

January 8, 2021

Dr. Mark A. Calabria
Director
Federal Housing Finance Agency
Constitution Center
400 7th Street SW
Washington, DC 20219

Dear Director Calabria:

U.S. Mortgage Insurers (USMI)¹ represents America’s leading providers of private mortgage insurance (MI) and our members are dedicated to a robust housing finance system backed by private capital that enables access to affordable housing finance credit for all home-ready borrowers while simultaneously protecting taxpayers. The MI industry has more than 60 years of expertise in underwriting and actively managing mortgage credit risk to balance access to affordable mortgage credit while protecting Fannie Mae and Freddie Mac (the Enterprises or GSEs) and American taxpayers from mortgage credit-related losses. During that time, the MI industry helped more than 33 million households achieve sustainable homeownership, including more than 1.5 million in the past year alone.

USMI appreciates the opportunity to comment on the Federal Housing Finance Agency’s (FHFA) Notice of Proposed Rulemaking (NPR) on “Prior Approval for Enterprise Products”² and to share our industry’s perspectives on this important rulemaking. This NPR is designed to replace the FHFA’s 2009 Interim Final Rule³ which established a process for the GSEs to obtain prior approval for new products and provide prior notice for new activities, and the MI industry welcomes this action. USMI has long called for a more transparent and objective process for reviewing new products and activities at the GSEs and we commend the FHFA for proposing a framework that builds on the 2009 Interim Final Rule, recognizes its shortcomings and elements of subjectivity, and acknowledges developments in the market over the past 12 years. We note that this transparency and objectivity is especially important given the government-conferred advantages and responsibilities granted by the GSE charters⁴ that, unchecked, could cause the GSEs to act in ways that stifle competition and disadvantage other market participants.

During their more than 12 years in conservatorship, the GSEs have significantly expanded their role in the housing finance system by developing and introducing numerous new products and activities, including via “pilots,” without meaningful transparency into their economics, risk, or consumer impact. While innovation can certainly play a role in better serving homebuyers, it is critical that new pilots, products, and activities be subject to a transparent assessment that provides stakeholders with the opportunity to comment on the potential impact to both consumers and non-GSE market participants. USMI welcomes FHFA’s initiative to set forth a transparent and objective approval process to ensure proper oversight of the GSEs’ expansion into new areas of the market, that private capital plays a

¹ USMI’s membership comprises the following private mortgage insurance companies: Essent Guaranty, Inc.; Genworth Mortgage Insurance Corporation; Mortgage Guaranty Insurance Corporation; National Mortgage Insurance Corporation; and Radian Guaranty, Inc.

² 85 Fed. Reg. 71276 (November 9, 2020).

³ 74 Fed. Reg. 31602 (July 2, 2020).

⁴ Fannie Mae Charter, 12 U.S.C. 1716 *et seq.*; Freddie Mac Charter, 12 U.S.C. 1451 *et seq.*

significant role in the housing finance system, and that consumers are well served, all consistent with the GSEs' statutory charters. Our responses to specific questions posed by the NPR can be found below.

1. FHFA requests comments on the scope of the criteria for identifying a new activity, specifically on whether they are sufficient for capturing an activity that would require an Enterprise to submit Notice of a New Activity to FHFA.

Proposed Section 1253.3⁵ outlines the tripartite test for identifying a new activity that would trigger the Notice of a New Activity requirements:

- 1) Business line, practice, offering, or service provided on a standalone basis or as part of the business line, practice, offering, or service; AND
- 2) Not provided as of the final rule's effective date or is an enhancement, alteration, or modification to an existing activity; AND
- 3) Requires new resource, data, policy, process, or infrastructure, expands the scope or increases level of risk to the GSE, involves a new category of borrower, investor, counterparty, or collateral, would substantially impact the mortgage finance system or safety and soundness of the GSE, is a pilot, or results from a pilot.

