Alfred M. Pollard
General Counsel
Federal Housing Finance Agency
Eighth Floor
400 Seventh Street, SW
Washington, DC 20219

August 31, 2020

RE: RAA Comments in Response to RIN 2590-AA95

Dear Mr. Pollard:

This letter is submitted by the Reinsurance Association of America (RAA) on behalf of and in coordination with its numerous interested members in response to the FHFA 2020 notice of proposed rulemaking ("2020 Proposed Rule"). RAA is a national trade association representing reinsurance companies doing business in the United States. RAA membership is diverse, including reinsurance underwriters and intermediaries licensed in the U.S. and those that conduct business on a cross-border basis.

INTRODUCTION

Since 2013, the reinsurance industry has supported the transfer of mortgage credit risk from government-sponsored entities Fannie Mae and Freddie Mac (collectively the "Enterprises") to our private sector balance sheets as part of their rehabilitation during government conservatorship.[1] RAA's membership includes companies across the entire value chain of mortgage credit risk transfer, from brokers to private mortgage insurers to reinsurers. We urge you to consider these comments as a complement to those submitted by individual RAA members.

Prior to the 2008 financial crisis, the Enterprises entirely retained 100% of the mortgage credit risk they accumulated until 2013, when the credit risk transfer (CRT) program began. The success of the CRT program renewed confidence in the revised practices of the Enterprises and, until FHFA's 2020 Proposed Rule, had been a priority of the FHFA. The CRT program has transferred substantial risk from U.S. taxpayers to the private sector. The objective third-party view of reinsurers and investors willing to regularly evaluate and partner in this risk also has oversight benefits far beyond government-required capital and the limits of governmental supervision.

In May 2020, the FHFA re-proposed a new Enterprise Regulatory Capital Framework, using its 2018 proposed rule as a "foundation".[2] The new proposal calls for sweeping and comprehensive changes, including changes that have severe, and negative, impacts on the capital relief the Enterprises would receive from CRT. At its core, the proposal has laudable goals and a workable

framework, but some adjustments and alternatives are needed to better achieve the FHFA's goals and preserve CRT for the benefit of the Enterprises and, ultimately, U.S. taxpayers, homeowners and renters.

EXECUTIVE SUMMARY/KEY TAKEAWAYS

As applied, the FHFA's proposed new capital framework would effectively eliminate CRT, which has been a successful post-2008 financial crisis risk management tool for the Enterprises since its inception. Disincentivizing the CRT market would result in severe consequences for the residential housing market and return the Enterprises to a "relative" of their pre-2008 model, when the Enterprises were owned by equity shareholders and retained 100% of their mortgage credit risk, resulting in substantial exposure to U.S. taxpayers. Diminishing the value of CRT would result in:

- Increasing risk of loss to U.S. taxpayers, particularly during periods of economic turmoil, such as the COVID-19 pandemic;
- Jeopardizing or delaying the Enterprises' exit from conservatorship due to the increased risk that the Enterprises will not be able to raise the unprecedented levels of equity capital required under the proposal, or at the very least, extending the time it will take to raise that capital;
- Raising the cost of housing for homeowners and renters through increased guarantee fees ("g-fees") necessary to replace the lower cost CRT capital; and
- Pushing greater risk of loss to the Federal Housing Administration (FHA), the Federal Deposit Insurance Corporation (FDIC), and potentially the Board of Governors of the Federal Reserve System (Federal Reserve).

The 2020 Proposed Rule requires the Enterprises to hold capital of at least $243 billion. This amount: is nine times the $28 billion of capital held as of August 2020; requires the Enterprises to raise additional capital that is seven times larger than the largest initial public offering in world history ($29.4 billion raised by Saudi Aramco in 2019); and is six times higher than the $43 billion Dodd-Frank Stress Act Test for the severe adverse scenario. Exclusive reliance on equity capital of that size without the benefits and diversification of CRT would be risky and expensive.

The FHFA should avoid these consequences by revising its 2020 Proposed Rule to recognize the value CRT provides to the Enterprises, homeowners, renters and taxpayers. With suitable improvement to its 2020 Proposed Rule, the FHFA can still achieve its objectives and preserve the benefits that CRT provides for the Enterprises today, including:

- loss-absorbing transfer of risk to the private sector to protect taxpayers during times of stress;
- a bridge to raise equity capital; and
- cost-effective capital relief and housing affordability.

BACKGROUND

The Enterprises are corporate entities created by Congress to extend financing liquidity for single-family homeowners and multifamily, rental property owners.[3] The impact of post-crisis reforms

is that the Enterprises no longer purchase mortgage-backed securities to hold in their asset portfolio. The Enterprises are essential to the functioning of the U.S. mortgage and housing market, however, because they finance about half of all U.S. mortgages and in the process guarantee the credit risk on those mortgages.

Excessive risk-taking and insufficient capital precipitated the Enterprises' losses during the 2008 financial crisis. The resulting losses prohibited the Enterprises from fulfilling their mission without government intervention, and as such, the FHFA placed both entities into conservatorship at substantial initial cost to taxpayers.

