Office of the Comptroller of the Currency
Board of Governors of the Federal Reserve System
Federal Deposit Insurance Corporation
Office of Thrift Supervision

Interpretive Letter #1058
May 2006
12 CFR Part 3

April 20, 2005

Suzanne C. Hutchinson
Executive Vice President
Mortgage Insurance Companies of America
1425 K. St., NW
Washington, D.C. 20005

Dear Ms. Hutchinson,

Thank you for your recent letters regarding the agencies' risk-based capital rules and supervisory processes governing structured second mortgages. The agencies are aware of your views and concerns with respect to the elevated credit risk related to high loan-to-value (LTV) financing. The agencies have issued interagency guidance[1] that indicates an institution will come under supervisory scrutiny as the total of all loans in excess of the supervisory LTV limits, including high LTV residential real estate loan exceptions, approach 100 percent of total capital.

The agencies regularly review our existing examination policies, procedures, and capital standards and make revisions when warranted. Regarding the capital treatment associated with second liens, the agencies provided you with an interpretative letter dated March 17, 2003. The agencies are still of the view that second mortgages would not meet the definition of a recourse arrangement even when the first and second mortgages were made to the same borrower simultaneously. The agencies view the second mortgage as a separate transaction that does not – in and of itself – serve as a credit enhancement.

As you may know, the agencies are considering modifications to update our existing risk-based capital standards to ensure our capital rules remain broadly representative of risks present in the banking system. The agencies intend to consider the existing capital requirements on residential mortgages in connection with this effort. Also, to reiterate a point made in Acting Comptroller Julie Williams' January 28, 2005 letter addressed to you, the agencies are in process of developing guidance to reinforce and clarify our expectations

[1] Interagency Guidance on High LTV Residential Real Estate Lending, October 8, 1999.

regarding risk management practices for home equity lending. We expect banks to have appropriate risk management controls in place to manage the growth and changing product terms, structure, and underwriting in home equity lending, including use of high LTV home equity credits extended as part of structured mortgage transactions.

Should you have additional questions, please contact Tom Boemio, Senior Project Manager, Policy, Federal Reserve Board (202-452-2982), Nancy Hunt, Risk Expert, OCC, (202-874-5211), Jason Cave, Chief, Capital Markets Policy, FDIC (202-898-3548), or David W. Riley, Senior Analyst (Capital Policy), OTS (202-906-6669).

Sincerely,

/s/

Barbara Bouchard
Deputy Associate Director
Federal Reserve Board

/s/

William A. Stark
Associate Director
Federal Deposit Insurance Corporation

/s/

Tommy Snow
Director, Capital Policy
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/s/

Michael D. Solomon
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