August 1, 2011

VIA E-MAIL TO
regs.comments@occ.treas.gov
Office of the Comptroller of the Currency
250 E Street, S.W., Mail Stop 2-3
Washington, D.C. 20219
Re: Docket Number OCC-2011-0002

VIA E-MAIL TO Reg-Comments@fhfa.gov
Alfred M. Pollard, Esq., General Counsel
Federal Housing Finance Agency, Fourth
Floor
1700 G Street, N.W.
Washington, D.C. 20552
Re: RIN 2590-AA43

VIA E-MAIL TO
regs.comments@federalreserve.gov
Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve
System
20th Street & Constitution Ave., N.W.
Washington, D.C. 20551
Re: Docket No. R-1411

VIA E-MAIL TO rule-comments@sec.gov
Elizabeth M. Murphy, Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090
Re: File Number S7-14-11

VIA E-MAIL TO Comments@FDIC.gov
Robert E. Feldman, Executive Secretary
*Attention:* Comments
Federal Deposit Insurance Corporation
550 17th Street, N.W.
Washington, D.C. 20429
Re: RIN 3064-AD74

SUBMITTED ELECTRONICALLY TO
www.regulations.gov
Regulations Division
Office of the General Counsel
Department of Housing and Urban
Development
451 7th Street, S.W., Room 10276
Washington, D.C. 20410-0500
Re: FR-5504-P-01; Credit Risk Retention

Ladies and Gentlemen:

The undersigned ten Federal Home Loan Banks ("FHLBanks") are writing to comment on the proposed rule and request for comment on credit risk retention published on April 29, 2011 (the "Proposed Rule"). 76 Fed. Reg. 24090. The Proposed Rule has been jointly issued by the U.S. Treasury Department's Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the U.S. Securities and Exchange Commission, the Federal Housing Finance Agency ("FHFA") and the Department of Housing and Urban Development. The Proposed Rule seeks to implement the credit risk retention requirements of § 941 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, 15 U.S.C. 780-11, which generally requires a securitizer to retain not less than 5% of the credit risk of the assets which underlie the asset-backed securities. The Act includes a variety of exemptions, including one for asset-backed securities that are collateralized exclusively by residential mortgages that qualify as "qualified residential mortgages." The undersigned FHLBanks appreciate the opportunity to submit the following comments.

## I. Summary.

We are writing to share the experiences gained over the past decade managing successful FHLBank mortgage purchase programs that include credit risk retention features. These mortgage programs (herein referred to as "Acquired Member Assets Programs" or "AMA Programs") use a unique structure that allows a member of a participating FHLBank (a "Member") to retain a significant portion of the credit risk of the fixed-rate mortgages it originates when selling conventional loans to the FHLBanks. They demonstrate how credit risk retention can work to benefit mortgage lenders and American consumers. These programs are popular with smaller community financial institutions because they provide an alternative to the traditional secondary market that can be difficult or prohibitively costly for many community financial institutions to access. Approximately 1,500 FHLBank member institutions, typically community banks, thrifts and credit unions, have used these programs to fund about $235 billion of mortgages that have helped homebuyers in every State, including large numbers of low and middle income buyers, purchase a new home or lower the cost of their existing home through refinancing. These programs offer valuable insights and lessons about structuring credit risk retention for residential mortgages. For example, the AMA Programs establish the amount of risk to be retained in connection with a loan based on its individual risk characteristics whereas the Proposed Rule requires the same 5% risk be retained for all loans regardless of the likely risk presented by a specific loan.

Given their popularity and success, we are also writing to ensure that the AMA Programs will be allowed to continue unaffected by the Proposed Rule. While the essential activities of the AMA Programs would not be affected by the Proposed Rule, we wish to clarify that other aspects of the AMA Programs, such as the sale and purchase of participation interests in AMA Program loans between FHLBanks would not be subject to the Proposed Rule. We also suggest that any future securitizations of AMA Program loans be exempt from the Proposed Rule because risk retention is already an integral aspect of these programs. Subjecting the AMA Programs to the Proposed Rule would significantly reduce their ability to customize the fit between the credit risk of each loan and the credit enhancements required of the Member that originates the loans.

## II. The AMA Programs.

### A. AMA Program Risk Retention Structure.

Pursuant to 12 C.F.R. Part 955, promulgated by the FHFA, and with its approval and continuing oversight, many FHLBanks have established programs whereby they acquire or fund conventional and government-insured residential mortgage loans originated and serviced by Members, known as Acquired Member Assets ("AMA"). The FHLBanks' AMA Programs include the Mortgage Partnership Finance® ("MPF®") Program (established in 1997)[1] and the Mortgage Purchase Program ("MPP") (established in 2000). The majority of participants in the AMA Programs are small to mid-sized community banks, thrifts and credit unions.

