The Florida Senate

BILL ANALYSIS AND FISCAL IMPACT STATEMENT

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

Prepared By: The Professional Staff of the General Government Appropriations Committee

BILL: SB 2084

INTRODUCER: Senator Richter

SUBJECT: Mortgage Guaranty Insurers/Surplus Requirements

DATE: April 13, 2010 REVISED:

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Messer	Burgess	BI	**Favorable**
2.	Johansen	McKee	FT	**Favorable**
3.	Frederick	DeLoach	GA	**Favorable**
4.				
5.				
6.				

I. Summary:

When a lending institution makes a loan to a homebuyer, it often requires that an insurance policy be written on the loan that compensates the lender in the event that the borrower fails to make payments on the loan. This type of insurance is written by mortgage guaranty insurers, which are regulated by the Office of Insurance Regulation (office). This bill grants the Commissioner of Insurance Regulation, within the Office of Insurance Regulation, discretion to grant a temporary exception to mortgage guaranty insurers with regard to the current minimum capital surplus requirements. Mortgage guaranty insurance companies may request such an exception and the Commissioner of Insurance Regulation, at his discretion, will determine whether to grant the temporary exception.

This bill substantially amends section 635.042, Florida Statutes.

II. Present Situation:

Mortgage Insurance

Mortgage insurance is insurance coverage which compensates lenders in the event that the borrower defaults on a mortgage. Lenders typically require mortgage insurance for any mortgage loan that is in excess of 80 percent of the value of the mortgaged property. Because many homebuyers are unable to make a down payment of 20 percent, mortgage insurance is a prevalent component of Florida's housing market. Mortgage insurance makes it possible for qualified buyers to purchase a house with a smaller down payment, allowing them buy a home sooner than they otherwise could. The use of mortgage insurance is most common among first-time homebuyers.

Mortgage Insurance Capital Surplus Requirements

Mortgage insurance companies are required to maintain a sound financial structure and adequate reserves to ensure that they can meet their obligations. Minimum surplus and capital requirements for mortgage guaranty insurers writing business in Florida are included in s. 635.042, F.S. This section requires that a mortgage insurer maintain a minimum surplus of the greater of $4 million or 10 percent of its liabilities.[1] Insurers must also possess sufficient capital and surplus so that their outstanding aggregate exposure (net of reinsurance) does not exceed 25 times the insurer's paid-in capital, surplus, and contingency reserve combined. In effect, an insurer is required to set aside one dollar of capital for every $25 of risk it insures, and is prohibited from writing new business when its risk-to-capital ratio reaches 25 to 1. This is an inflexible limit and the office currently has no discretion to broaden this limit.

The 25-to-1 ratio is likely based on a study that was performed a half century ago, which suggested that a prudent reserve ratio for the industry was between 12.5 to 1 and 40 to 1.[2] To date, 16 states require a 25 to 1 surplus ratio.[3] These 16 states appear to have picked a point near the middle of the study's recommended range.

Mortgage guaranty insurers are required to establish and maintain a contingency reserve pursuant to s. 635.041, F.S. This reserve requires insurers to set aside 50 percent of every earned premium dollar and to maintain contributions made to the reserve. Upon approval by the mortgage guaranty insurer's state of domicile and 30 days' notice to the office, the contingency reserve will be made available to a mortgage guaranty insurer only when the insurer's incurred losses in a calendar year exceed 35 percent of earned premiums.

III. Effect of Proposed Changes:

This bill amends s. 635.042(2), F.S., to grant the Commissioner of Insurance Regulation the discretion to allow a temporary exception to the capital requirements for mortgage guaranty insurers. The bill provides that the Commissioner of Insurance Regulation may grant a temporary exception from these requirements, on a case-by-case basis, upon a finding that the mortgage guaranty insurer's financial position is reasonable in relationship to the mortgage guaranty insurer's aggregate insured risk and financial needs.

This act takes effect July 1, 2010.

[1] Section 635.042, F.S., provides that an insurer is never required to maintain surplus in excess of $100 million.
[2] See James A. Graaskamp and Richard M. Heins, *Mortgage Loan Guaranty Reconsidered—An Objective Study of Modern Mortgage Loan Default Insurance—Its Economics, Law, Regulation, and Administration as Related to Reserve Adequacy*, 1961.
[3] Those states are: Arizona, California, Florida, Idaho, Illinois, Iowa, Kansas, Kentucky, Missouri, New Jersey, New York, North Carolina, Ohio, Oregon, Texas and Wisconsin.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

V. Fiscal Impact Statement:

A. Tax/Fee Issues:

None.

B. Private Sector Impact:

This bill attempts to ensure that mortgage insurance companies will continue to provide coverage on new loans. If these companies cease writing new coverages, the private sector will experience a decline in new mortgages and home purchases.

By lowering insurers' capital requirements, there is an increased risk that such insurers may become insolvent. If mortgage insurers were to become insolvent, the state's lenders could experience losses. However, this bill appears to protect against this risk by providing requirements that the Commissioner of Insurance Regulation must consider before granting the capital surplus exception.

C. Government Sector Impact:

The Office of Insurance Regulation may experience a temporary increase in workload to conduct the required reviews of insurers seeking an exception to minimum surplus requirements. However, the office has indicated that the increased workload will be absorbed within current resources.

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

VIII. Additional Information:

A. Committee Substitute – Statement of Substantial Changes:

(Summarizing differences between the Committee Substitute and the prior version of the bill.)

None.

B. Amendments:

None.