements in an understandable and transparent way. While more complex models could be used that perhaps add more accuracy in measuring default risk, for this purpose we do not believe the additional complexity, loss of transparency, and model risk are worth the tradeoff. It is important that the Financial Requirements not only accurately gauge counterparty risk, but do so in a transparent way so all interested parties can understand and comment on the proposed measures.

17. *What comments or suggestions are there related to including LTV and Credit Score as the primary factors in the grid framework for performing loans?*

    LTV and Credit Score are the two most important drivers of default risk, and the two factors present in every loan; we agree that basing the grid framework for performing loans on these two factors is appropriate.

    We would like to recommend, however, that the credit score dimensions have greater granularity, particularly for newly originated loans covered by Table 3. We note that the Enterprises' own LLPA / Delivery Fee grids divide Credit Score into 20 point wide categories (e.g. 620-639, 640-659, etc); we believe that a similar refinement to the grid in Table 3 would be appropriate.

    Consistent with our desire to ensure that the Financial Requirements promote prudent behavior, we feel that increasing the granularity of the Credit Score classifications in Table 3 would create better incentives, while adding little additional complexity. In particular, we believe the 621-680 and 681-740 Credit Score classifications need to be further subdivided. The default rate under stress of a borrower with a Credit Score of 621 at origination can be 2X or more higher than a borrower with a Credit Score of 680.

    Also, as a practical matter, it would be helpful if the Credit Score classifications started on multiples of 20 (e.g. 620-639, 640-659, etc), to better align the Financial Requirements with how Approved Insurers and the Enterprises categorize risk (and as an extension, price risk).

18. *What comments or suggestions are there related to the treatment of HARP loans in calculating the Financial Requirements?*

    The treatment of HARP loans will not affect us; therefore, we have no comment on their treatment at this time.

19. *What comments or suggestions are there related to the treatment for non-performing loans in calculating the Financial Requirements?*

We believe non-performing loans should be treated differently than performing loans, given the increased certainty of claims given a default. Regarding the proposed factors, while we feel there may be an opportunity to moderate these somewhat, we understand that a source of the uncertainty regarding the proper factors is the fact that a large number of serious delinquencies from the housing crisis have yet to be resolved. We recommend that these factors in particular be revisited frequently over time, as today's serious delinquencies are resolved as either cures or claims.

Also, to the extent a delinquent loan is in a modification program, we believe there should be separate treatment of that loan. Loans in trial modification programs may continue to show as delinquent until the trial period is complete. To assume these loans have a high probability of going to claim is in direct opposition to the goal of these modification programs—that of keeping homeowners in their homes. It would be inconsistent with this goal if Financial Requirements are adopted in the PMIERs that treat loans in modification programs the same as non-performing loans.

However, we feel strongly that there is a need for a standardized approach to assessing the risk of non-performing loans, one based on actual performance of settled delinquencies. We have observed a large discrepancy around the cure rate assumptions for non-performing loans across MI industry participants. Such large discrepancies not only increase risk for the Enterprises under the current statutory capital rules, but call into question the validity of these assumptions for some Approved Insurers, and in turn tarnish the reputation of the industry.

While each MI is free to work with its actuaries to determine the treatment of delinquent loans in setting its loss reserves, this treatment should not be allowed to influence PMIER Financial Requirements. The Enterprises should have a clear and consistent treatment of delinquent loans for all Approved Insurers.

20. *Is the segregation of books of business by vintages appropriate?*

Yes, we believe it is appropriate to segregate books of business by vintage. In today's environment, older vintages are obviously higher risk than more recently originated vintages, as a result of house price depreciation in most housing markets. In the future, today's vintages may present lower default risk due to house price appreciation. Whatever the case, there is information to be learned through the aging of books of business, information which can be applied in assessing default risk. In contrast, with newly originated business, one must rely mostly on future projections of performance.

