STATEMENT OF TERESA BRYCE BEFORE THE SUBCOMMITTEE ON CAPITAL MARKETS, INSURANCE AND GOVERNMENT SPONSORED ENTERPRISES OF THE HOUSE COMMITTEE ON FINANCIAL SERVICES
June 16, 2009

I am Teresa Bryce, president of Radian Guaranty Inc. I am here today on behalf of the Mortgage Insurance Companies of America (MICA), the trade association representing the private mortgage insurance industry. The Subcommittee today is discussing critical issues on which to focus, issues that must be addressed before Congress considers pending initiatives to address systemic risk and U. S. insurance regulation. This debate is complex, and often overlooks the role insurance plays in mitigating risk to homeowners, retirees, families and corporations -- a role that must be preserved and promoted as broad financial reform legislation advances. We look forward to providing our expertise to the Subcommittee on our portion of the insurance industry.

I should note that the mortgage insurance (MI) industry is not significantly engaged in international activities, so I will not address these issues in my statement. In addition, MI does not pose systemic risk. To the contrary, the ability of mortgage insurers to pay claims under unprecedented stress has helped to stabilize the market despite the ongoing crisis. In my testimony, I will describe the capital and regulatory structure that has allowed private MI to play this critical role, a structure bank regulators are only now seeking to institute for insured depositories and their holding companies.

The mortgage insurers' reserve structure is mandated by state law. It has been a vital bulwark against systemic risk in housing finance and will play a critical role in the recovery. MICA thus supports maintaining this state regulatory structure. Federal regulators were in many ways less prepared with their capital standards and other requirements than the state insurance regulators who applied the existing rules governing MI.

Finally, I will also address how MI is helping with the housing recovery by responsibly expanding the number of new homebuyers. This, in turn, will restore overall investor confidence in the economy.

The Role of Mortgage Insurance

MI enables borrowers to buy homes with less than a 20% down payment because MI stands in front of investors if borrowers default. When the borrower defaults, the MI coverage pays the investor 20% to 25% of the loan amount plus expenses. That insurance payment, along with the proceeds from the sale of the house, makes up for much, but not all, of the investor's losses. Without MI standing in this first loss position, borrowers would have to put 20% down to buy a home.

Mortgage insurers are aligned with both the borrower and the investor (most prominently the Government Sponsored Enterprises (GSEs)), thus ensuring better quality mortgages. Mortgage insurers act as review underwriters for the credit and collateral risks related to individual loans. In effect, they are a second set of eyes determining the safety and soundness of

an individual mortgage. This role not only protects both borrowers and investors and helps to ensure that the home is affordable not only at the time of purchase, but throughout the years of homeownership.

Having their own capital at risk also means that mortgage insurers have very clear incentives to mitigate their losses if loans are in default. The best way to do that, of course, is to avoid foreclosures altogether by working with borrowers to keep them in their homes. Mortgage insurers have a history of partnering with lenders, investors and community groups to work with borrowers in default. This often means that, with the servicers' permission, mortgage insurers counsel the borrowers personally and determine if their financial problems can be resolved. In today's devastating mortgage market, mortgage insurers continue to play a leadership role in working with all parties, including with the Obama Administration. In 2008 alone mortgage insurers were able to save almost 100,000 people from losing their homes.

Since 1957, the private mortgage insurance industry has helped more than 25 million families buy homes. Today, the MI industry's capital stands behind almost 1 trillion of mortgage loans. That is approximately 10% of all home mortgages outstanding. In 2007 and 2008, mortgage insurers paid approximately $15 billion in claims and continue to significantly support their insured mortgage lender clients in 2009.

According to the 2007 Home Mortgage Disclosure Act (HMDA) data (the most recent data available), 51% of the borrowers who received mortgages insured by private mortgage insurers made less than area median income and 35% made less than 80% of area median income. The income distribution of mortgage insurers customers combined with the fact that numerous studies have determined that the lack of a substantial down payment is the major barrier to homeownership leads us to believe that a substantial share of our purchase business is comprised of first-time homebuyers who would not be able to get into an affordable home without the benefit of mortgage insurance.

Strong Reserve and Regulatory Structure to Better Manage Risk

The backbone of the industry's financial strength is its state-imposed reserve requirements. The requirements are specifically structured to address the long-term nature of MI risk. They enable the industry to withstand a sustained period of heavy defaults arising from serious regional or national economic downturns, as well as routine defaults and claims that occur normally throughout the cycle.