Following the 2008 financial crisis, under two Administrations from different political parties, the FHFA has directed the Enterprises to strengthen, diversify, and increase private capital. The Enterprises have achieved this by enlisting the private sector to provide real-time, objective, third-party feedback to help the Enterprises better evaluate, price, manage, and reduce risk,[4] through the FHFA's formation of the CRT program. CRT operates like an insurance contract, transferring a portion of the Enterprises' mortgage credit risk to private markets. Suitable application of CRT:

- protects U.S. taxpayers and Enterprise shareholders from losses;
- enhances each Enterprise's safety, soundness, and resiliency;
- provides valuable feedback to the Enterprises on credit costs and on underwriting standards; and
- supports affordable housing for homeowners and renters.

Starting in 2012, FHFA's strategic plan for the Enterprises' conservatorships first directed the Enterprises to transfer mortgage credit risk to the private sector.[5] FHFA has continued to reference this goal as recently as FHFA's June 2020 Annual Report to Congress.[6] The report also states that:

> CRT will continue to be a component of the Enterprises' approach to risk management. Continuing to transfer risk to private sources of capital both reduces risk to taxpayers and provides a measure of market discipline otherwise lacking under conservatorship.[7]

Moreover, at a recent House Financial Services Committee hearing, Treasury Secretary Steven Mnuchin confirmed the Administration believes the Enterprises should receive equitable capital relief for their CRT transactions.[8]

To date, the Enterprises have transferred over $130 billion of mortgage credit risk on over $4 trillion of single-family and multifamily mortgages through more than 200 CRT transactions.[9] Of that, $30 billion of single-family risk and $2 billion of multifamily risk was transferred to over 40 highly-rated, diversified and well capitalized (re)insurers.[10] Indeed, the Enterprises have transferred risk on the vast majority of the business they have acquired since 2013 to private investors and (re)insurers. The CRT program is in fact modeled after reinsurance catastrophe bonds that transfer peak losses from natural catastrophes.[11]

CRT is either fully collateralized or partially collateralized by highly rated, diversified reinsurers, which means that the collateralized funds are stored in trust, and therefore guaranteed to be recoverable by the Enterprises in the event of a triggering loss. The presence of this private sector risk transfer support explicitly reduces the risk of systemic defaults that can destabilize the U.S. mortgage and housing markets and financial systems during periods of stress like the 2008 financial crisis.

According to the FHFA's April 2020 Credit Risk Transfer Progress Report, "…the Enterprises purchase insurance primarily from diversified reinsurers. These transactions are partially collateralized and distributed among a variety of highly-rated insurers, reinsurers, and reinsurer affiliates of mortgage insurers, which reduces counterparty, reimbursement, and correlation risk." The report further states that "[r]einsurers are often characterized by diversified lines of business, which helps mitigate the risk that the Enterprises' counterparties are correlated to housing market stress and would have increased claims at the same time the Enterprises themselves are under stress."[12]

As recognized by the Department of Treasury, "[t]he [Enterprises'] CRT programs enhance taxpayer protection and foster price discovery and market discipline, and in light of these features, the FHFA should continue to support efforts to expand these programs."[13] Further, Treasury recommended that "FHFA should, in prescribing regulatory capital requirements, provide for appropriate capital relief to the extent that a guarantor, or a [Enterprise] pending legislation, transfers mortgage credit risk through a diverse mix of approved forms of CRT."[14]

To date, the Enterprises have $112 billion of CRT coverage limits available (combined single-family and multifamily).[15] Stress losses from a replay of the 2008 crisis would result in an estimated $41 billion of credit risk losses transferred to private CRT investors, using the CRT capital impact from FHFA's 2018 proposed capital rule as a proxy.[16]

In relevant part, the purpose of the 2020 Proposed Rule is to create a framework of incentives under which the Enterprises will operate. The rationale for the rule is three-fold: (1) position the Enterprises to exit conservatorship; (2) increase the quantity and quality of capital held by the Enterprises; and (3) mitigate pro-cyclicality. Striking a balance between protecting taxpayers from future losses and maintaining affordability are key issues to address.