USMI strongly supports the inclusion of "pilots" in the criteria for identifying new activities, consistent with the 2009 Interim Final Rule. Categorizing a new offering as a "pilot" appears to have been routinely used by the GSEs during conservatorship to launch new initiatives, including expansions into areas long considered to be functions of the primary mortgage market, without adhering to the processes contemplated by the 2009 Interim Final Rule. This has included pilots for guaranteeing loans for single-family rental (SFR) properties, financing a select group of large non-bank entities to support mortgage servicing rights (MSR), executing lender risk sharing credit risk transfer (CRT) transactions, and utilizing less regulated and capitalized forms of credit enhancement – Fannie Mae's "Enterprise-Paid Mortgage Insurance" (EPMI) and Freddie Mac's "Integrated Mortgage Insurance" (IMAGIN). All of these were developed without soliciting input from industry stakeholders and, at the sole discretion of the GSEs, were often available only to certain market participants. Going forward, it is important that this rule close the loopholes that could be used again to circumvent the objectives of the proposed framework.

Further, USMI also supports the broad definition of "pilot" in the proposed Section 1253.2⁶ to ensure that the approval process is "substance over form" and captures activities that are pilots in everything except name. USMI urges the FHFA to require the GSEs to halt all current pilots and, following the implementation of a final rule, require the GSEs to submit Notices of New Activity should they want to continue to offer such products and programs. As the FHFA endeavors to increase oversight of pilots and transparency for the approval of new products, existing pilots should not be subject to any grandfather clause since they were never subject to the review contemplated

⁵ 85 Fed. Reg. 71283 (November 9, 2020).

⁶ 85 Fed. Reg. 71283 (November 9, 2020). A "pilot" is "an activity that has a defined term and scope for purposes of understanding the viability of a new offering. A pilot may also be referred to as testing initiative, test and learn, temporary authorization, or other names."

by the 2009 Interim Final Rule.⁷ At a minimum the final rule should provide greater clarity on the precise process governing current pilot programs that the GSEs seek to convert to permanent product offerings or activities.⁸

2. FHFA requests comments on whether the criteria used to identify a new activity are unambiguous and transparent or, if not, how they can be improved.

The proposed Section 1253.9⁹ outlines the process by which a GSE would submit a Notice of New Activity to the FHFA, as well as the requisite elements of the submission. While the NPR would require the GSEs to submit comprehensive information about a new activity as part of the Notice of New Activity, it does not require that the submission and contents of the Notice be made public. Industry stakeholders will only know about a Notice of New Activity if the FHFA determines it is in fact a new product, thereby triggering a 30-day public comment period. To increase transparency regarding new activities at the GSEs and FHFA's review actions, USMI recommends that the final rule include a requirement for FHFA to maintain a page or portal on its website to publicly post Notices of New Activity submitted by the GSEs. This would ensure that industry participants are fully aware of the GSEs' intent to engage in a new activity and promote a level of transparency that has not always existed in the marketplace between the GSEs and other housing finance stakeholders. USMI supports the FHFA's intention behind the proposal to synchronize processes at the GSEs with regard to the introduction of new activities and products in order to promote uniform transparency.

Recognizing that the GSEs are critical components of the housing finance system, the FHFA must balance robust assessment of new activities and adequate flexibility for the GSEs to react to market development and conditions. The proposed Section 1253.3(a)(3)(ii)¹⁰ states that an "activity that expands the scope or increases the level of credit risk, market risk, or operational risk to the Enterprise" is one characteristic of a business line, practice, offering, or service that would meet the third requirement for triggering a Notice of New Activity. As proposed in the NPR, this requirement could potentially allow certain activities to evade review and prior approval by the FHFA. For example, asserting that a new activity is designed to *decrease* risk could be enough to circumvent the notice and approval requirement, thereby bypassing review and public comment that could challenge the GSE's view on risk. Accordingly, USMI recommends that this section be modified to read: "Activity which *changes* the level of credit risk, market risk, or operational risk to the Enterprise."

⁷ The GSEs have introduced numerous pilots with little to no transparency and the FHFA has directed the GSEs to end several pilots after analysis revealed a lack of necessity in the market. See FHFA, Determination on Enterprise Activity in the Single-Family Rental Market (August 21, 2018); FHFA, End of Mortgage Servicing Rights Financing Pilot Program (September 18, 2019); FHFA, Credit Risk Transfer Progress Report: 4Q 2019, commentary on lender risk sharing, page 14 (April 3, 2020).

⁸ While the NPR is clear with regard to pilots that are cancelled prior to the implementation of the final rule and for which a GSE wants to re-engage (85 Fed. Reg. 71279, Example 2 – Activity Which Is a Pilot), it is less clear about a current pilot that continues to exist and for which a GSE wants to expand or make permanent. The NPR stipulates that re-engaging in cancelled pilots, for example facilitating the financing of SFR properties, would require a Notice of New Activity but it does not provide clarity on active pilots, such as EPMI and IMAGIN.