[1] "Mortgage Partnership Finance," "MPF" and "MPF Xtra" are registered trademarks of the Federal Home Loan Bank of Chicago.

The loan products available through the AMA Programs use an effective risk-sharing structure that seeks to allocate the risks of fixed-rate mortgages between the originating Members, which retain the principal credit risk, and the FHLBank investors that take the interest rate risk for each loan.[2] Members originating AMA Program loans, which are predominately community banks, thrifts and credit unions, know their customers and the properties better than any secondary market entity can. Members' knowledge of their customers and their local housing market puts them in a better position to underwrite the loans than any secondary market entity or investor. These Members continue to bear the primary credit risk responsibility for the mortgage loans they make by providing a credit enhancement to the FHLBank purchasing the loans, which effectively requires them to retain a significant portion of the credit risk of their loans. As government-sponsored enterprises with immediate access to the capital markets, the FHLBanks provide community lenders an outlet to sell fixed-rate mortgages in order to manage capital, interest rate risk and liquidity.[3] In this way, the component risks of fixed-rate mortgages are better allocated than in the traditional secondary market approach and result in more efficient, risk-adverse financing structures.

The amount of credit enhancement for which participating lenders are responsible is determined by a sophisticated and objective model that calculates for each individual loan the dollar amount of enhancement -- beyond the borrower's equity and any primary mortgage insurance -- necessary to provide a layer of credit protection on a pool of assets equivalent to at least an "investment grade" security and more typically a AA-rated security.[4] Pool level adjustments are also made, providing additional safety. Evaluating the credit characteristics of each loan allows Members to determine whether to make the loan, and therefore accept the accompanying credit enhancement, or not to make the loan. In this way, each Member and FHLBank can determine for itself the amount of risk it is willing to take.

Under this structure, Members are rewarded for their credit judgments and expertise. Members are typically compensated, (through fees or payment of price hold-backs), based on the performance of the loans they have delivered to an FHLBank. The better the loans perform, the more income Members receive. Depending on the AMA program, lenders can receive this compensation monthly or in accordance with a predetermined schedule. To the extent that losses are experienced due to delinquencies, the compensation may be reduced or eliminated by the

---

[2] The majority of products offered through the AMA Programs are intended to be sold to a Member's FHLBank to be held in portfolio by the purchasing FHLBank, with the exception of the MPF Xtra® Product, where loans are concurrently sold to Fannie Mae without a credit risk retention feature. In addition. MPF Xtra loans are originated and serviced by community lenders. which. as discussed further above, have a business interest in making loans that are appropriate for their customers and that will perform over time. In fact, the historical credit performance of MPF Xtra loans has been superior to the national averages. For the remainder of this commentary, when referring to the AMA Program or the MPF or MPP Programs or AMA Program loan products, we refer to those with a credit risk retention structure.

[3] The subject of the Proposed Rules is the management of credit risk. The AMA Programs allocate other types of risk associated with mortgage loans among investors and originators, but, to stay within the scope of the Proposed Rule, this comment letter addresses only credit risk.

[4] For example, as specifically approved by the FHFA, the MPF Program and the MPP Program utilize Standard and Poor's proprietary LEVELS model as a part of its methodology for assessing the amount of credit risk that must be retained by a Member for loans sold to an FHLBank. Other models potentially could be used, subject to regulatory approval.

FHLBank until the losses are recovered. As an additional safety feature, the amount of credit enhancement provided by the Members is secured at all times either by high quality collateral pledged to the FHLBank as the investor in the mortgage loans or held and controlled by the investing FHLBank until payment is due based on loan performance.

B. AMA Program Results.

The AMA Programs provide FHLBank Members with an attractive alternative to selling their conventional mortgages in the secondary mortgage market. The AMA Program structure is essentially the opposite of that used by Fannie Mae and Freddie Mac, under which the originator relinquishes the credit responsibility in exchange for deducting a guarantee fee from the purchase price of each loan. Rather than setting minimum credit standards that loans must meet, and providing no price benefit for exceeding that bar, the AMA Programs incentivize lenders to create high quality mortgage loans regardless of whether they deliver one loan or one million loans. Rather than pricing loans based on the volume of loans delivered, the AMA Programs price mortgages based on their underlying credit characteristics, rewarding mortgage lenders for their credit expertise.