However, we would like to see more clarity on the potential treatment of vintages as they age, perhaps through some sensitivity analysis of the FHFA's Mortgage Analytics Platform. For example, we would expect that as today's insured loans age through an expected benign economic environment, the conditional probability of stress claims will decline. However, the extent of that decline under different scenarios would be useful to understand. While knowing the required assets for an insured loan at origination is necessary to determine premium rates to generate adequate returns, it is not sufficient in and of itself. Rather, it is necessary to understand how the required asset factor will develop over time. Without this information, determining appropriate

premium rates is very difficult, if not impossible.

21. *How often should the grids be updated?*

    Broad trends in credit risk do not change materially over the short run, but as evidenced by the recent housing bubble, risk drivers can shift over time. In attempting to balance the need for accuracy versus the disruptive effect that frequent changes would have on the ability of industry participants to do capital planning and maintain appropriate pricing, we feel a 36 month refresh cycle for the treatment of newly originated loans is reasonable.

22. *What comments or suggestions are there related to employing a remaining life of coverage loss horizon in calculating the grids?*

    We feel that employing a remaining life of coverage loss horizon is appropriate, given that it reflects the risk faced by the Approved Insurers in issuing coverage. We reiterate that these tables should represent conditional probabilities, and as such should be updated to reflect the current risk posed by insured loan cohorts as they age.

23. *What comments or suggestions are there related to the use of multipliers for certain loans with certain high risk features?*

    See our response above in Question 1B. We believe the multiples should be extended to more risk features, and applied to all loans, regardless of end investor.

    Prior to the crisis, the MI industry's capital requirements were essentially regulated by Standard and Poor's through their Risk-Based Capital Model. This model was developed in 2001, and we believe it was structurally sound; as it attempted to measure the sources of funds under a stress scenario versus the uses of funds. Fundamentally, we believe this is the correct approach.

    However, where it failed was in its ability to accurately measure stress losses as driven by risk layering – the model only assessed risk on four dimensions: FICO, LTV, Vintage, and Fixed vs ARM. There were no penalties for Occupancy, Loan Purpose, Documentation, etc. As such, the model failed to identify the additional risk layering the industry insured during the housing bubble.

    We believe it is important that the Financial Requirements recognize the additional risks embedded in these loan characteristics.

24. *It is common underwriting practice to consider additional factors that help reduce or offset risks associated with higher DTIs (often described as compensating factors). Should the Enterprises take compensating factors into consideration when determining risk multipliers as described in Exhibit A, table 3a? How should compensating factors be incorporated into table 3a?*

    As stated in our response to earlier questions, we believe that an expanded list of loan-level risk features (excluding DTI) such as those in Table 3A should be developed and applied to all loans. In this scenario, some features may have multiples less than 1.0 and others more than 1.0. To the extent additional risk features are incorporated into the determination of risk-based required

asset amounts, the need to separately incorporate compensating factors into the calculations becomes unnecessary and redundant. Therefore, we do not recommend that compensating factors be separately incorporated into the calculation of risk-based required assets.

Compensating factors generally exclude variables that are factored into pricing unless there is a broad pricing band (e.g., a 60 point FICO band rather than a 20 point band) and the loan falls near the low end of the band from a risk perspective. While the evaluation of compensating factors is an important component of the underwriting process, compensating factors are often best captured via narrative. Because it will be difficult to sufficiently and consistently capture, quantify and report for the purpose of determining risk-based required assets how compensating factors impact individual underwriting decisions, the list of potential compensating factors is further limited.

If a decision is made to incorporate compensating factors in some fashion, there are a few variables that are excluded from pricing and quantifiable. Assuming DTI is not factored into pricing (or risk-based required assets), DTI below the maximum may be considered a compensating factor (e.g., 10% or more below the maximum). Or alternatively disposable income (gross monthly income multiplied by (1-DTI)) could be a compensating factor (e.g., > $4,000 per month). High verified reserves may be another compensating factor. If these compensating factors were present, one or more risk factor multipliers would not need to be applied or the risk-based asset amount for the loan would be limited in some way.