BENEFITS OF CREDIT RISK TRANSFER

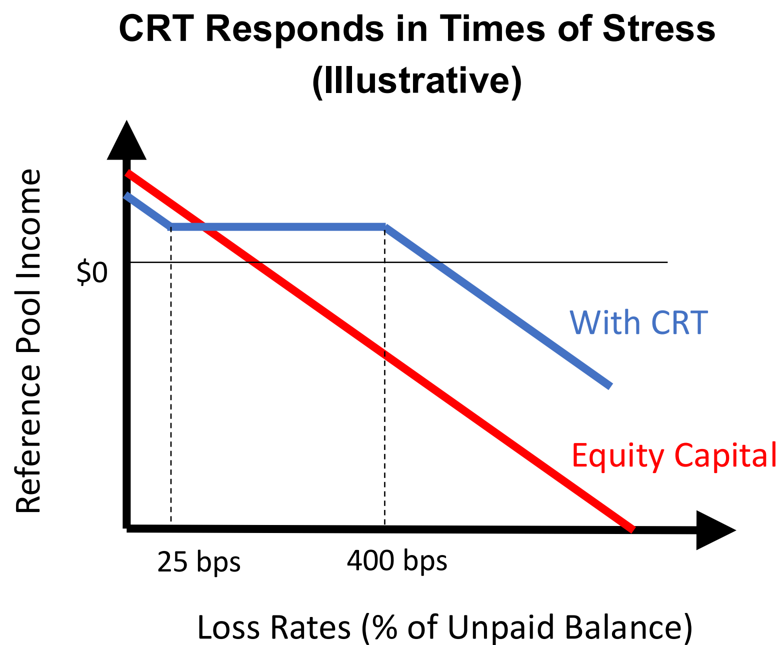
At a high level, CRT transfers mortgage credit risk from Enterprises to the private sector, protects taxpayers, and reduces costs to the Enterprises and to homeowners and renters. Through CRT, the private sector has enabled the Enterprises to become efficient distributors of risk, with a large, diverse group of private (re)insurers and investors.

CRT Protects Taxpayers (and the Enterprises)

Deteriorating economic conditions such as high unemployment or house price declines increase the possibility of future losses to taxpayers. The presence of CRT equips the Enterprises to weather

these times of distress because it transfers stress losses to the private sector, reducing earnings volatility and minimizing risks for the Enterprises.

The illustration below shows the different results for a reference portfolio with and without CRT. As the loss rate to a portfolio increases, the expected income to the pool decreases. However, the presence of CRT caps the downside to the Enterprises and results in greater certainty of income for the Enterprises. In the face of an uncertain housing market, having a reference pool that is protected by CRT effectively covers deterioration, which leads to a material benefit to the shareholders.



CRT helps to avoid financial distress in the Enterprises and the subsequent burden on taxpayers. Sudden and unexpected deterioration in credit conditions (such as those we are currently experiencing due to COVID-19) introduces a significant amount of uncertainty around the magnitude of losses, which can be reduced through the effective use of CRT. The Enterprises account for this uncertainty through loan loss provisions that are subject to development over time. Evidence demonstrates how CRT stabilizes these loan loss provisions in Freddie Mac 2020 Q1 and Q2 earnings.[17]

The presence of this effective indemnity in CRT results in a number of benefits to the stakeholders in the Enterprises. During periods of stress losses, CRT essentially creates a "capital call" that causes capital to flow from (re)insurers to the Enterprises in periods where debt and equity capital costs are highest. As a result, CRT reduces the volatility of earnings and thus the volatility of capital.

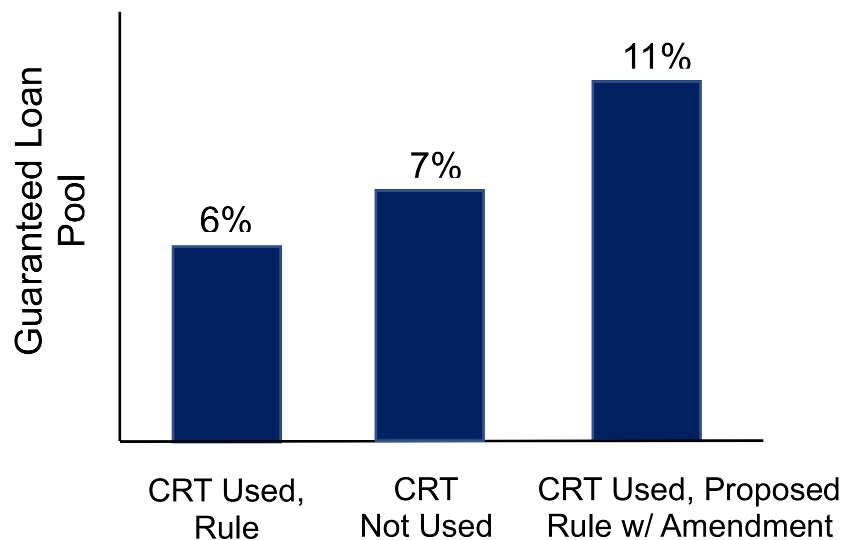
CRT Supports Effective Management of Liquidity Risk

CRT also provides an effective source of feedback to the Enterprises about risks contained in the portfolio. If reinsurers see underwriting or credit conditions deteriorating or the Enterprises increasing the risk in their new guarantees, reinsurers will respond with live pricing feedback of products to the Enterprises, which has a material benefit to the risk management teams in the Enterprises.

Reinsurers that participate in CRT are fully subject to solvency regulation by state insurance departments to the same extent and in the same manner as insurance companies. Because of collateralization and regulatory oversight of reinsurers, counterparty risk is de minimus.

CRT Better Positions the Enterprises to Raise Capital

CRT better positions the Enterprises to raise the capital they need to emerge from conservatorship. CRT can act as a bridge to the private capital the Enterprises need to raise, both by reducing the overall level of equity capital they need to raise initially, and by helping to attract the necessary capital by improving Enterprise returns through the use of lower cost CRT capital. Given the extraordinary scale of the capital raise contemplated by the 2020 Proposed Rule, maintaining the incentives to use CRT and the benefits that derive from it is essential.