Mortgage insurers are required to keep three types of reserves, the most important of which is the contingency reserve. Half of each premium dollar earned goes into the contingency reserve and generally cannot be touched by the mortgage insurer for a 10-year period. It ensures that significant reserves are accumulated during good times not only to handle claims under stress, but also to avoid boom-bust cycles. Therefore, unlike other financial institutions that may pay high dividends during profitable periods, MI companies build their contingency reserves during these periods in order to have the capital ready to pay the higher claims that inevitably occur during periods of market corrections such as the one the U.S. is now experiencing.

Mortgage insurers' contingency reserves are directly comparable to the "dynamic provisioning" bank regulators now know they need. Mortgage insurers are subject to similar mortgage default risk as banks but only mortgage insurers raise capital counter-cyclically. Bank regulators are only now working to construct a similar system for banks in the U.S. and around the world, with Chairman Bernanke recently highlighting this as a critical initiative.

The history of the MI industry proves that they have paid their claims through good and bad economic cycles. For example, in the early 1980s, the mortgage market had to cope with double-digit interest rates and inflation in a period of severe recession and, therefore, introduced many experimental adjustable-rate mortgages. As economic conditions deteriorated—particularly in energy-oriented regions of the country—defaults began to rise, resulting in numerous foreclosures. The MI industry paid more than $6 billion in claims to its policyholders during the 1980s. In the early 1990s, the MI industry paid more than $8 billion in claims primarily in California and the Northeast. Policyholders included the GSEs, commercial banks, savings institutions, institutional mortgage investors, mortgage bankers, the Federal Deposit Insurance Corporation, and the Federal Savings and Loan Insurance Corporation.

The attached appendix is composed of three charts. They show how the MI industry statutory structure and resulting capital build-up allowed it to handle these various regional recessions described above. Mortgage insurers built capital after the oil patch recession and then were able to pay claims during the recessions in California and the Northeast. Once again the industry built capital so mortgage insurers are able to meet the challenges of today.

The other two reserves that mortgage insurers must maintain are case-basis loss reserves and unearned premium reserves. Case-basis loss reserves are established for losses on individual policies when the insurer is notified of defaults and when foreclosures occur. Premiums received for the term of a policy are placed in unearned premium reserves and are earned over time in accordance with state regulation.

Beyond the reserves requirements, state regulators have detailed and comprehensive regulations designed to protect policyholders. State insurance regulation addresses among other things, the licensing of companies to transact business, policy forms, claims handling, financial statements, periodic reporting, permissible investments, adherence to financial standards, and premium rates. The premium rates and policy forms are generally subject to regulation in every state and are intended to protect policyholders against the effects of excessive, inadequate or unfairly discriminatory rates and to encourage competition.

Sustainable and Affordable Housing

As the Subcommittee knows, the members of MICA have requested capital assistance from Treasury. I want to emphasize that we are not asking for assistance because we cannot meet our claim obligations. As previously noted the industry's rigorous reserve system assures mortgage insurers can pay their claims. However, with additional capital, we could work more effectively with our lender and investor partners to expand the mortgage market which, in turn, would help spur the economic recovery.

One of the unique features of the MI industry is the way in which mortgage insurers' capital supports significant incremental growth in housing. First, it enables people to responsibly purchase homes with less than a 20% down payment, thus enabling them to buy homes much sooner than they otherwise could. Since many of those home buyers are lower-income or first-time home buyers, their purchases enable homeowners who are ready to "trade-up" their existing homes to do so.

MI also provides capital relief for banks who originate and hold mortgages with a loan-to-value ratio (LTV) greater than 90%. This frees up bank capital to prudently support more mortgage lending. Importantly, the GSEs are our largest and primary counterparties. Mortgage insurers' private capital stands in front of loans held by the GSEs, enabling them to better serve the mortgage market.

As illustrated in the table below, every billion dollars of capital mortgage insurers hold translates into approximately $100 billion of new funding for home purchases. This means there will be 666,667 new mortgage loans.

Value of MI Capital
(per every $1 billion dollars invested)

New Mortgage Funds Insured	$100 billion
Average MI coverage	25%
Incremental Risk Insured	$ 25 billion
Risk to Capital Ratio	25:1
Average Insured Loan Amount (for home purchase loans)	$150,000
Number of Incremental Homes Financed	**666,667**

Such a capital investment would dramatically benefit housing and housing finance, enable more borrowers to realize the dream of homeownership on terms they can afford and sustain, and generally restore investor confidence in the overall U.S. economy. Industry estimates call for $2.3 trillion and $2.0 trillion in originations for 2009 and 2010, respectively, with as much as 20% being low-down payment mortgages that will require MI. That means mortgage insurers will be asked to provide approximately $840 billion of new insurance written, which in turn translates into a need for $7 billion to $10 billion in new capital investment to support that production. With this capital flexibility, over six million new loans could be insured, facilitating a reduction in the unprecedented levels of excess housing inventory that the market is currently experiencing.

