

**MEMORANDUM**

**TO:** File No. DF Title IX - Asset-Backed Securities

**FROM:** Jay Knight  
Attorney-Adviser  
Office of Rulemaking  
Division of Corporation Finance  
U.S. Securities and Exchange Commission

**RE:** Meeting with the Mortgage Insurance Companies of America

**DATE:** October 5, 2010

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On October 5, 2010, Katherine Hsu, Rolaine Bancroft, and Jay Knight of the Division of Corporation Finance and Eric Emre Carr and Stanislava Nikolova of the Division of Risk, Strategy and Financial Innovation met with the following representatives of the Mortgage Insurance Companies of America: Suzanne Hutchinson (MICA); Christopher Nard (Republic Mortgage Insurance Company); Patrick Sinks (Mortgage Guaranty Insurance Corporation); and Peter Romeo (Hogan Lovells). Among the topics discussed was the case for private mortgage insurance to be within the definition of qualified residential mortgage in any rule promulgated pursuant Title IX, Subtitle D, Section 941 of the Dodd-Frank Wall Street Reform and Consumer Protection Act. Handouts are attached to this memorandum.

Attachment

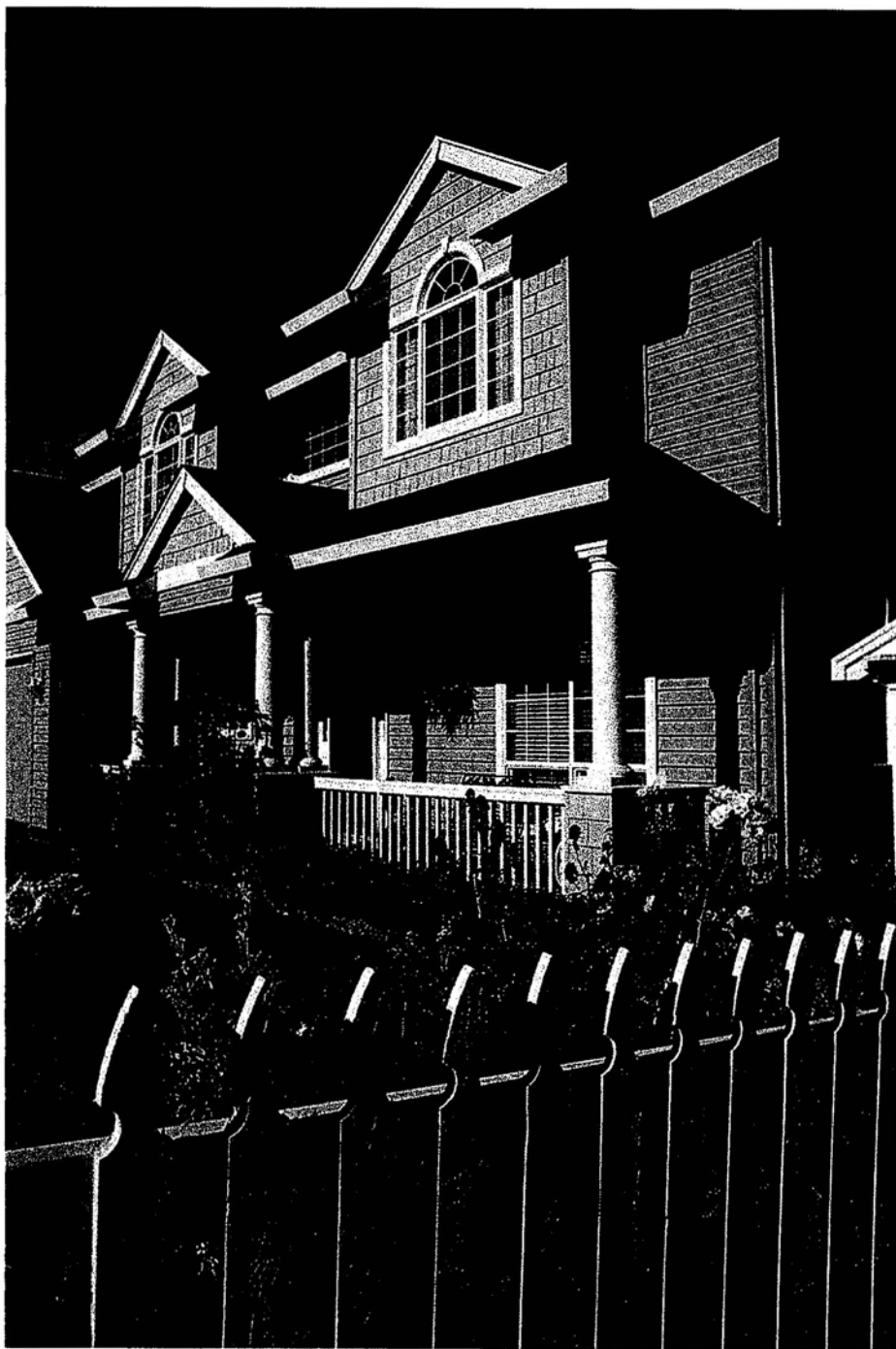
## Agenda

Private MI Industry Overview