Sources: FDIC, Bloomberg, Guy Carpenter

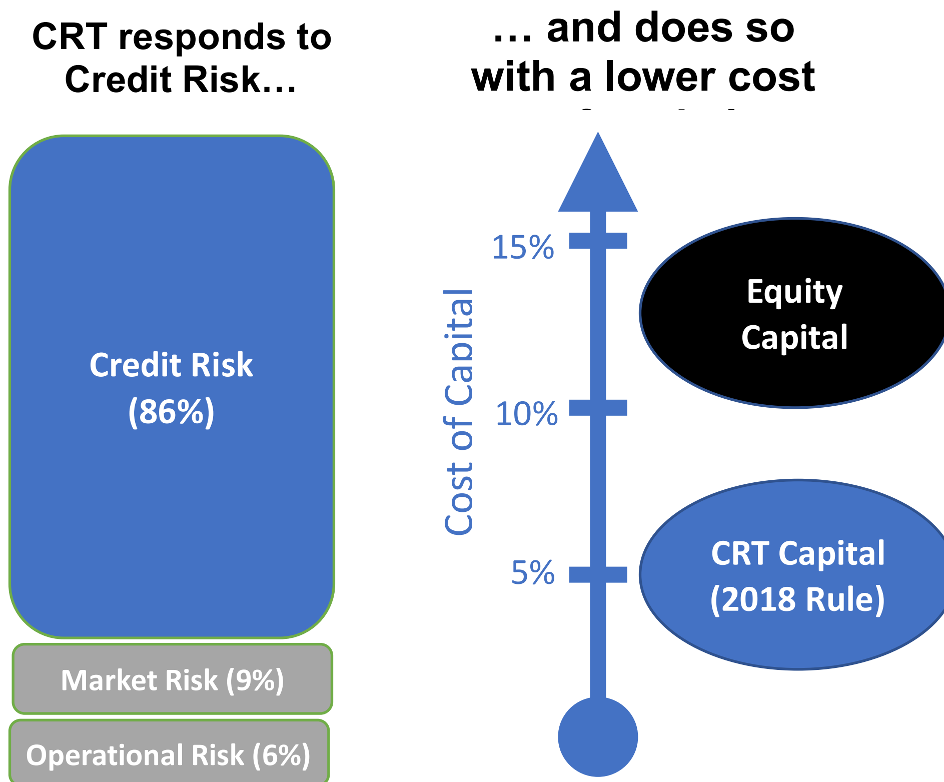
Assumes CIRT 2020-1 guaranteed loan pool with 10 bps credit loss and 25 bps non-credit costs,

Under the 2020 Proposed Rule and the 2020 reference pool, the Enterprises' return on equity without using CRT is expected to be approximately 7%. As proposed, the presence of CRT actually reduces the return on equity (ROE) down to approximately 6% because the costs under the current proposal are not offset by a corresponding capital benefit. The 2020 Proposed Rule

therefore directly disincentivizes the purchase of CRT protection from the private sector because it would deteriorate the returns that are available to shareholders of the Enterprises.

Under the 2020 Proposed Rule, Enterprise returns of 6% would be inferior to banks and other financial institutions, making it difficult or impossible for the Enterprises to raise capital. Banks and financial institutions typically require 10-15% expected shareholder returns. The only way for the Enterprises to remedy their inferior returns will be to increase fees, which will raise mortgage costs and pressure affordability. The proposed modifications the RAA supports (discussed below) and that also are reflected in the comments of individual RAA members would create a framework where the Enterprises are incentivized to use CRT, which will bring their returns in line with banks and other financial institutions, making the Enterprises more attractive to investors and placing the Enterprises on a more even footing with others in a competitive marketplace for the capital. The suggested modifications to the 2020 Proposed Rule of RAA and its members therefore allow the Enterprises to achieve their mission to U.S. homeowners and positions the Enterprises to exit conservatorship.

The Enterprises become more attractive to investors by enhancing equity capital.



As noted in table 2 of the 2020 Proposed Rule, as illustrated above, 86% of the Enterprises' total risk landscape consists of mortgage credit risk, and CRT responds to this driving risk of the Enterprises with a lower cost of capital. The Enterprises have shown that, if properly incented, they will utilize CRT to protect taxpayers. Moreover, the CRT execution experienced by the

