Private Mortgage Insurance and Housing Finance Reform

- Strong state-based regulation is currently in place to monitor the activity of private mortgage insurers (PMIs), and efforts are underway to strengthen it further. Given recent experiences with the financial crisis, state insurance regulators are in the process of making changes to the NAIC Mortgage Guaranty Model Act, and it is anticipated that all the states primarily responsible for regulation of Private Mortgage Insurers will adopt the updated version soon after it is finalized.

- State insurance regulators have a long history of carefully balancing our dual mission to protect policyholders by ensuring the solvency of the PMIs we regulate while also ensuring the availability and affordability of coverage for consumers.

- Any federal housing finance reform legislation must not unintentionally destabilize the PMI markets by creating a new regulatory structure that duplicates and potentially undermines state insurance regulatory efforts to achieve their dual mission.

Private mortgage insurance, sometimes called “default insurance” or “mortgage guaranty insurance,” protects lenders against losses when a homeowner defaults on a loan. It is used to transfer risk from lenders to PMIs until the homeowner has more than 20% equity in the property, providing increased flexibility to both the homeowner and the lender. The homeowner pays the insurance premiums, but the lender is the policy beneficiary. The amount of loss coverage is usually capped as a proportion of loan principal.

State insurance regulators require PMIs to follow strict requirements, including but not limited to adequate capital and reserving (including special contingency reserves), restrictions on investment and geographic concentrations, limits on non-mortgage activities, risk-to-capital ratios, and minimum policyholder positions. As with other lines of insurance, all policy forms, premium rates, and financial statements must be filed with and approved by state insurance departments. In light of lessons learned from the financial crisis, state insurance regulators are in the process of making adjustments to the regulation of PMIs, including the creation of a mortgage insurance specific risk-based capital formula and placing prohibitions on affiliated captive insurers. It is anticipated many of these changes will be adopted by the NAIC this year and by individual states shortly thereafter.

In applying these requirements, state insurance regulators seek to protect policyholders and ensure a robust, competitive market so mortgage insurance can be available and affordable to those who need it most. Even in the depths of the financial crisis, when PMIs, like other financial institutions faced significant stress, state insurance regulators through their flexible authorities ensured that the PMI market remained viable and continued to provide coverage, thereby helping to avoid an even worse housing market meltdown. Today, 5 years later, in part due to the actions of state insurance regulators, new capital has entered the market and the PMI market has bounced back.
Recent housing finance reform proposals, particularly in the Senate, seek to provide a new federal regulator, charged with administering a proposed government guarantee, with authorities to set standards for private mortgage insurers that are duplicative to the already existing state regulatory standards. State insurance regulators are concerned that if this new regulator’s authorities are too broad, it will be incentivized to exercise its authorities in such a way that it will go beyond protecting the proposed government guarantee and undermine state regulators’ efforts to protect policyholders and ensure a robust and affordable private mortgage insurance market. State regulators, through the NAIC, have been working with Congress to ensure that this new regulator’s authority is appropriately tailored to protect the taxpayer guarantee.

**Key Points**

- Mortgage insurance provides increased flexibility for both homeowners and lenders by transferring risk until the homeowner has more than 20% equity in the property.

- State insurance regulators’ robust and flexible authorities during the recent financial crisis allowed them to help the PMI industry survive, thereby avoiding an even worse housing market meltdown.

- State regulators are concerned that recent legislative proposals to create a new federal regulator to administer a taxpayer guarantee provide authorities that are too broad to achieve this narrow purpose and, through the NAIC, are working with Congress to ensure that its authorities do not undermine state regulators’ dual mission of protecting policyholders and ensuring available and affordable coverage.