Sustainable Low Downpayment Lending Critical to Recovery

Prudent Underwriting - Qualified Residential Mortgages

The Case for Mortgage Insurance Within the Qualified Mortgage Definition



# **U.S. Securities and Exchange Commission**

## **Private Mortgage Insurance Industry Discussion**

October 2010

# **Agenda**

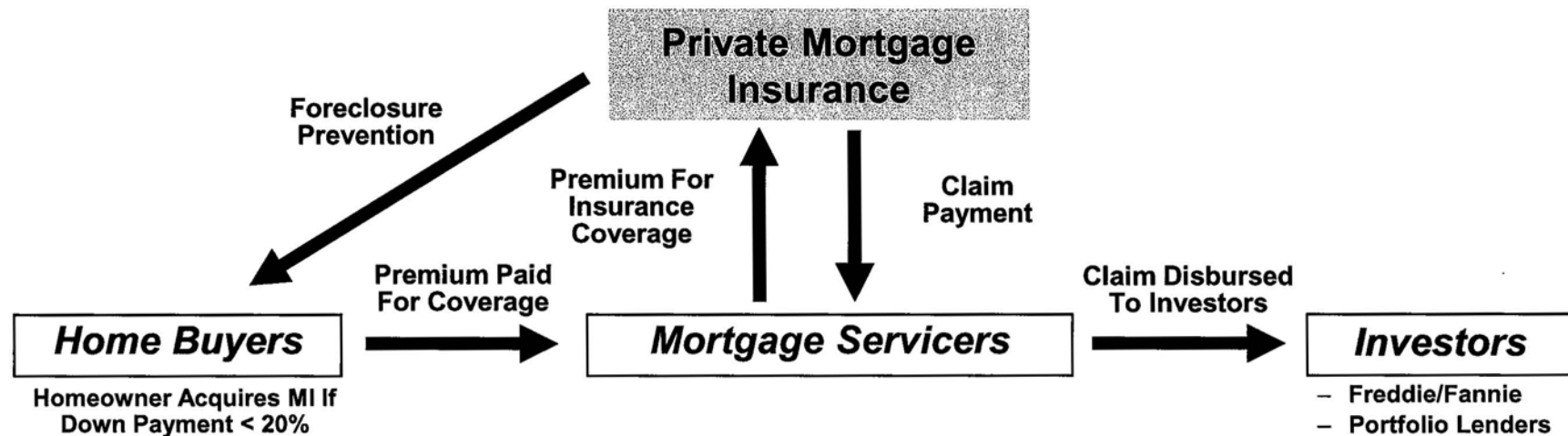
**Private MI Industry Overview**

**Sustainable Low Downpayment Lending Critical to Recovery**

**Prudent Underwriting - Qualified Residential Mortgages**

**The Case for Mortgage Insurance Within the Qualified Mortgage Definition**

# Private Mortgage Insurance – How It Works



**MI Facilitates Purchase Of Homes With Less Than 20% Down**

**Pays In a “First Loss” Position After Borrower Equity ... Shielding Banks and Investors from Credit Losses**

**MI's Independent Underwriting Standards Provide Credit Risk Discipline**

**Immediately Commits Private Capital Against Each Loan – “Skin in the Game”**

**Countercyclical Model ... Capital Builds via Requirement to Hold 50% Of All Premiums Received in Reserve**

**Interests Directly Aligned With Borrowers and Investors ... Proactively Works With Borrower and Servicer to Prevent Foreclosure**



