



Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

January 14, 2004

Interpretive Letter #985
February 2004
12 CFR 5.36(e)

Subject: Proposed Group Mortgage Reinsurance Program

Dear []:

This responds to your letter dated October 16, 2003, requesting the OCC's confirmation that a national bank's non-controlling investment, made directly or indirectly through an operating subsidiary, in [] (the "Reinsurer"), would qualify for the notice process in 12 C.F.R. 5.36(e) because the activity of the Reinsurer is substantively the same as that of a group mortgage reinsurance facility previously authorized by the OCC. The Reinsurer is an association captive insurance company that will provide mortgage reinsurance on the loans of its participating financial institutions ("Participating Banks") and their affiliates and subsidiaries.

As explained below, we conclude that the activities of the Reinsurer are substantively the same as those of a group mortgage reinsurance facility previously authorized by the OCC. Accordingly, a national bank seeking to make a non-controlling investment, directly or indirectly through an operating subsidiary, in the Reinsurer, may use the notice procedure available under the OCC's regulations at 12 C.F.R. § 5.36(e), if the bank otherwise qualifies under the criteria of that section.

I. Background

The Reinsurer was organized under the sponsorship of the [] ("ABC") as an association captive insurance company¹ pursuant to Vermont's captive insurance law (Title 8 of the Vermont Statutes Annotated, Chapter 141). The Vermont Commissioner of Banking, Insurance, Securities and Health Care Administration (the "Vermont Commissioner")

¹ Captive insurers insure or reinsure risks related to the business of their owner(s) and are subject to special insurance regulations. Association captives are a type of captive insurer, all of whose participants or owners are also members of a sponsoring industry association or similar group (in this case, the [ABC]), and which insures or reinsures only risks relating to its members.

approved the [ABC]’s application to organize the Reinsurer and granted it a Certificate of Authority to conduct business on [*date*].

Pursuant to the Reinsurer’s Business Plan filed with the Vermont Commissioner, ownership of the Reinsurer’s common stock is limited to member financial institutions of the [ABC] and their subsidiaries and affiliates. Participating Banks are not liable for the Reinsurer’s reinsurance obligations or other debts and liabilities.² The Reinsurer’s authorized activities consist solely of reinsuring the mortgage insurance coverage³ issued by non-affiliated third party mortgage insurers with respect to loans originated, purchased or serviced by the Participating Banks and their subsidiaries and affiliates. Any material change in the Reinsurer’s Business Plan, including the writing of any direct insurance or any other kind of reinsurance, requires the prior approval of the Vermont Commissioner.

As a licensed Vermont captive insurance company, the Reinsurer will be subject to ongoing supervision and regulation by the Vermont Commissioner, and its operations will be limited to those specified in its Certificate of authority from the Vermont Commissioner (mortgage reinsurance). Any material change in the Reinsurer’s Business Plan, including the writing of any direct insurance or any other kind of reinsurance, requires the prior approval of the Vermont Commissioner. In return for accepting the limited credit risk associated with the program, the Reinsurer will receive reinsurance premiums.

The Reinsurer has entered into a Reinsurance Agreement with [] (“Co.”), a [*state*] monoline mortgage insurance company, to assume (reinsure) a portion of [Co.]’s risk on mortgage insurance it provides on residential mortgage loans originated, purchased, or serviced by the Participating Banks, or their affiliates or subsidiaries. The Participating Banks’ credit underwriting analysis and decision-making in connection with insured mortgage loans will not be delegated to [Co.], or any other party. [Co.] will perform its own independent insurance underwriting evaluation of loans submitted for coverage by a particular Participating Bank (other than Participating Banks approved by [Co.] for delegated underwriting⁴) and will accept for mortgage insurance only those loans that

² The Reinsurer is organized as a Vermont corporation. Under Vermont law, the shareholders of a corporation are not personally liable for the acts and debts of the corporation. *See* 11A V.S.A. § 6.22.

³ Mortgage insurance protects an investor holding a mortgage loan against the risk of default by the mortgagor. Lenders generally require that borrowers obtain mortgage insurance on low down payment loans (generally loans having a down payment of less than 20% or a loan-to-value ratio in excess of 80%). Mortgage insurance serves an important function by assisting low and moderate-income families to become homeowners. Mortgage insurance also has expanded the secondary market for low down payment mortgages and the funding available for these loans. *See* Interpretive Letter 828 (citing Mortgage Insurance Companies of America 1995-1996 Fact Book).

⁴ [Co.] may approve delegated underwriting authority for certain Participating Banks. A lender with delegated underwriting authority has the ability to bind mortgage insurance coverage for a loan that it approves utilizing [Co.]-approved underwriting criteria. [Co.] periodically reviews that lender’s exercise of its delegated authority to insure that its credit underwriting criteria are being properly and consistently applied. Generally, lenders approved for delegated underwriting are those that generate a significant loan volume and have exhibited a proven favorable track record in the performance of their insured loan portfolios.

meet its underwriting criteria. You represent in your letter that it is expected that [Co.]’s underwriting criteria will be applied by the Participating Bank as a supplement to their own particular organization’s underwriting criteria, and will thus ensure homogeneity among the Participating Banks in the standards for origination and approval of reinsured loans.