25. *An alternative would be to have several DTI risk multipliers, for example, 43%, 45%, 47% and greater than 50%. What are the merits or drawbacks of this approach?*

As is the case with GSE LLPAs, key risk variables that drive pricing should be readily determinable (e.g., loan amount, property type, occupancy type, loan type, amortization term) or obtained by independent third parties (e.g., FICO score, appraised value driving LTV). DTI is not such a variable – presumably this is why the GSEs do not price by DTI. Building MI capital requirements based on DTI is asking the MIs to price by DTI, but it is not a good idea no matter who does it. The calculation of DTI depends upon many variables and calculations that are subject to "management" including the sufficiency of income documentation, calculation of income from the documentation, debt balances, debt payment amounts and other factors.

Creating pricing incentives for borrowers driven by small changes in these calculations will rightly cause borrowers and mortgage originators seeking to maximize the benefits to their borrowers to find ways to drive down DTIs. The additional work to minimize DTI among a subset of borrowers who already qualify is not productive from an operational perspective and likely to increase the frequency of underwriting errors and audit findings.

Macroeconomic Scenarios

26. *What comments or suggestions are there related to using the house price, interest rate and unemployment rate projections from the CCAR Baseline scenario for calculating the grids for Pre-2009 and delinquent policies?*

While we understand the desire to capture the concept of "credit burnout", we disagree with the approach of using a milder stress scenario for different vintages. By definition, an Approved Insurer can only experience one stress environment at a time. A better approach would be to subject all books of business to the same stress scenario, and if believed appropriate, to apply a "credit burnout" factor to older vintages. While estimating this factor may be difficult, in our opinion this is a more logically defensible, and more transparent, approach.

27. *What comments or suggestions are there related to using the house price, interest rate and unemployment rate projections from the CCAR Severely Adverse scenario for calculating the grids for non-HARP Post-2008 policies?*

We feel this is appropriate.

28. *What comments or suggestions are there related to using the house price, interest rate and unemployment rate projections from the CCAR Baseline scenario for calculating the grid values for loans refinanced through HARP?*

Again, we feel it is better to apply the same stress scenario to all exposures, and then apply adjustment factors if deemed appropriate.

Available Assets

29. *What is the appropriate frequency for an Approved Insurer's senior management team to certify compliance with the available and minimum required asset provisions of Section 704?*

Annually

30. *What suggested changes are there to the categories either included or excluded from the definition of Available Assets?*

We propose that credit be given for two years of monthly premiums (measured by {written premiums from the most recent quarter} x 8) for monthly pay products, and 50% of Unearned Premium Reserve for single and annual products, subject to the limitations we noted in our response to question 2. Using the most recent quarter's written premium captures the most recent run rate for a company whether it is experiencing growth or decline in NIW.

While the eventual premium stream from a company in runoff will likely exceed two years of written premiums (as witnessed by Triad Guaranty, who, since 7/1/2008, has already collected three times the premium it collected in the twelve months prior to 7/1/2008), we feel that two

years is sufficiently conservative to solidify an Approved Insurer's financial strength, but long enough to discourage return-reducing behavior.

Other than this inclusion, we agree with the approach taken. There are many assets that are currently admitted as statutory assets that provide questionable claims paying resources. To the extent the Financial Requirements exclude those assets it strengthens the ability of the PMIERs to properly assess the true economic strength of Approved Insurers.

31. *What comments or suggestions are there related to the proposed treatment of premium income in Available Assets?*

    As mentioned above, there is ample justification for including future earned premiums for all business. Additionally, including future premium will help alleviate concern regarding inadequate risk-adjusted returns, by immediately penalizing those who reduce premium rates.

    We do not believe there is any justification for treating future premiums from different vintages differently. Either future premiums should be included on all business, or excluded entirely. Inclusion of premiums for only select business undermines the credibility of the model.

32. *Should the proposed treatment of premium income in Available Assets be aligned with the exclusion of premiums that currently occurs as part of state regulatory calculations?*

    There are many things in the proposed Financial Requirements that are not aligned with state regulatory calculations; therefore, we do not feel that the issue of credit for premium income should be singled out. Nevertheless, we would point out that the most common state regulatory capital limit is a risk to capital ratio in excess of 25:1, which does implicitly recognize and give credit for future premium income as a claims paying resource.