# **Private MIs Industry Well Positioned**

**Industry Has Ample Regulatory Capital**

**Additional \$7.4B Capital Raised by Existing MIs**

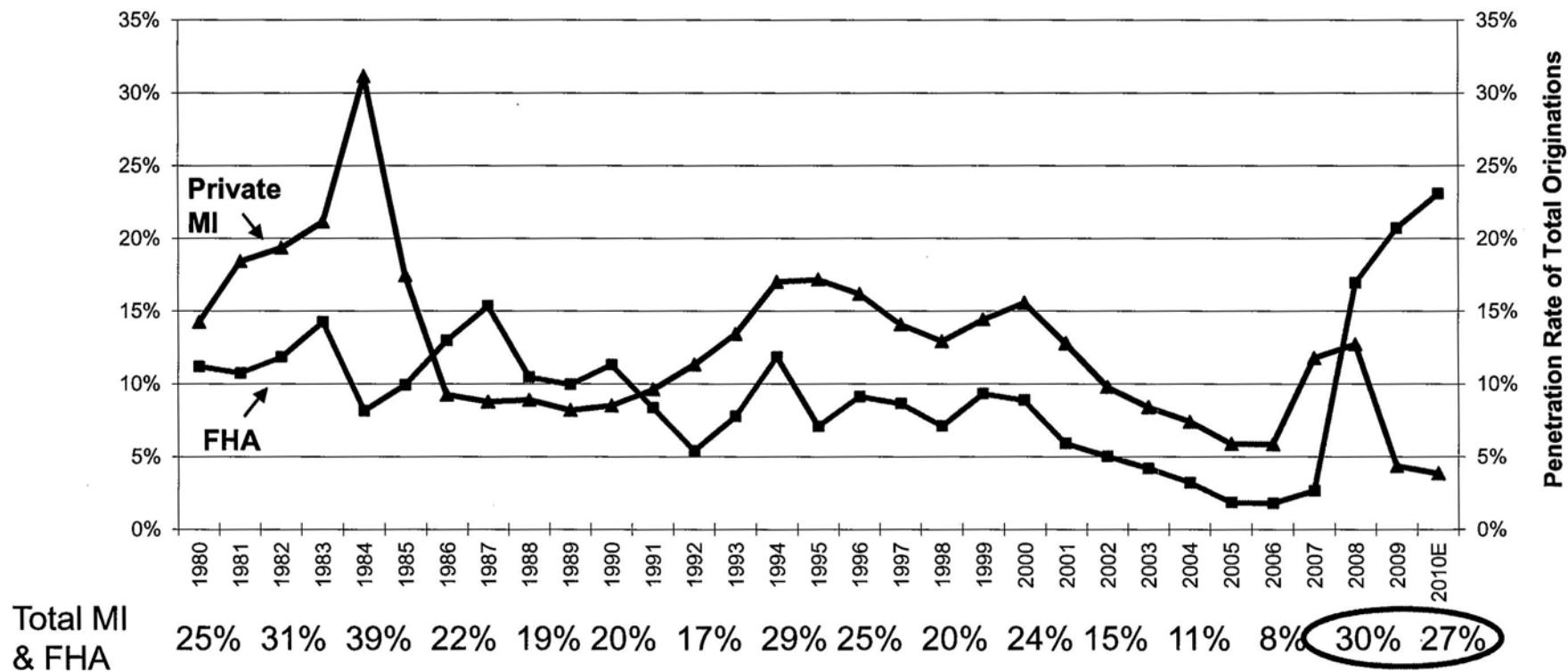
**New Entrant Has Invested \$575MM In Industry**

**Delinquency Growth Slowing**

**Gov't Programs Having a Real Impact<sup>1</sup>**

- 289,190 HAMP Trials Started and 67,484 Completed
- 70,042 HARP Approvals and 57,051 Closed Refinances
- 462,316 Total Workouts since 2008 ... \$93 Billion in Loans

# Low Down Payment Lending Penetration



**Prudent Low Down Payment Lending Critical to Recovery**  
**Qualified Residential Mortgage Considers This Important Sector of Housing Market**

Sources: Private MI data from MICA (excludes HARP), FHA Data from August 13, 2010 IMF, Origination Data from IMF  
 Note: '2010E' penetration rates are based on MICA estimate



# Risk Retention and Qualified Residential Mortgage

- **Dodd-Frank Wall Street Reform and Consumer Protection Act Creates New Obligation for Securitizers to Retain Interest in Securitized Assets**
- **Bill Directs Regulators to Exempt Qualified Residential Mortgages (QRM)**
- **Regulators Must Define a QRM Taking into Consideration Underwriting and Product Features That Result in a Lower Risk of Default Such as:**
  - Documented and verified financial resources
  - Standards for: a) residual income after meeting all obligations; b) ratio of housing payment to income; c) ratio of all installment payments to income
  - Standards and features that mitigate the payment shock of ARMs
  - Mortgage guaranty insurance (or other insurance or credit enhancement) obtained *at the time of origination* to the extent such insurance/credit enhancement reduces the risk of default.
  - Prohibitions/restrictions on balloon payments, negative amortization, prepay penalties, interest only & other similar high risk features