⁹ 85 Fed. Reg. 71285 (November 9, 2020).

¹⁰ 85 Fed. Reg. 71284 (November 9, 2020).

3. FHFA requests comments on how the exclusion for the automated underwriting systems as set forth in the Safety and Soundness Act should be applied to related but independent system and to future technology systems.

The proposed Section 1253.3(b)(1), consistent with the 2009 Interim Final Rule, stipulates that a new activity excludes “The automated underwriting system of an Enterprise, including any upgrade to the technology, operating system or software to operate the underwriting system.”¹¹ This exclusion, however, should be narrowed to only apply to the features that are included in the GSEs’ automated underwriting systems (AUSs) as of the effective date of the final rule. Further, any new benefit, protection, right, relief, or change to the origination process – as well as activities traditionally associated with the primary mortgage market – should be considered new activities and outside the scope of the proposed exclusion. In order to fully understand the parameters of the Section 1253.3(b)(1) exclusion, the final rule should clearly indicate the specific technologies and systems that are included in the GSEs’ AUSs. This guidance will promote transparency in the housing finance system and ensure that all industry participants understand what *is* and *is not* captured by this exclusion.

Importantly, the exclusion does not cover technologies that are not part of the GSEs’ AUSs, such as offerings that evaluate the appraised value of a property – Fannie Mae’s Collateral Underwriter (CU) and Freddie Mac’s Home Value Explorer (HVE) or Loan Collateral Advisor. While these technologies will predate the implementation date of the final rule, future changes would trigger Notice of New Activity requirements as provided by the NPR. USMI supports this element of the NPR since changes to collateral analysis can broadly impact the safety and soundness of the housing finance system. This is an important component of the NPR that will increase transparency in the market and ensure that market participants understand, and support, changes to the GSEs’ appraisal requirements and processes.¹²

4. FHFA requests comments on whether the exclusions should be narrowed or expanded, consistent with the Safety and Soundness Act.

The proposed Section 1253.3(b)(2) stipulates that a new activity excludes “Any modification to the mortgage terms and conditions or mortgage underwriting criteria relating to the mortgages that are purchased or guaranteed by an Enterprise, provided that such modifications do not alter the underlying transaction so as to include services or financing, other than residential mortgage financing.”¹³ While the GSEs and other market participants periodically modify their underwriting requirements based on market developments, it is important that the FHFA and industry have the opportunity to assess potential changes to the GSEs’ underwriting criteria which could materially impact their credit box and consumers’ access to conventional mortgage financing. The final rule should amend this exemption to balance the GSEs’ ability to manage the risk on mortgages in their

¹¹ 85 Fed. Reg. 71284 (November 9, 2020).

¹² For example, during the ongoing COVID-19 pandemic, the GSEs have dramatically increased the use of appraisal waivers but the parameters and accompanying compensating factors have not been uniformly applied or publicized by the GSEs. The NPR, however, would address this issue and increase the information available to market participants and the public.

¹³ 85 Fed. Reg. 71284 (November 9, 2020).

pipelines and visibility into their underwriting criteria which, due to their size and centrality in the housing finance system, essentially set the rules for the market.

While the GSEs and private MI companies have strong working relationships and open channels of communication regarding underwriting changes, USMI fully supports additional policies that encourage robust engagement and optimize collaboration between private market participants and the GSEs to best serve borrowers and protect taxpayers. USMI strongly believes that increased transparency into the credit decisioning of the GSEs, documentation processes, and underwriting technologies would greatly improve the ability of private market participants to support the conventional mortgage market. Data such as the compensating factors used by the GSEs during the underwriting process should be made available to better inform potential homebuyers and credit risk takers, such as private MIs, and could also help facilitate greater participation from other private markets, including private label securitization (PLS), CRT, and portfolio lending.

5. FHFA requests comment on any other factors FHFA should include in the consideration of whether a new product is in the public interest.