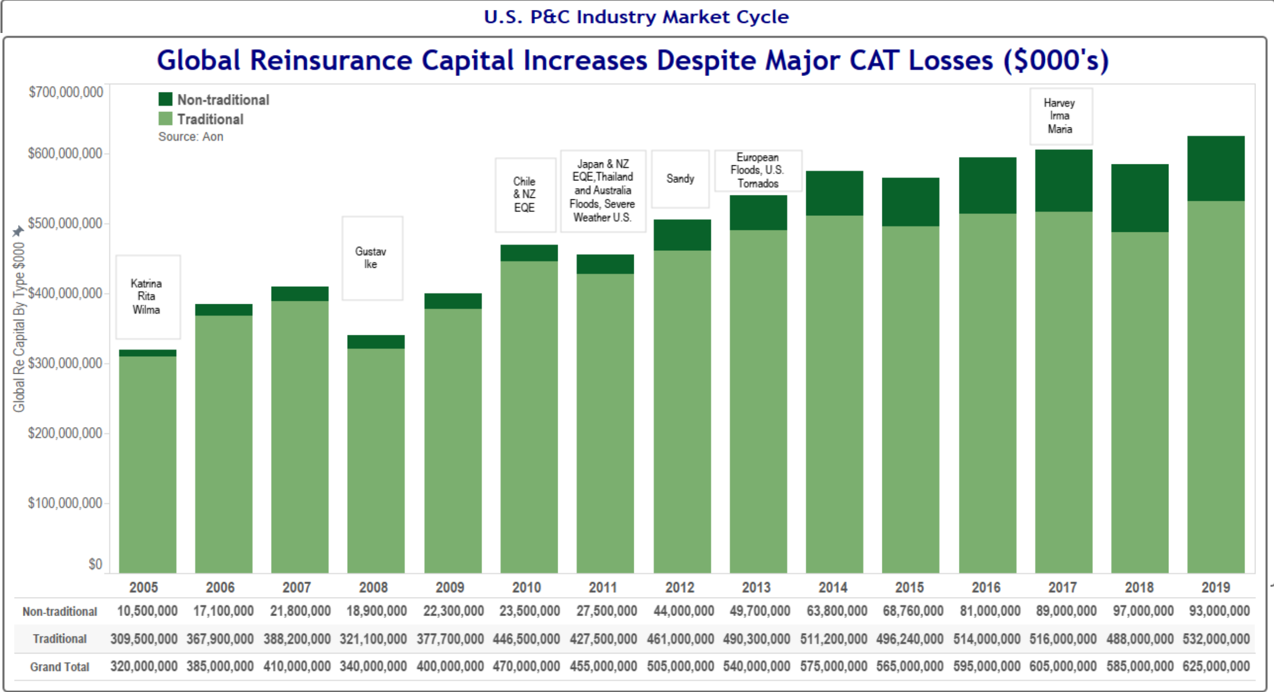
Enterprises in recent years has been extremely efficient. As a result, it is clear that the cost of CRT capital is substantially lower than the cost of alternative equity capital.

At the same time, CRT provides the additional benefit of capital diversification, and reduces volatility. It complements equity capital and, by lowering the cost of capital, helps preserve housing affordability. In addition, diversified sources of capital increase Enterprise durability through the cycle. That diversification is further achieved by two different types of CRT execution – the capital markets and the reinsurance markets. Capital markets represent approximately 75% of the CRT that has been transferred to the private sector to date, and reinsurers represent the other 25%. Reinsurance companies have diverse, non-correlated portfolios that enable counter-cyclical capital support. The ability of reinsurers to respond to changing market conditions highlight that diversity of thought and diversity of appetite. That diversity includes the ability to provide commitments to take on mortgage credit risk that is accepted by the Enterprises in the *future* (through "forward" transactions) and other custom-tailored solutions that can adjust to the prevailing conditions. Notably, after COVID-19 temporarily halted CRT transactions, there has been a continued issuance of both reinsurance and capital markets CRT transactions. In fact, the reinsurance market was the first to re-enter the CRT market to provide capacity with new CRT offerings. To date, every CRT transaction the Enterprises have brought to market has been successfully placed. Given the inherent instability that could come from a crisis, having as many sources of this diversified capital as possible (including reinsurance capital) is incredibly valuable to the Enterprises.

ROLE OF REINSURANCE

As noted above, reinsurers have been an effective and important piece of the CRT program. Reinsurance is a risk management tool for insurance companies that can be used to reduce the volatility in their insurance risk portfolios and to improve their financial performance and security. Insurance and reinsurance as financial risk management tools are inherently counter-cyclical: in times of strong mortgage performance, the expected premium outlay will be greater than the expected claim benefit, but in a stress scenario, the claim benefit received can dwarf the cost of the premiums paid. The effectiveness of reinsurance as a risk management tool is enhanced to the extent it can spread risk over the broadest possible base of responsible capital.

It is widely recognized that reinsurance performs at least four primary functions in the marketplace: to limit liability on specific risks; to stabilize loss experience; to provide coverage for insurers of major natural and man-made catastrophe risk; and to increase insurance capacity. By helping to mitigate the potential losses that could result from risks such as major new construction projects or breakthrough technologies, reinsurers help enable innovation. Finally, reinsurers play an important advisory role based upon their often-greater experience with certain insurance markets and products and the underwriting experience from a wide range of insured populations across the globe. By writing diversified insurance risk from around the world, reinsurance companies avoid overexposure and act as a stabilizing force in local insurance markets. Reinsurance takes the volatility out of insurer financial performance over time. Indeed, as illustrated in the chart below, in the wake of a major event or crisis, reinsurers typically proactively look to take on additional risk, resulting in a growth in reinsurance capital post event.