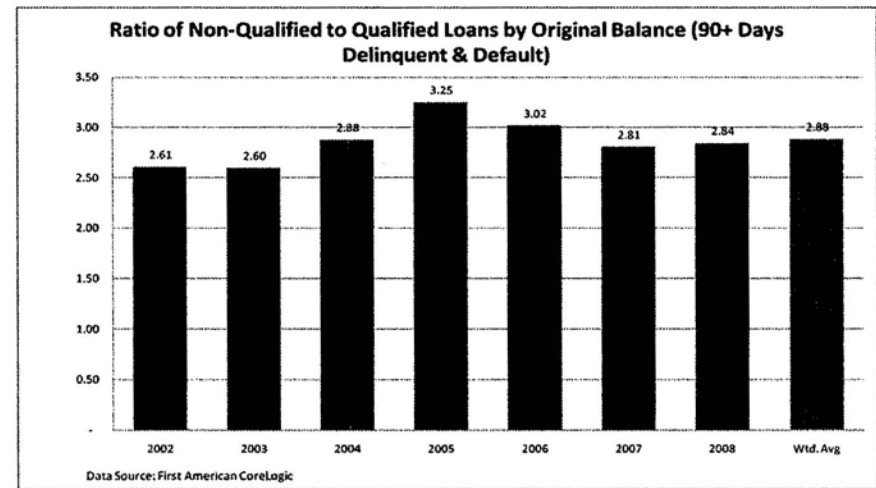
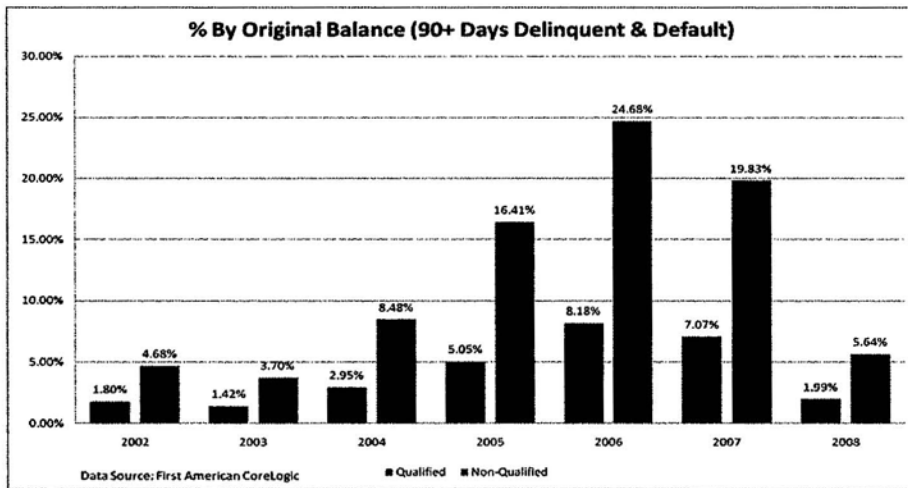
## **Data Clearly Demonstrates:**

- **A Qualified Mortgage standard mitigates the risk of default**
- **On low down payment loans, Insured Loans have a lower risk of default than comparable Piggyback (uninsured) Loans**

# Qualified Mortgage Study

➤ A Study of Performance by Vertical Capital Solutions using CoreLogic Servicing Dataset Reveals that “Qualified Mortgages” Significantly Outperformed “Non-Qualified Mortgages”, Based on the Underwriting Standards Below:

- Fully Documented Income & Assets;
- Total Debt-To-Income  $\leq$  41%;
- 7/1 ARM's & Greater or Fixed Rate;
- Loans with a CLTV  $>$ 80% must carry MI
- No Balloon; No Interest Only; No Negative Amortization; Term  $\leq$  360 months



