

Congress of the United States
Washington, DC 20515

May 23, 2023

The Honorable Gary Gensler
Chair
U.S. Securities and Exchange Commission
100 F Street NE
Washington, DC 20549

Dear Chair Gensler,

We are writing to request that the Securities and Exchange Commission (the “Commission”) clarify via language in the final regulation or accompanying release that Mortgage Insurance-Linked Notes (MILNs) are not synthetic asset-backed securities (ABS) or conflicted transactions within the meaning of the Commission’s Reproposed Rule 192, “Prohibition Against Conflicts of Interest in Certain Securitizations.”¹ Language in the Reproposed Rule may unintentionally prohibit private mortgage insurers from procuring reinsurance via the capital markets through MILNs, which would negatively impact homebuyers, lenders, and taxpayers.

Statutory charters of the government-sponsored enterprises, Fannie Mae and Freddie Mac (the “GSEs”), require that loans with down payments lower than 20 percent include credit enhancement which is primarily obtained using private mortgage insurance from a qualified mortgage insurer. Private mortgage insurance facilitates access to affordable and sustainable homeownership and more than 60 percent of purchasers with private mortgage insurance are first-time homebuyers and 35 percent of borrowers with private mortgage insurance have incomes below \$75,000.² The use of private mortgage insurance also promotes safety and soundness as private mortgage insurance stands in the “first loss” position to absorb credit losses before the GSEs and the taxpayers.

Like other insurers, private mortgage insurers must manage capital positions and risk exposures, including through the programmatic use of reinsurance, by leveraging traditional reinsurance from rated counterparties as well as capital markets-based reinsurance through the issuance of MILNs. In a typical MILN structure, a mortgage insurer enters into a reinsurance agreement with a special purpose insurance company that subsequently issues securities to investors. The proceeds of those securities are placed in a reinsurance trust and used to make payments to the mortgage insurer under the terms of the reinsurance agreement. MILNs have become an important tool in dispersing concentrated risk and providing protection against elevated losses.

¹ SEC Press Release 2023-17 (Jan. 25, 2023) and published for comment at 88 Fed. Reg. 9678 (Feb. 14, 2023).

² GSE aggregate data and Home Mortgage Disclosure Act (HMDA) data.

We are concerned about the potential impact that the Reproposed Rule could have on MILN transactions as the Reproposed Rule does not define the term “synthetic asset-backed securities” or provide specific guidance regarding whether any specific products are synthetic asset-based securities. Under current language it appears that MILNs could be interpreted as synthetic securitizations, and the reinsurance agreements used in MILNs as prohibited conflicted transactions. We do not believe the Commission intended to capture MILN transactions in the Reproposed Rule. The structure of providing mortgage insurers with reinsurance on specified pools of mortgage insurance policies through MILNs has historically been approved by state insurance regulators and both Enterprises.

As you know, the Commission’s Reproposed Rule would implement Section 27B of the Securities Act of 1933. Section 27B was added by Section 621 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 prohibiting an underwriter, placement agent, initial purchaser, or sponsor of an asset-backed security, or any affiliate or subsidiary or such an entity, from engaging in transactions that would involve or result in material conflicts of interest. The Reproposed Rule and underlying legislation target the types of transactions tainted by conflicts of interest that were the subject of regulatory and Congressional investigations following the 2007-2009 financial crisis such as “bets” against the performance of securities issued to investors.

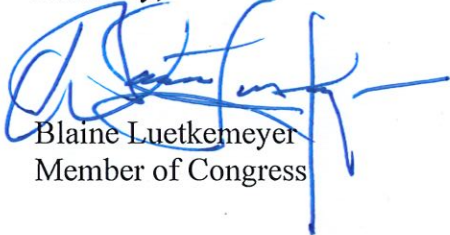
MILNs are a risk and capital management tool that do not give rise to the conflicted risks that Section 27B was intended to address. In a MILN transaction, the private mortgage insurer remains responsible for payment on the mortgage insurance policies in the pool, retains risk on the mortgage insurance policies that is not insured by the reinsurance agreement, and is only entitled to recover its actual losses incurred under the mortgage insurance policies. As a result, there is alignment of interest between the parties in MILN transactions since both private mortgage insurers and investors are incentivized for borrowers to be, and remain, successful as homeowners.

We understand these same concerns have been articulated by housing organizations in comments filed with the Commission.³ To address this issue, we suggest that the Commission clarify that MILNs are not synthetic asset-backed securitizations within the meaning of the Reproposed Rule and that the reinsurance agreements embedded in MILNs are not conflicted transactions. Any rule that may unintentionally restrict or prohibit the ability of private mortgage insurers to manage risk and capital may negatively impact homebuyers, lenders, and taxpayers. We also urge the SEC to consider the feedback of other market participants who may have other prudential activities that should not be included within the scope of a conflicted transaction.

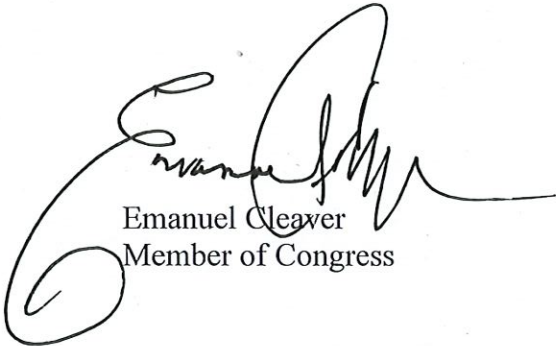
The Commission’s attention to striking the appropriate approach in prohibiting material conflicts of interest without restricting ordinary-course risk and capital management activities, including reinsurance transactions entered into by U.S. regulated insurers that utilize the capital markets, is appreciated. Securities transactions which give rise to material conflicts of interest should unquestionably be addressed. We look forward to engaging with you and your staff as the Commission moves toward finalizing a rule on this important matter.

³ HPC comment letter available at <https://www.sec.gov/comments/s7-01-23/s70123-20161796-330672.pdf>, MBA comment letter available at <https://www.sec.gov/comments/s7-01-23/s70123-20161722-330596.pdf>, SFA comment letter available at <https://www.sec.gov/comments/s7-01-23/s70123-20161787-330610.pdf>, and private mortgage insurance industry comment letter available at <https://www.sec.gov/comments/s7-01-23/s70123-20161715-330577.pdf>.

Sincerely,



Blaine Luetkemeyer
Member of Congress



Emanuel Cleaver
Member of Congress