Various aspects of the NPR include an analysis of whether a new activity or product is in the public interest, most notably as it relates to consumers' access to affordable mortgage finance. This is a critical component for a prior approval framework and ensures that a proposed activity or product has an identified purpose prior to its approval, is in the public interest and not merely the interest of the GSEs, and does not negatively impact access to credit or market participants' role in the housing finance system. Factors for determining whether a new product is in the public interest, the NPR include: (1) the degree to which the new product is being or could be supplied by other market participants; and (2) the degree to which the new product promotes competition in the marketplace or, to the contrary, would result in less competition.¹⁴ USMI supports these factors in the FHFA's proposed review framework and believes it is critical that the FHFA assess whether a new product or activity would: (1) disintermediate private capital and, in particular, compete against market participants that they effectively regulate;¹⁵ or (2) allow the GSEs to operate in a manner that is beyond the scope of the secondary market functions set forth in their charters. USMI proposes that the NPR be revised to provide additional clarity and oversight as set forth below:

- 1) The degree to which private market participants are meeting or could meet the needs of the market and consumers, and whether the new activity or product would disintermediate non-GSE market participants. The GSEs should not be permitted to leverage their statutory advantages to engage in new activities or offer new products that other market participants can provide on similar terms with similar consumer advantages.
- 2) Consideration of whether the new activity or product would rely on limited or broad participation by market participants. Many of the GSEs' pilots have been introduced and operated using a single or severely limited number of companies from a particular industry. For example, the GSEs exercised sole discretion with inviting market participants to

¹⁴ Proposed Section 1253.4(b)(3)-(4). 85 Fed. Reg. 71284 (November 9, 2020).

¹⁵ For example, entities that participant in Freddie Mac's IMAGIN and Fannie Mae's EPMI pilots insure the same mortgage credit risk as private MIs yet they are not subject the GSEs' PMIERs which were developed after a public notice and comment period and are periodically revised. These are standards that require private MIs to routinely submit detailed financial and pricing information to the GSEs, and also include extensive operational requirements that give the GSEs insight into private MIs' underwriting policies and portfolio composition.

participate in their MSR financing and credit enhancement pilots, thereby picking winners and losers among market participants.

- 3) Examination of how certain market participants will be selected over others, whether the activity or product will be made available to other market participants on similar terms, and whether other participants would be harmed by the engagement in the activity or product.
- 4) Consideration of whether the new activity or product would present a conflict of interest for the GSEs, especially where anti-competitive concerns may be present, such as when the GSEs may be seeking to engage in activities while effectively regulating market participants already engaged in such activities or offering such products.

6. FHFA requests comment on whether the scope of the exclusion described in proposed §1253.8 is too broad or too narrow, given the requirements of the Safety and Soundness Act.

The proposed Section 1253.8¹⁶ would permit a GSE to offer a new product – both the “same as the original new product” and one that is “substantially similar to the original new product” – that the FHFA previously approved for the other GSE. Such a product would not be subject to a public notice and comment period and the GSE would merely need to submit an abbreviated notice to the FHFA stating: (1) the name of the activity/product that is substantially similar to the previously approved new product at the other GSE; (2) a complete and specific description; and (3) an explanation of why the new product is substantially similar to the previously approved new product at the other GSE.¹⁷ As proposed, this exclusion is unnecessarily broad since “substantially similar” is not a defined term in the NPR and represents a subjective determination without clear metrics. The 2009 Interim Final Rule, however, included “substantially similar” as a defined term in its Section 1253.2¹⁸ with factors and criteria that the FHFA would consider and USMI recommends that the NPR be amended to either include “substantially similar” as a defined term or modify the proposed Section 1253.8 to retain the specific elements¹⁹ referenced in the Interim Final Rule.

The exclusion contained in proposed Section 1253.8 should be designed in a manner such that the approval framework is not unnecessarily duplicative but ensures that safeguards are in place to fully assess the second GSE’s new product. Absent a regulatory opportunity for industry stakeholders to provide comments and observations on market trends following the approval of the first product and articulate concerns for expanding the product to the other GSE, the FHFA should consider changes to the required elements of the “abbreviated notice” outlined in the proposed Section 1253.8. USMI recommends that the abbreviated notice include a requirement that the GSE clearly

¹⁶ 85 Fed. Reg. 71285 (November 9, 2020).

¹⁷ *Id.*

¹⁸ 74 Fed. Reg. 31605 (July 2, 2009).