**Qualified Mortgages Clearly Have Lower Risk of Default**

# Piggybacks Versus Insured Loan Study

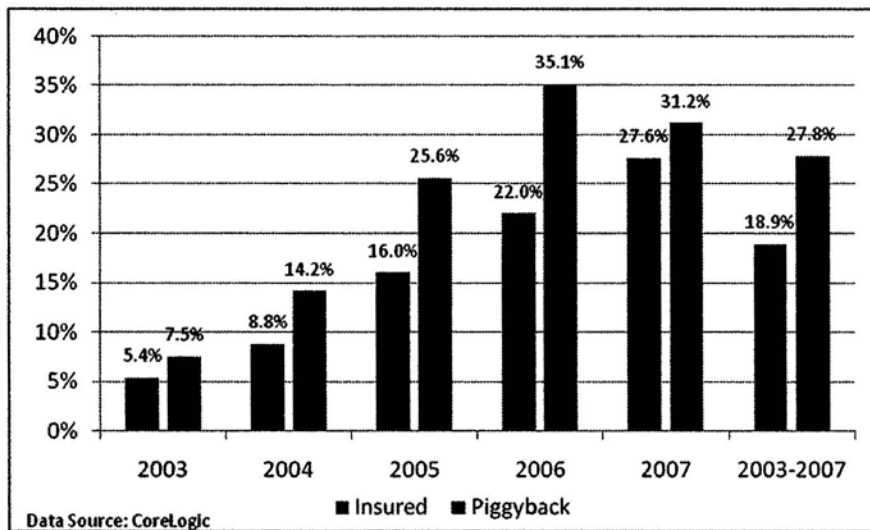
- MICA set out to compare default performance of Insured loans to comparable Piggyback Loans to support the inclusion of a Mortgage Insurance requirement in the Qualified Residential Mortgage definition
- Used CoreLogic Servicing Database of over 120 Million Loans
- Extracted high CLTV loans and divided them into two Populations:
  - Insured Loan = loan with mortgage insurance (3.8mm loans)
  - Piggyback Loan = uninsured loan where 1<sup>st</sup> lien LTV = 80% and CLTV >80% (1.1mm loans)
- Examined Performance Data as of June 30, 2010 and segregated each population into 5040 segment combinations of:
  - 5 Origination Years (2003-2007)
  - 7 FICO score ranges
  - 4 Combined Loan-To-Value (CLTV) ranges
  - 9 US Census Regions
  - 2 Loan Purpose Categories
  - 2 Documentation Levels
- Delinquency, Cure & Non-Performing data normalized to the distribution of the Piggyback population across all 5040 segments & compared performance

**Findings: Insured Loans Became Delinquent 47% Less Frequently, Cured 54% More Frequently and Have Performed 65% Better than Comparable Piggyback Loans**

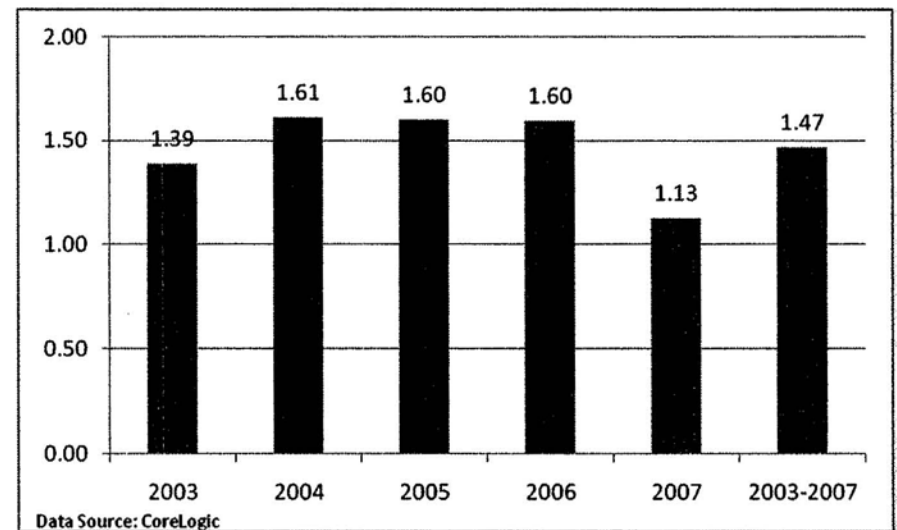
# Piggybacks Versus Insured Loans

## DELINQUENCY PERFORMANCE\*

**Delinquency Rates By Origination Year**  
Weighting Segments By Piggyback Profile



**Ratio of Piggybacks Delinquency Rates to Insured**  
% Piggyback Delinquency / % Insured Delinquency



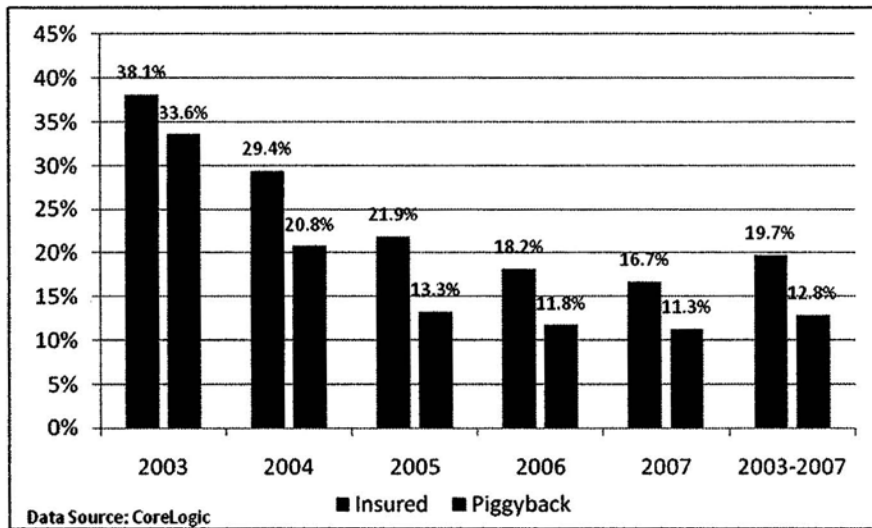
**Insured Loans Have Significantly Lower Incidence of Delinquency than Comparable Piggyback Loans**