    Furthermore, when state regulators weighed taking action on Insurers during the financial crisis, the Insurer's entire claims paying ability, including future premium streams, was considered. Not every Insurer who exceeded statutory capital ratios was subject to Corrective Action and/or Receivership. It was only when regulators believed future uses of funds would exceed future sources of funds that action was taken.

    If the primary goal of the Financial Requirements is to determine the economic claims paying ability of an Approved Insurer, then state regulatory accounting rules for determining a point-in-time balance sheet play little part in that calculation.

    The Financial Requirements exclude a number of Admitted Assets that are included in statutory accounting, and for the most part we agree with those exclusions. The Financial Requirements also include a significant liability which is not included in statutory liabilities – lifetime projected claims payments. Under statutory accounting, only projected claims on delinquent insured loans are counted as a liability, not projected lifetime claims on all insured loans.

However, we understand and agree with these differences, because we believe the goal of the Financial Requirements should be to ensure the Enterprises' claims are paid.

To that end, the income from future earned premium is a large, important source of financial strength in a stress scenario. As mentioned previously, Triad Guaranty in runoff has collected over $860M in premiums, money that has largely gone to the benefit of the Enterprises in paying their claims. To totally ignore this important component of claims paying ability is unjustified and inappropriate.

33. *Should premium income for the Post-2009 vintages be included in the calculation of Available Assets, and if so, should the inclusion of this premium income be limited to the transition period, or should it extend beyond the transition period? What would be an appropriate phase- out and/or haircut for premium income credit given during the transition period?*

Yes, we believe projected premium income from all vintages be included in the calculation of Available Assets, for the reasons we have detailed above. This inclusion should be a permanent inclusion. We proposed that the calculation of available assets include i) two years of monthly premiums (measured by {written premiums from the most recent quarter} x 8), and ii) 50% of non-refundable UPR, subject to the limitations previously noted.

34. *Should unearned premium reserves (UPR) be included in the calculation of Available Assets? Should there be different treatment of refundable versus non-refundable premium?*

Yes, we believe that 50% of non-refundable UPR is appropriate, to reflect the component of UPR that could be expected to be earned in the near term.

However, we caution that it is important to keep the treatment of monthly and single premiums equal, or risk the unintended consequences of tipping the usage of these products drastically in one direction or the other. For example, if credit were given for UPR, even partially, but no credit given for future premiums on monthlies, the industry would likely move to a majority usage of single premiums.

Alternative Approaches

35. *Should an alternative approach to determining Minimum Required Assets be considered in the future? If so, please describe the approach.*

We feel the framework set forth, with appropriate adjustments as recommended above, is a good start. While greater accuracy may be achieved through more complex modeling, the added accuracy would most likely sacrifice transparency. We believe that the proposed framework strikes an appropriate balance between accuracy and transparency. Confidence is an important attribute during a financial crisis, and if interested parties feel secure that an appropriate, strict, and transparent standard has been applied to determine counterparty strength, they will more likely remain confident in that strength, versus relying on a more opaque and less easily understood standard.

Limitations Triggered by a Minimum Required Assets Shortfall

36. *What comments or suggestions are there related to the limitations triggered by an Available Assets shortfall to the Minimum Required Assets Amount described in Section 706 if they were expanded to include:*

    a. *Paying dividends, making any payments, or pledging or transfer asset(s) to any affiliate or investor; and*

    c. *Assuming any obligations or liabilities other than those arising from mortgage guaranty insurance policies.*

    The limitations listed above, as well as those in the draft, are appropriate.

Risk Sharing and Reinsurance

37. *Should risk sharing or reinsurance transactions that do not receive full credit for the risk transferred under GAAP or SAP be permitted, and, if so, what limitations should there be on such transactions?*

    In the interest of designing the Financial Requirements so the Enterprises can accurately predict an Approved Insurer's claims paying ability, the Enterprises should provide more information about what factors will determine when and if reinsurance transactions receive credit.

    Statutory requirements with respect to credit for reinsurance vary by state. For example, one state previously gave no credit to foreign reinsurers. Therefore, the absence of risk transfer credit under SAP should not automatically cause the Enterprises to also withhold risk transfer credit.