	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Non-traditional	10,500,000	17,100,000	21,800,000	18,900,000	22,300,000	23,500,000	27,500,000	44,000,000	49,700,000	63,800,000	68,760,000	81,000,000	89,000,000	97,000,000	93,000,000
Traditional	309,500,000	367,900,000	388,200,000	321,100,000	377,700,000	446,500,000	427,500,000	461,000,000	490,300,000	511,200,000	496,240,000	514,000,000	516,000,000	488,000,000	532,000,000
Grand Total	320,000,000	385,000,000	410,000,000	340,000,000	400,000,000	470,000,000	455,000,000	505,000,000	540,000,000	575,000,000	565,000,000	595,000,000	605,000,000	585,000,000	625,000,000

Reinsurance has proven to be a stable source of capital that responds proactively to crises and continues to deploy capacity.

As of Q1 2020, the global reinsurance market represents approximately $600 billion of capital[18] and already provides meaningful support to the private market, the Enterprises, and government programs, such as the National Flood Insurance Program and Export-Import Bank of the U.S. These entities have successfully transferred risk to reinsurance companies and their affiliates, simultaneously protecting taxpayers while helping families and businesses in the private sector. After hurricane Harvey in 2017, reinsurers absorbed over $1 billion to help pay NFIP claims.[19] Claims were paid by the reinsurance market within seven days. Despite this total loss to their reinsurance limit in the first year of the program, the reinsurance markets not only renewed, but increased their coverage for 2018.[20] This is just one clear example of how reinsurance helps to stabilize the economy after crisis events and remains viable as a market following major events with significant insured losses. Reinsurance by its nature is used to support business through the cycle, even in the period immediately following a major event/loss.

KEY FEATURES OF 2020 PROPOSED RULE THAT EFFECTIVELY ELIMINATE CRT

The 2020 Proposed Rule has three key features that create negative housing market impacts through the effective elimination of CRT. These features are:

1. New leverage ratio cap;

2. New minimum tranche risk weight floor; and
3. New overall effectiveness adjustment.

The combined impact of these three features is to make risk transfer to the private sector uneconomical. Effectively, these features eliminate CRT by destroying the incentives to transfer risk. The overall impact of these changes is significant.

If CRT is not used as a source of capital, then a greater amount of equity capital would be required, raising the execution risks needed to exit conservatorship. It also increases the time needed to exit conservatorship, as it will take more time to raise additional levels of capital or more time for earnings to reach the necessary levels. The 2020 Proposed Rule requires the Enterprises to hold capital of at least $243 billion, and in order to operate responsibly, they would inevitably need to impose their own buffer above the required level to avoid facing a regulatory cliff in their everyday operations. The amount is extraordinary (as discussed more fully below) and would take years to accumulate.

Reliance on a single source of capital (equity) makes the Enterprises less durable through the cycle. The Enterprises can never be sure that they will be able to replenish their equity capital in a time of crisis, but if the Enterprises had multiple sources of capital, they could be more durable and more diversified. In addition, sole reliance on the more expensive form of capital means that higher g-fees would be needed. This will result in increases in the cost of housing for homeowners and renters.

The Enterprises also compete in the marketplace with another federal government-created and taxpayer-backed program, the FHA. If the 2020 Proposed Rule increases the cost of Enterprise loans, then it is inevitable that a significant portion of the mortgage business will be diverted to the FHA. This puts taxpayers at risk because there is no mechanism at the FHA to transfer risk to the private sector.

OBSERVATIONS AND IMPACTS OF THE PROPOSED RULE

The 2020 Proposed Rule is an inversion from the FHFA's prior plans and reports and would penalize the Enterprises for transferring mortgage credit risk to third parties. The RAA respectfully makes the following observations on the proposed rule, along with the impact of each of those observations.

Observation 1: The 2020 Proposed Rule requires the Enterprises to hold capital to the higher of the leverage ratio and risk-based capital requirements. Under the first standard, the non-risk-based, leverage ratio requirement, the Enterprises receive absolutely zero capital credit for CRT (and in practice the costs they pay for the risk transfer protection will reduce their overall returns). Under the risk-based capital requirement, the Enterprises would receive less than *half* the credit they receive today over the life of the CRT transactions.

> **Impact:** Requiring the Enterprises to comply with the higher of the two capital requirements threatens to eliminate the successful CRT program, which would be detrimental to risk management, taxpayers, homeowners, and renters. There is no incentive

for the Enterprises to use CRT going forward, given that the 2020 Proposed Rule materially devalues CRT. In fact, in some cases, the 2020 Proposed Rule would actually impose negative capital credit because the Enterprises will be required to hold more capital on mortgages that are covered by CRT than they would hold if they kept 100% of the risk themselves. The publication of the 2020 Proposed Rule already has caused Fannie Mae to hit "pause," stating it "currently [does] not have plans to engage in additional credit risk transfer transactions as [it] evaluate[s] FHFA's recently re-proposed capital rule, which would reduce the amount of capital relief [it] obtain[s] from these transactions."[21] Without CRT, the Enterprises will regress to a pre-2008 financial crisis state, where equity shareholders retain all of the Enterprises' mortgage credit risk.