II. The Reinsurer’s Activities are Substantively the Same as Activities Previously Approved by the OCC

A. Reinsurer’s Activities are Substantively the Same as Previously Approved Activities

Pursuant to OCC regulations at 12 C.F.R. § 5.36(e), well managed, well capitalized national banks may make a non-controlling investment directly, or indirectly through an operating subsidiary, in an enterprise that engages in certain pre-approved activities or activities that are “substantively the same” as activities previously approved in published OCC precedent. The pre-approved activities, which are listed in 12 C.F.R. § 5.34(e)(5)(v), include “reinsuring mortgage insurance on loans originated, purchased, or serviced by the bank, its subsidiaries, or its affiliates. . . .”⁵ The activities of the Reinsurer, however, involve reinsuring mortgage insurance on the loans of unaffiliated financial institutions. In this respect, the Reinsurer’s activities are substantively the same as activities previously approved by the OCC. Specifically, the Reinsurer’s activities are substantively similar to the reciprocal mortgage reinsurance exchange (the “Exchange”) activities the OCC approved as being part of, or incidental to, the business of banking, in Interpretive Letter No. 828 (April 6, 1998) (“IL 828”).⁶

In IL 828 the OCC authorized national banks to participate in a reciprocal mortgage reinsurance exchange that provided for the reinsurance of mortgage insurance on loans originated or purchased by participating lenders.⁷ Participants in the Exchange used the Exchange arrangement as a means to reinsure their own mortgages. Similarly, Participating Banks will use the reinsurance arrangement as a means of reinsuring their own mortgages. In both situations, the risks assumed by the banks are essentially the same risks associated with underwriting mortgage loans. The analysis of the permissibility of the Exchange participants’ activities described in IL 828 applies equally to the activities of the Participating Banks in this case, and supports the conclusion that participation in the Reinsurer’s program is a permissible activity.

⁵ 12 C.F.R. § 5.34(e)(5)(v)(Q).

⁶ The Exchange described in IL 828 differs from the Reinsurer in that the Exchange is not a separate legal entity, but rather, exists as a relationship among the participating lenders that is established through agreements. The Reinsurer, on the other hand, is a separate incorporated legal entity. The reinsurance activities of the Exchange and Reinsurer, however, are substantively the same.

⁷ Like the Reinsurer in this case, the Exchange was a Vermont group captive insurer open to participation by nonaffiliated financial institutions; and like the Reinsurer, the Exchange provided economies of scale to small to mid-size banks which would otherwise have been unable to maintain a captive mortgage reinsurance facility of their own.

B. Application of Section 302 of the Gramm-Leach-Bliley Act

Under Section 302 of the Gramm-Leach-Bliley Act (“GLBA”), national banks and their subsidiaries may not provide insurance products as principal, except for “authorized products.” The term “authorized products” is defined to include any product that the OCC had determined in writing, as of January 1, 1999, that national banks may provide as principal, or that national banks were in fact lawfully providing as principal, provided that, as of such date, no court had rendered a final judgment overturning such determination. Thus, Section 302 of the GLBA preserves the authority of national banks and their subsidiaries to provide an insurance product as principal so long as the product was authorized by the OCC on or before January 1, 1999.

The Participating Banks’ mortgage reinsurance activities constitute authorized products. The OCC authorized national banks and their subsidiaries to reinsure mortgage insurance prior to January 1, 1999.⁸ Further, in IL 828, issued on April 6, 1998, the OCC determined that the authority to reinsure mortgage insurance included national banks’ participation in the Exchange, a group mortgage reinsurance facility involving unaffiliated lenders. These determinations had not been overturned by any court as of January 1, 1999 (nor have they been overturned subsequent to that date). Accordingly, mortgage reinsurance, including such reinsurance offered through a group facility involving unaffiliated lenders, satisfies the “authorized product” exception in Section 302 of the GLBA.⁹

III. Conclusion

Accordingly, the activities of the Reinsurer are substantively the same as those of a group mortgage reinsurance facility previously authorized by the OCC, and thus, a national bank

⁸ See, e.g., Corporate Decisions No. 97-97 (November 10, 1997) (First Tennessee); No. 97-93 (October 20, 1997) (SunTrust); No. 97-89 (September 26, 1997) (Norwest); No. 97-27 (May 2, 1997) (Bank One); No. 97-15 (March 17, 1997) (PNC); and No. 97-06 (January 22, 1997) (Chase); and Interpretive Letter No. 743, *reprinted in* [1996-1997 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶81-108 (October 17, 1996).

⁹ See also, Corporate Decision 2001-10 (April 23, 2001) (OCC approved, after January 1, 1999, credit-related reinsurance activities in connection with loans of both affiliated and unaffiliated lenders, because the OCC had established the authority of national banks and their subsidiaries to reinsure credit-related products in connection with the bank’s and other lenders’ loans, prior to January 1, 1999).

seeking to make a non-controlling investment, directly or indirectly through an operating subsidiary, in the Reinsurer, may use the notice procedure available under 12 C.F.R. § 5.36(e),¹⁰ if the bank otherwise qualifies under the criteria of that section.

Sincerely,

- signed -

Julie L. Williams
First Senior Deputy Comptroller and Chief Counsel

¹⁰ If a national bank seeks to make a non-controlling investment in the Reinsurer through an operating subsidiary, the bank must ensure that it complies with the applicable requirements of 12 C.F.R. § 5.34.