MICA has worked closely with the Federal Housing Finance Agency (FHFA) in the industry's request for assistance from the Treasury Department. FHFA is the regulator of the GSEs and since the vast majority of privately insured loans are held by the GSEs, it is imperative that FHFA understand the value MI brings when its capital stands in front of the GSEs on their riskiest loans. In fact, shortly after Director Lockhart came to FHFA's predecessor agency MICA began to have regular meetings with him and his staff to discuss MI issues as they relate to the GSEs.

FHFA has been fully supportive of the industry's request to Treasury and we have worked in partnership with them in our attempt to receive capital assistance. The state insurance regulators from the states where MICA's members are domiciled also have spoken frequently with the FHFA on our behalf. Indeed, Director Lockhart testified before this subcommittee two weeks ago that he supported MICA's request for assistance. We are extremely grateful for his support and pledge to continue to work with FHFA to ensure that the GSEs are properly protected.

Systemic Risk

MICA believes it is absolutely critical for Congress, Treasury and regulators – including state insurance agencies – to grapple with the dangers firms and products can pose to the financial system as a whole. However, neither private mortgage insurance firms nor private mortgage insurance contracts pose systemic risk, as has been proven throughout this crisis. To the contrary, mortgage insurance is part of the solution.

The reason why MI does not now or in the future pose systemic risk is simple. Mortgage insurers' substantive reserve requirements have long included a critical counter-cyclical provision that bank regulators are only now putting in place for the banking system. This capital at risk is buttressed with disciplined underwriting that has ensured that MIs can meet anticipated claims.

MICA has no specific suggestions on ways to address systemic risk in the broader financial market. However, one reason MICA supports action to address systemic risk is that the industry problems we are experiencing today are largely the result of systemic risks outside the control of private MI and its regulatory construct. As noted, mortgage insurers can meet current claims because our capital requirements are designed even for catastrophic situations.

Conclusion

Once again, thank you for the opportunity to comment. As you will note, MICA strongly supports the state regulatory system and, indeed, believes that structure has ensured that mortgage insurers can continue to meet their obligations during these very challenging times. We also would like to more significantly help in the economic recovery by giving deserving lower-income and first-time homebuyers a leg up on the homeownership ladder. With some assistance we believe that we can do that to the fullest extent possible.