Observation 2: The 2020 Proposed Rule emphasizes the quality of equity capital and devalues CRT.

Impact 1: Without CRT, the Enterprises lose a valuable source of diversifying external capital, making them too reliant on equity shareholders. Moreover, it will make the Enterprises less durable across the economic cycle, jeopardizing the Enterprises' safety and soundness and increasing the likelihood of a future U.S. taxpayer bailout.

Impact 2: Sole reliance on more expensive equity capital will require the Enterprises to take on more risk and/or increase their guarantee fees (g-fees) to satisfy minimum returns demanded by equity shareholders. Increasing g-fees will increase costs for borrowers and divert new mortgages to the 100%, federally-backed, FHA, increasing taxpayer risk and running counter to the Administration's housing reform plans.[22]

Impact 3: Devaluing CRT will reduce the Enterprises' loss-absorbing capacity. CRT does not respond to market and operational risk, but it does respond to the dominant risk (credit risk) which comprises 86% of the overall risk held by the Enterprises.

Impact 4: The Enterprises would lose valuable private market feedback and price discovery on the credit risk which they guarantee.

Observation 3: The 2020 Proposed Rule requires the Enterprises to hold capital of at least $243 billion. This amount: is nine times the $28 billion of the capital held as of August 2020; requires the Enterprises to raise additional capital that is seven times larger than the largest initial public offering in world history ($29.4 billion raised by Saudi Aramco in 2019); and is six times higher than the $43 billion Dodd-Frank Act Stress Test for the severe adverse scenario.

Impact: Without CRT, it will take five to ten years for the Enterprises to raise the required amount of capital, further delaying their exit from conservatorship and exposing taxpayers during this period.[23]

<u>SUGGESTED MODIFICATIONS</u>

RAA's membership is in unanimous agreement that the Proposed Rule devalues CRT. Our members have slightly different views on the path forward but share similar concerns about the

five issues outlined below. The independent and directionally aligned responses to the proposed rule of AON (reinsurance broker), Guy Carpenter (reinsurance broker), Arch (mortgage insurer and reinsurer) and Renaissance Re (reinsurer) represent the central thrust of the RAA's views and are recommended for consideration by FHFA as a basis for reinstating the value of CRT.

Leverage Ratio

The Leverage Ratio, the current binding constraint, does not provide capital credit for risk transfer. RAA believes that risk transfer should receive equal capital treatment under the Leverage Ratio and Risk-Based Capital requirements.

The Rule also proposes a Leverage Ratio set at 2.5% of total adjusted assets, plus 1.5% of Tier 1 Capital as the Prescribed Leverage Buffer Amount ("PLBA"), for a total Leverage Ratio of 4% of adjusted assets. The consequences of this higher ratio and proposed additional modifications at a lower level of calibration are discussed at length in our members' individual comment letters.

Tranche Risk Weight Floor

The Tranche Risk Weight Floor is designed to ensure that no retained exposure carries a zero capital requirement. RAA appreciates the rationale for the rule but we believe that its level of conservatism has inherent flaws. We refer FHFA to our members' recommendations regarding its removal or modification with an intention to incentivize proper risk management behavior.

Overall Effectiveness Adjustment

RAA recognizes the Overall Effectiveness Adjustment is intended to compensate for the superior flexibility, fungibility and loss-absorbing capacity of equity capital. While CRT capital may not have the same attributes as equity capital, RAA strongly believes that embracing diverse forms and sources of capital is essential to ensuring the quality, quantity, and loss-absorbing capacity of Enterprise capital across economic cycles.

Risk-Based Buffers

The risk-based capital requirements include three buffer amounts: the countercyclical (currently set at zero), stress, and stability capital buffers. The stress and stability buffers comprise almost 80% of the total risk-based capital requirements, which presents some of the same risks and issues as an overly conservative Leverage Ratio. RAA members' comment letters present the case for recalibrating the buffers making them more sensitive to risk.

Counterparty Assessment Should be Transparent and Objective

The Proposed Rule is opaque as it respects the counterparty assessment process. RAA members encourage FHFA to provide further transparency on the assessment of mortgage concentration and counterparty ratings. The goal of such transparency is to create "virtuous competition".

CONCLUSION

As set forth above, while RAA recognizes that the FHFA's 2020 Proposed Rule has worthy objectives, as drafted, it would effectively eliminate CRT, destroying CRT's ability to enhance equity capital and limit taxpayer exposure to catastrophic mortgage credit losses. CRT is a valuable component of exiting conservatorship because:

- CRT works today to transfer risk to the private sector and can be a valuable bridge to recapitalization of the Enterprises;
- CRT protects taxpayers from the Enterprises' core mortgage credit risk;
- CRT improves housing affordability by lowering costs to homeowners and renters through a lower cost of capital (compared to equity capital);
- CRT increases certainty and improves stability through the cycle;
- CRT is an important source of diversified external capital; and
- CRT provides valuable feedback to the Enterprises on credit costs and on underwriting standards.