¹⁹ *Id.* When determining if an activity/product is “substantially similar” the FHFA may consider if it: represents an update to the way an approved product is delivered; poses a significant change in risk to the Enterprise or the mortgage finance system from a previously approved product or activity; involves a significant changes in terms, conditions, or limitations expressly contained in any prior approval granted; poses a significant change in its effect on the public interest compared to a previously approved product or activity; poses a significant change from a previously approved product or activity and if so, does a tradeoff exist in the composite of risk, public interest, and safety and soundness elements in the proposed new activity; is it likely to have significantly more Enterprise resources dedicated to it; and requires approval by regulators other than FHFA, including Federal, State, or local regulators.

explain, to its best knowledge, any differences between the first approved product and the second product and identify the technologies, systems, and resources it possesses that will allow the new product to be offered in a manner that complies with its charter, serves the public interest, and does not disintermediate private capital in the housing finance system.

7. FHFA requests comment on the content of a Notice of New Activity, specifically whether the requirements are clearly stated and sufficient for evaluating a New Activity.

The proposed Section 1253.9 outlines the required content of a Notice of New Activity for purposes of: (1) assessing the impact, risk, and benefits of the new activity; and (2) determining whether the new activity is a new product that merits public notice and comment.²⁰ While this proposed section would require a GSE to submit a thorough analysis of a new activity, USMI recommends the following modifications to the requirements:

- 1) Section 1253.9(a)(5) should be amended to require the GSE to describe: (1) the extent to which the activity or product is already provided by market participants; and (2) the impact on market participants' and consumers' access to credit.
- 2) Section 1253.9(a)(9) should be amended to require the GSE to describe: (1) any proposed relationship with market participants; and (2) the rationale for the specific market participants chosen if the activity or product is only available to one or a select group of entities instead of the entire industry.

10. In addition to the questions asked above, FHFA requests comment on any aspect of the proposed Prior Approval for Enterprise Products rule.

As drafted, the NPR does not include a requirement or mechanism for the FHFA to assess a new activity or product's performance and operation in the marketplace once approved. USMI suggests that FHFA consider a mandatory "lookback" to confirm that the new offering performed as contemplated. USMI recommends that the FHFA conduct an examination of each new product following six months of being offered and that the resulting analysis be publicly available on the FHFA's website and included in the agency's annual report to Congress.

The proposed rule would allow a GSE to offer a new product if the FHFA receives a Notice of New Activity, deems it a "new product," facilitates a 30-day public comment period, and "If the Director does not make a determination within 30 days after the end of the public comment period."²¹ This would essentially create an assessment framework where "silence is deemed approval" and permit the GSEs to offer new products without a direct determination from the FHFA. While we acknowledge that this element of the proposed rule is based on a statutory²² requirement, the FHFA should explore whether to recommend that Congress amend the existing statute to remove the "silent approval" option and require that new products may only be offered after a formal approval by the FHFA.

²⁰ 85 Fed. Reg. 71285 (November 9, 2020).

²¹ Proposed Section 1253.6. 85 Fed. Reg. 71285-6 (November 9, 2020).

²² 12 USC 4541(c).

Further, it would be beneficial for the FHFA to have discretion to allow for an extension of the notice and comment period if requested by impacted stakeholders and deemed appropriate by the FHFA. Likewise, the FHFA should have flexibility with regard to assessment timelines in the event of a national emergency or disaster to ensure proper feedback from industry participants and adequate time to review the new product. The proposed rule's timelines are mandated by statute²³ but FHFA should consider whether to recommend that Congress amend the statute to permit FHFA to exercise such flexibilities for the new product review process. Events such as the current COVID-19 pandemic are circumstances that could warrant extensions in the public comment period, or other timelines, to ensure proper review and oversight of proposed products.

A well-functioning housing finance system should provide consistent access to affordable mortgage credit for borrowers across the nation and through all parts of the credit cycle without putting taxpayers at undue risk. USMI supports the FHFA's initiative to conduct proper oversight of the GSEs' activities and products to ensure compliance with their congressional charters and best serve borrowers as well as the broader housing finance system. Questions or requests for additional information may be directed to Lindsey Johnson, President of USMI, at ljohnson@usmi.org or 202-280-1820.

Sincerely,



Lindsey D. Johnson
President
U.S. Mortgage Insurers

²³ 12 USC 4541.