Appendix

Chart A

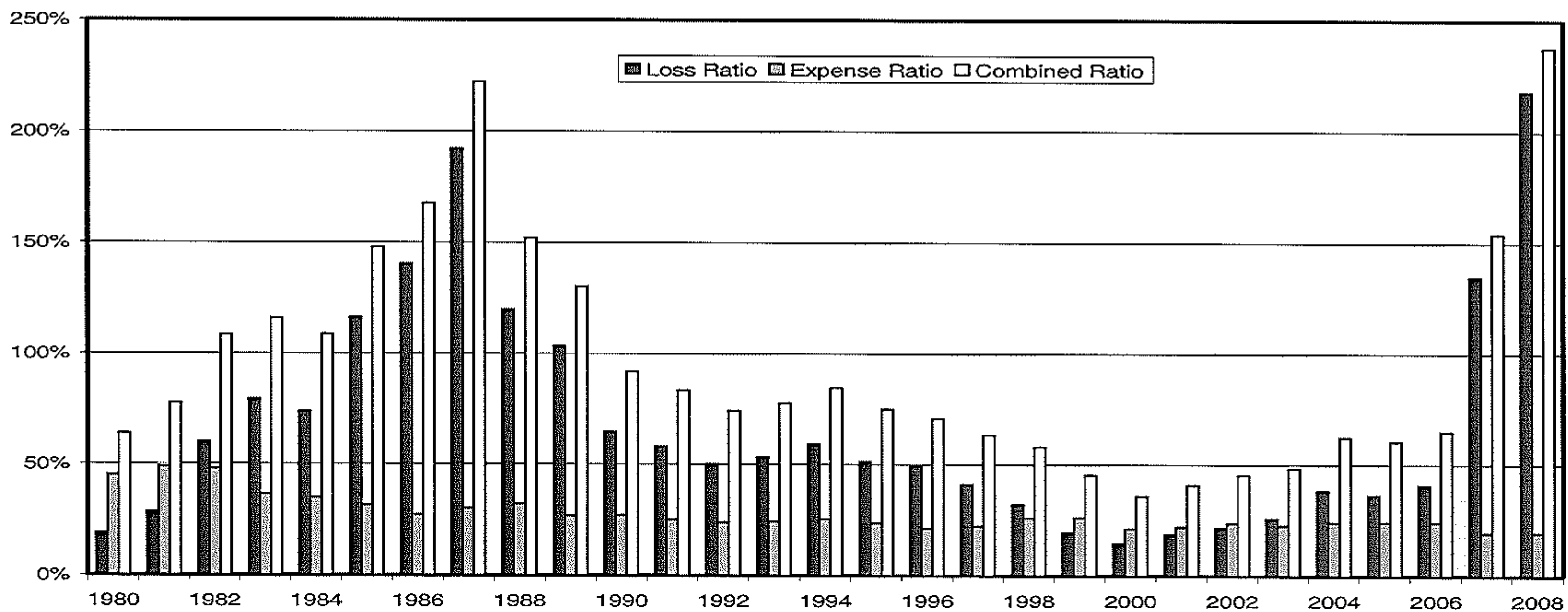

Chart A above shows the critical ratios for the MI industry from 1980 through 2008. The current stress in the housing market matches that experienced by the MI industry during the oil patch decline of the mid-1980s. However, note that the annual combined ratios exceeded 100% or more for eight straight years beginning in 1982 and the industry paid all claims and grew during that period. The reason for the continued strong claims paying ability of the MI industry is tied to its state capital and reserve requirements.