As a result, the RAA strongly believes that the 2020 Proposed Rule should be modified to provide robust incentives for the Enterprises to continue to use CRT.

Thank you for the opportunity to provide comments. The RAA and its members would be happy to brief you regarding the recommendations in this letter or answer any questions you may have.

Sincerely,

Frank Nutter
President

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[1] https://crt.freddiemac.com/offerings/acis.aspx#document-details
https://capmrkt.fanniemae.com/portal/funding-the-market/credit-risk/credit-insurance-transactions-servicing-reports.html

[2] https://www.govinfo.gov/content/pkg/FR-2020-06-30/pdf/2020-11279.pdf;
https://www.govinfo.gov/content/pkg/FR-2018-07-17/pdf/2018-14255.pdf

[3] https://www.fhfa.gov/SupervisionRegulation/FannieMaeandFreddieMac/Pages/About-Fannie-Mae---Freddie-Mac.aspx

[4] https://www.fhfa.gov/Conservatorship/Pages/History-of-Fannie-Mae--Freddie-Conservatorships.aspx;
https://www.fhfa.gov/PolicyProgramsResearch/Policy/Pages/Credit-Risk-Transfer.aspx;
https://www.fhfa.gov/PolicyProgramsResearch/Policy/Pages/FHFA-Statements-on-Credit-Risk-Transfer.aspx; and
https://www.whitehouse.gov/presidential-actions/memorandum-federal-housing-finance-reform/

[5] https://www.fhfa.gov/PolicyProgramsResearch/Policy/Pages/Credit-Risk-Transfer.aspx#:~:text=%E2%80%8BCredit%20Risk%20Transfer%E2%80%8B&text=In%202012%2C%20the%20Federal%20Housing,to%20taxpayers%20while%20in%20conservatorship.

[6] https://www.fhfa.gov/AboutUs/Reports/ReportDocuments/20120221_StrategicPlanConservatorships_508.pdf; https://www.fhfa.gov/AboutUs/Reports/ReportDocuments/FHFA_2019_Report-to-Congress.pdf

[7] *Id.*

[8] Transcript of Hearing of the U.S. House Committee on Financial Services. "Oversight of the Treasury Department and Federal Reserve's Pandemic Response," June 30, 2020.

[9] Aon plc.

[10] Aon plc; Don Layton (https://www.jchs.harvard.edu/blog/demystifying-credit-risk-transfer/)

[11] Don Layton (https://www.jchs.harvard.edu/sites/default/files/harvard_jchs_gse_crt_part2_layton_2020.pdf)

[12] https://www.fhfa.gov/AboutUs/Reports/ReportDocuments/CRT-Progress-Report-4Q2019.pdf

[13] U.S. Department of Treasury Housing Reform Plan, September 2019.

[14] *Id.*

[15] Aon,plc; http://www.freddiemac.com/investors/financials/pdf/10k_021320.pdf; https://www.fanniemae.com/resources/file/ir/pdf/quarterly-annual-results/2019/q42019.pdf; https://www.fanniemae.com/portal/funding-the-market/credit-risk/multifamily/mf-credit-insurance-risk-transfer.html; https://freddiemac.gcs-web.com/news-releases/news-release-details/freddie-mac-closes-18-billion-mcip-reinsurance-transaction; https://freddiemac.gcs-web.com/news-releases/news-release-details/freddie-mac-announces-first-multifamily-credit-risk-transfer; and https://freddiemac.gcs-web.com/node/18646/pdf

[16] https://www.fhfa.gov/Media/PublicAffairs/PublicAffairsDocuments/Webinar_642020.pdf

[17] Freddie Mac 2020Q1 earnings release (http://www.freddiemac.com/investors/financials/pdf/2020er-1q20_release.pdf)

[18] http://thoughtleadership.aonbenfield.com/Documents/20200710-re-analytics-reinsurance-market-outlook-junejuly.pdf; Guy Carpenter estimates $435 billion in dedicated reinsurance capital as of midyear 2020.

[19] Page 59, https://www.whitehouse.gov/wp-content/uploads/2018/02/budget-fy2019.pdf; https://www.fema.gov/news-release/20200220/fema-will-recover-1042-billion-reinsurance-private-reinsurance-markets; https://www.fema.gov/news-release/20200220/fema-reflects-historic-year; and https://www.fema.gov/media-library-data/1522167351921-a5e457454262dd100e2f15a7210d21c5/Watermark_FY18_Q1_v6_508.pdf

[20] https://www.fema.gov/media-library-data/1522167351921-a5e457454262dd100e2f15a7210d21c5/Watermark_FY18_Q1_v6_508.pdf

[21] https://www.sec.gov/Archives/edgar/data/0000310522/000031052220000278/fnm-20200630.htm

[22] https://home.treasury.gov/news/press-releases/sm769

[23] https://www.cbo.gov/system/files/2020-08/56496-GSE.pdf; Aon plc