\* Ever 90 Day Delinquency Rate: # of loans that ever went 90 or more days delinquent / original number of loans

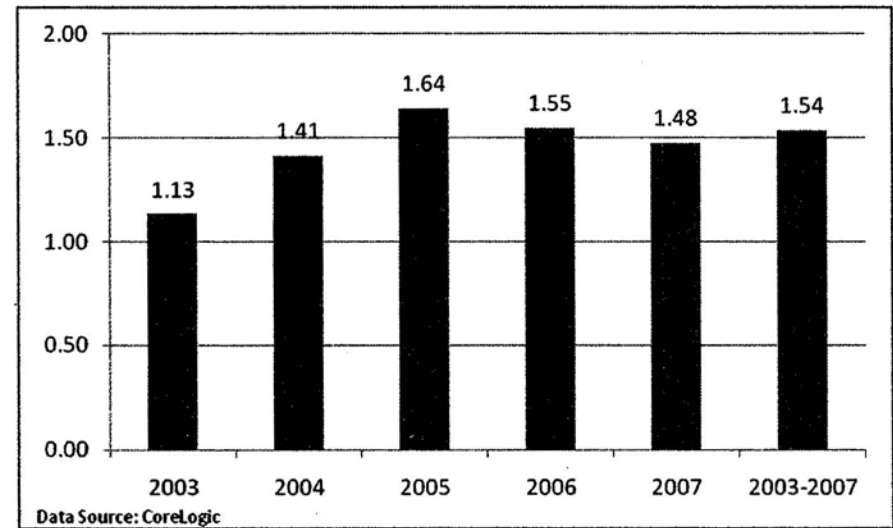
# Piggybacks Versus Insured Loans

## CURE PERFORMANCE\*

**Cure Rates On Delinquent Loans By Origination Year**  
Weighting Segments By Piggyback Profile



**Weighted Ratios Of Insured Cure Rates To Piggybacks**  
Insured Cure Rate % / Piggyback Cure Rate %



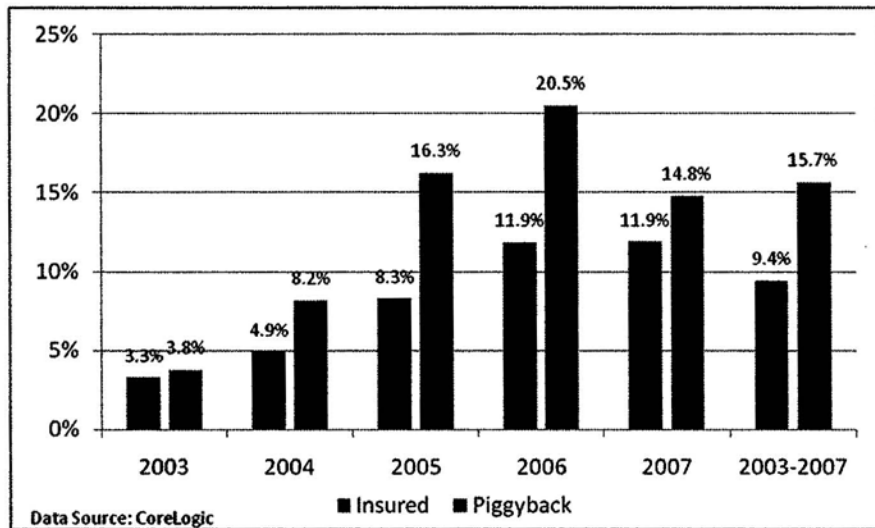
**Once Delinquent, Insured Loans Cure 54% More Frequently Than Piggybacks**

\* Cure Rate: # Ever 90 Day Delinquent loans that subsequently became current / total number Ever 90 Day delinquent loans