    In our experience GAAP accounting usually mirrors true risk transfer, but there could be cases where it would not allow risk transfer treatment even when true risk transfer has been achieved. If there is dispute between a mortgage insurers and one or both Enterprises over the issue of true risk transfer for a transaction, the issue could be resolved if a qualified third party firm was willing to write a strong opinion affirming risk transfer based on sound actuarial analysis.

38. *What would be the impact of the draft Financial Requirements, if any, on Approved Insurers who are considering writing pool level insurance on pools with LTVs below 85 percent?*

    The Financial Requirements as drafted, along with the recommendations we have proposed, would treat all risks fairly and equitably. We recommend, however, that the tables be further extended for LTVs below 85 percent, to reflect the reduced risk as LTVs are decreased. As well, reflective of these reduced risks, we recommend the 1% floor on the required asset factor be removed for these LTV ranges. In addition, the overall minimum asset charge of 5.6% will need to be adjusted lower if insuring <80 LTV loans becomes more common.

Third-Party Opinions and Risk Analytics

39. *Should the requirements of a third party opinion or analysis in Section 703 be restricted to a particular purpose, triggering event, and/or frequency?*

We recommend that the purpose of the third party opinion be a granular sources and uses runoff analysis of the mortgage insurer. The analysis should take all revenue and expenses into account to determine if the MI can pay its claims over the ensuing ten years. The analysis should include several scenarios with varied interest rate, portfolio persistency, housing price and unemployment assumptions. The analysis should seek to determine if the MI can pay its last claim over the period with its last dollar of assets or revenue rather than seek to guess at what point the MI might be subject to regulatory action.

We believe that the triggering event for such a study should be the determination that an MI has entered into either the Medium or High risk category referred to in Section 802. The analysis should be conducted annually as long as the MI is classified as Medium or High risk.

Overall Impact

40. *What may be the impact, if any, on high LTV borrowers of the draft PMIERS?*

If all risks are treated in a logical and consistent way, all LTVs would be treated fairly. If our suggested changes are implemented, we do not believe we would need to make any material changes to our current filed premium rates.

41. *What may be the impact, if any, on low credit score borrowers of the draft PMIERS?*

If our suggested changes are implemented, we do not believe we would need to make any material changes to our current filed premium rates.

42 *What may be the impact, if any, on Seller/Servicers of the Financial Requirements?*

As we are not a Seller/Servicer we will not speculate on any impacts to them.

43. *What may be the impact, if any, of the draft PMIERS on Approved Insurers who are considering writing forms of insurance that are different from the traditional loan-level, borrower-paid mortgage insurance (BPMI)?*

It is difficult to assess the impact of the PMIERs on non-traditional forms of insurance; therefore, we ask the Enterprises to agree to make adjustments to the PMIERs, if necessary, to accommodate new forms of insurance.

H. Failure to Meet Requirements (Post-Transition Process)

44. *Are the remediation measures sufficiently comprehensive? Should the number of measures be reduced, expanded or refined and if so how?*

Yes, we feel they are comprehensive and do not need to be expanded.

45. *Do the remediation measures present any unintended consequences or operational constraints?*

We do not believe so.

46. *Are there remediation frameworks that would serve as an alternative to the proposed approach?*

We feel that the proposed remediation framework is adequate.

47. *Should the PMIERs include an appeals process to provide an Approved Insurer with a means to dispute remediation actions taken by the Enterprises? If so, what should that process consist of and should it apply to all remediation actions or to a subset?*

We do not believe that any additional appeals processes need to be added.

I. Newly Approved Insurers

48. *What financial and business requirements should be placed upon new entrants? How would such requirements affect the market for mortgage insurance?*

The requirements imposed the most recent new entrants were reasonable and struck the proper balance between requiring adequate capital and expertise without presenting overly burdensome barriers to entry.

J. Transition Process

49. *What would be the appropriate length of time for Approved Insurers to fully comply with the Financial Requirements of the revised PMIERs?*

We believe that the proposed two year transition period is appropriate.

50. *Should the duration of a transition period for full compliance with the Financial Requirements of the revised PMIERs be consistent for all Approved Insurers or varied depending on each company's unique circumstances?*

The transition period should be the same for all companies.