Chart B

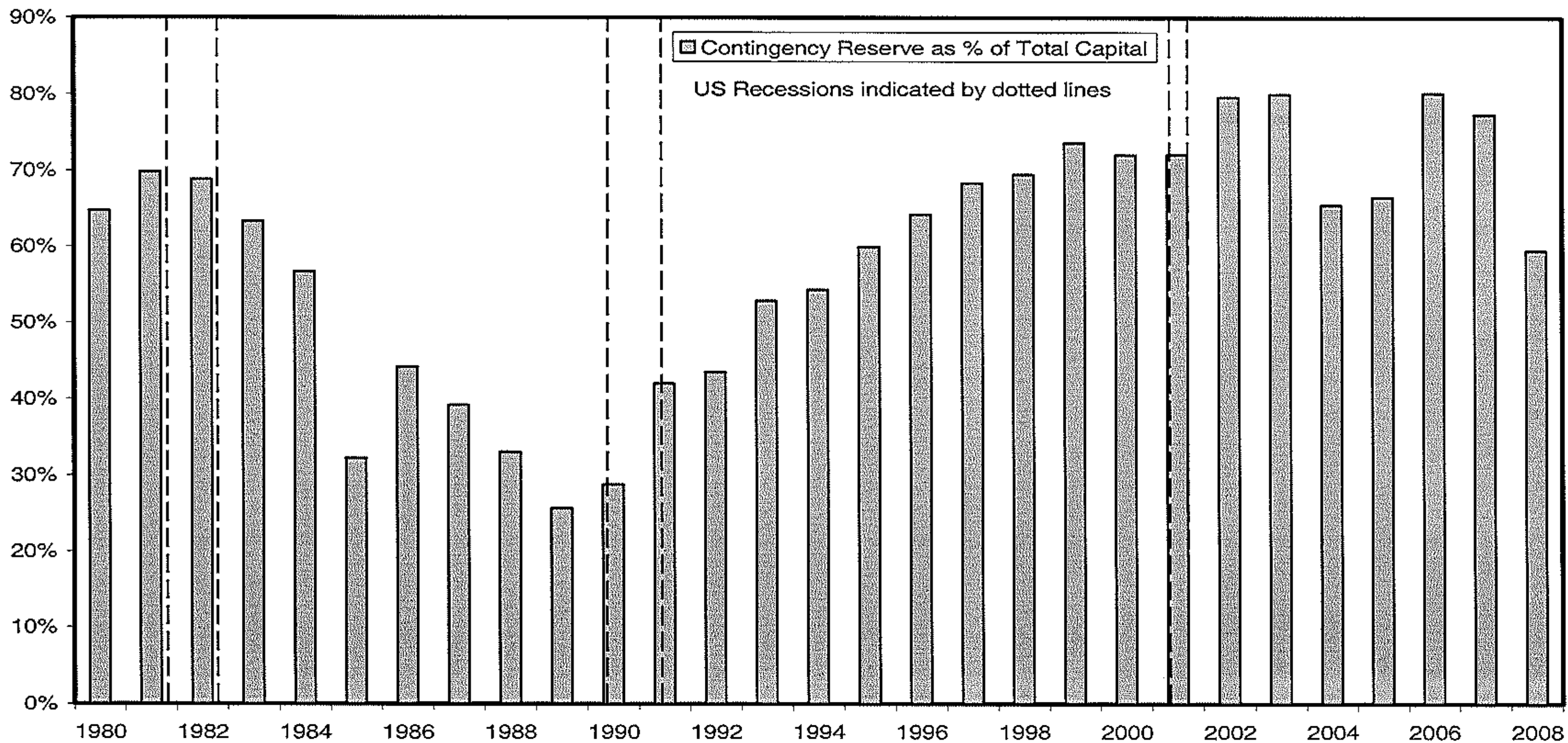

Chart B above shows how contingency reserves are built up during periods of low claims and economic prosperity to be used during periods of economic stress as we are currently experiencing.

Chart C

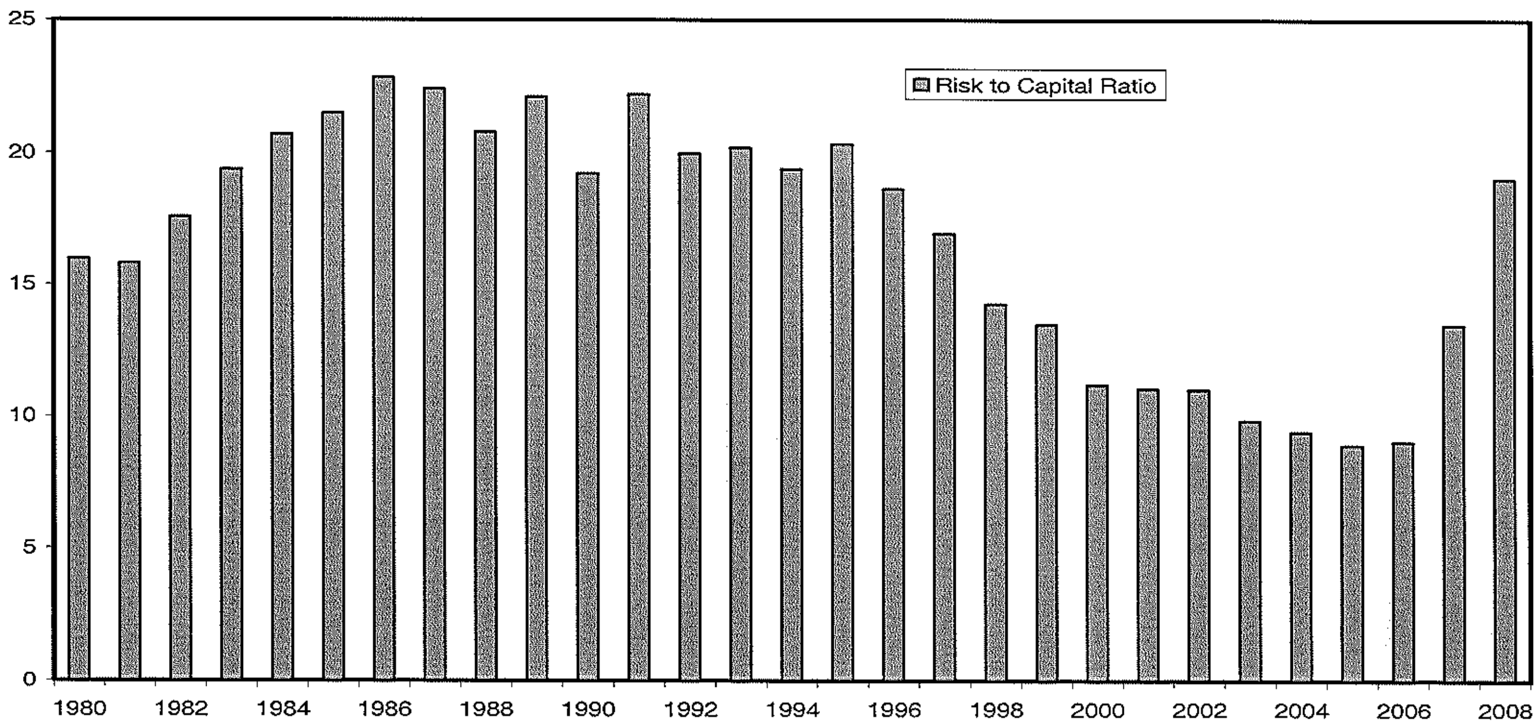

Chart C above shows the industry risk to capital ratio which now stands at 19 to 1, but still below levels seen in the mid-1990s and well below the levels reached during the mind-1980s house price declines.