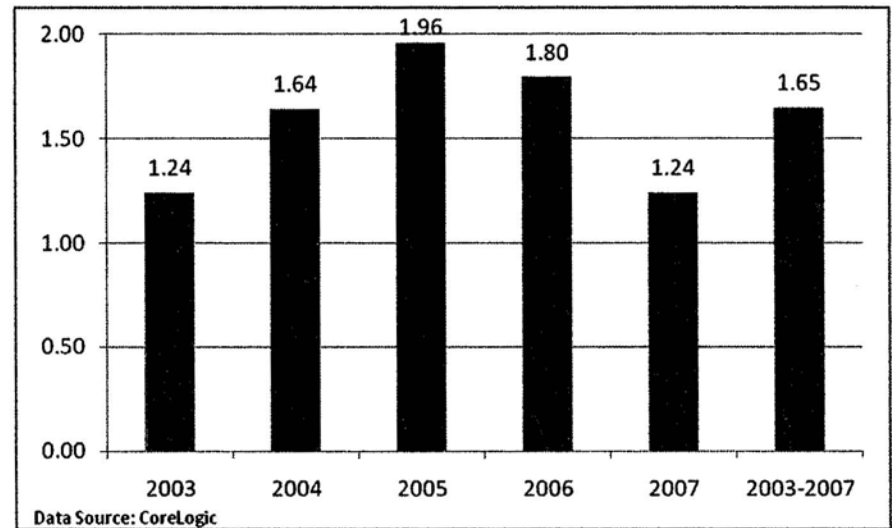
# Piggybacks Versus Insured Loans

## NON-PERFORMING RATES\*

**Non Performing Rates By Origination Year**  
(Currently 90+ Days Delinquent & Defaults)



**Ratios Of Piggyback Non-Performing Rates To Insured**  
Piggyback Non-Performing / Insured Non-Performing Rate

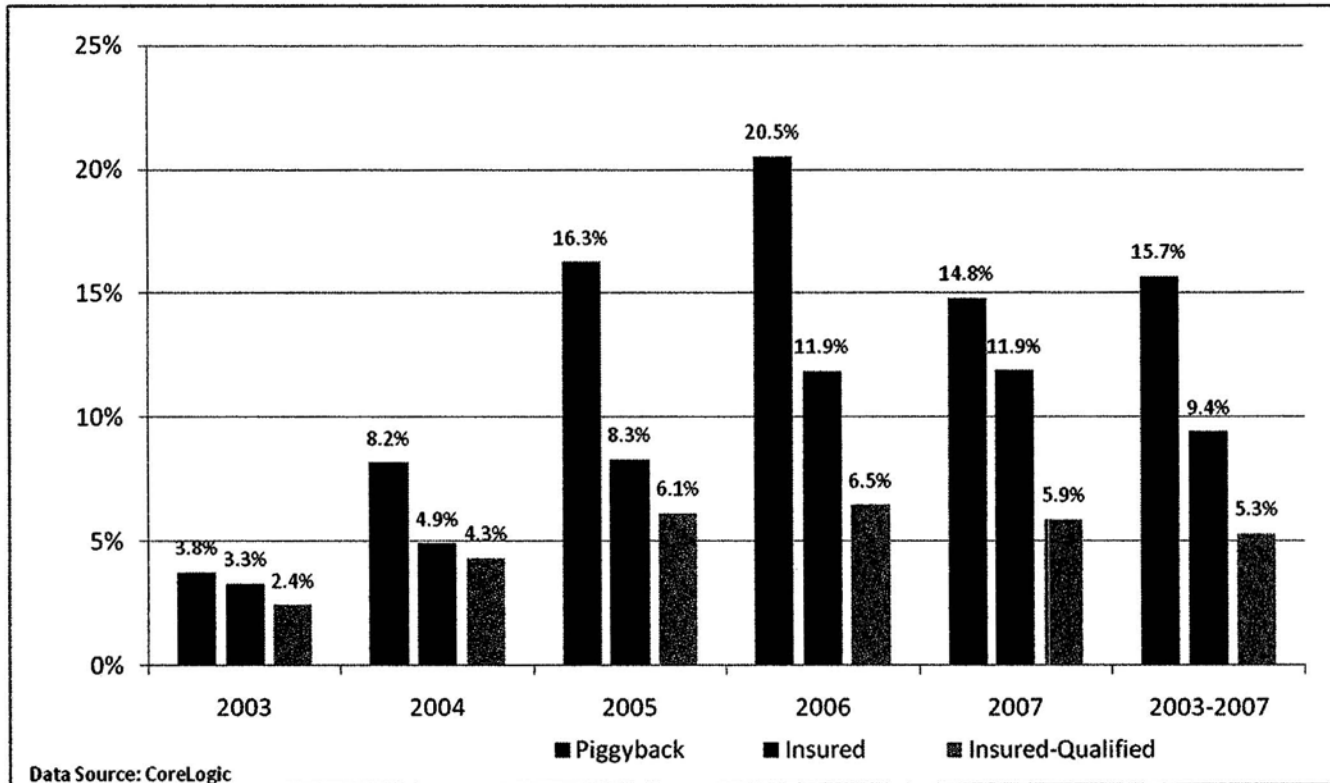


**End Result ... Insured Low Downpayment Loans Have Lower Risk of Default than Comparable Piggyback Loans**

\* Non-Performing Rate: (# Loans Currently 90 or more days delinquent + loans that terminated in default) / original number of loans

# Qualified Insured Loan Performance

## NON-PERFORMING RATES\*



**“Qualified” Insured Loans Have Performed Well Through the Downturn**

\* Non-Performing Rate: (# Loans Currently 90 or more days delinquent + loans that terminated in default) / original number of loans

# **The Case For Private Mortgage Insurance**

**QRM Exemption is Based on Prudent Underwriting Practices Including MI as a Risk Mitigant on Low Downpayment Mortgages**

**Loans With Mortgage Insurance Meet the Bar of Lowering Risk of Default as Required Under Dodd-Frank**

**Final QRM Definition Should Require Mortgage Guarantee Insurance on Loans With a Combined Loan to Value Greater than 80%**

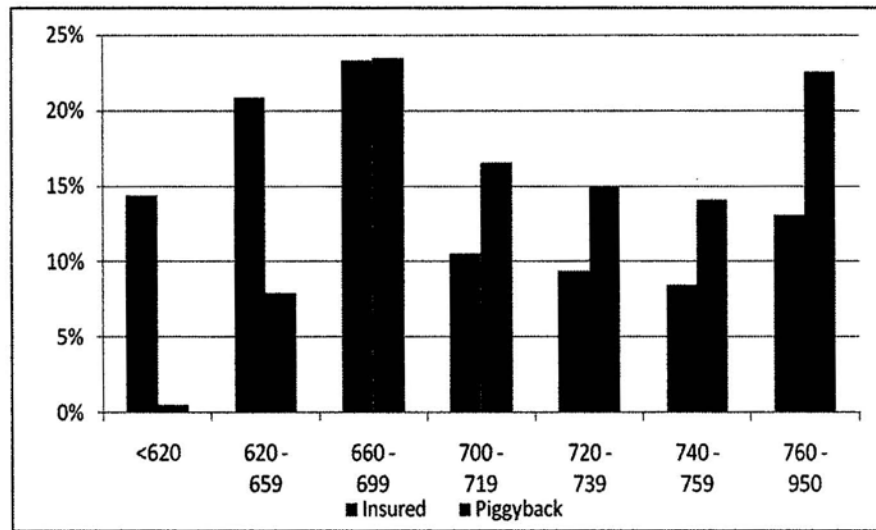


# Appendix

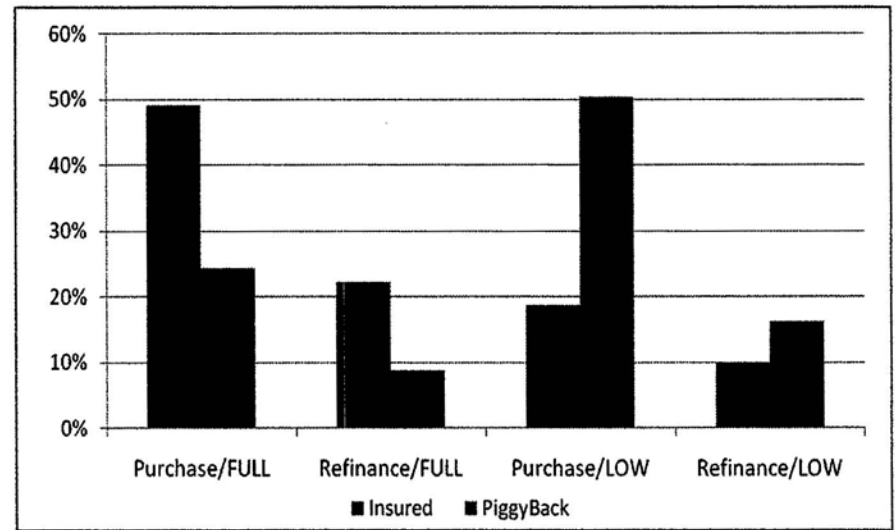
# Piggybacks Versus Insured Loans

## Differences In Distributions Across Key Metrics

Distribution by FICO Range



Distribution by Purpose / Documentation



**Piggyback Population Relied Heavily on FICO ... Less on Documentation**