1. AMA Programs Have Been Popular with Community Lenders.

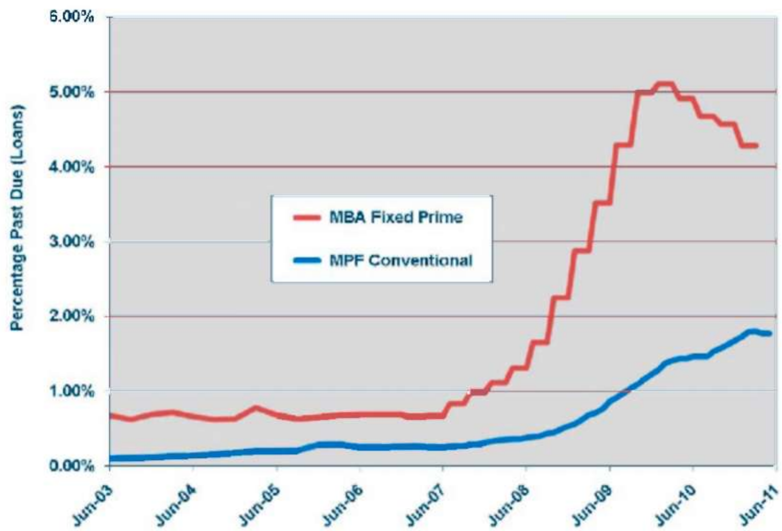
Since their inception, the AMA Programs have proven popular with FHLBank Members. For example, since 1997 when the MPF Program was launched, nearly 1,500 FHLBank financial institutions across the country have been approved to participate. These lenders have financed more than $235 billion of conventional and government-insured loans through these programs, helping approximately 1.6 million American families in every state, the District of Columbia, Puerto Rico and the Virgin Islands, buy a new house or lower the cost of their existing home through refinancing. The programs are focused on helping American homebuyers – including large numbers of lower and middle-class Americans – achieve the dreams of homeownership. For example, the median size of an MPF loan is $128,242.

Members of all sizes have used AMA Program loan products to finance the housing needs of their customers. However, the AMA Programs have been particularly popular with smaller and mid-sized community financial institutions that typically originate low volumes of conventional mortgages. These lenders cannot effectively compete with larger originators that receive much more favorable pricing in the secondary mortgage market. The AMA Programs have allowed many of these smaller lenders to be able to offer traditional fixed-rate mortgages to their customers at competitive rates. Without them, such lenders would not be able to compete effectively in the mortgage markets, which would further concentrate the markets in favor of a few dominant originators.

2. AMA Program Credit Experience Has Been Exceptional.

The overall credit performance of AMA Program loans is and always has been dramatically better than the national average for similar fixed-rate, prime quality, conventionally-sized mortgages. This has remained true throughout the housing downturn. The AMA Programs' risk retention structure appeals to community lenders who use traditional underwriting standards when making credit judgments. They have no interest in originating the kinds of non-traditional, exotic loans that created the current mortgage crisis. Community lenders value the long-term customer relationship that comes with making a mortgage and they work hard to ensure their customers receive a mortgage loan appropriate for their financial situation. Because they know their customers and their housing markets so well, they welcome the opportunity to retain a portion of the credit risk of their loans and earn fees based on their performance.

The chart below shows the historical comparison between delinquency rates (90+ days) of conventional loans originated or funded through the MPF Program versus the national average for such single-family conventionally-sized mortgages. Both in the years before the financial crisis and throughout its peak, MPF loan default rates have been only about one-quarter to one-third of the national average. MPP loans similarly have demonstrated exceptionally low loan delinquency and default rates. The performance of AMA Program loans demonstrates significantly superior credit quality over the national average.




*Sources: 1- to 4-Unit Fixed-Rate Mortgages (not seasonally adjusted) from the MBA National Delinquency Survey; FHLBanks.*

As of March 31, 2011, more than \$181.3 billion of MPF loans with a credit enhancement structure[5] had been funded through the Program since it began in 1997. Of these, \$146.4 billion were conventional loans, while the remaining were FHA, VA, or other government-insured or government-guaranteed loans. Despite funding \$146 billion of loans, the total amount of conventional loan losses (net of gains) through March 31, 2011 were only \$53.6 million, or 0.0366%. About half of these losses, \$27.8 million, were recaptured simply by reducing the amount of monthly fees paid to Members, meaning Members only incurred \$25.8 million in actual losses on an operating basis. In return, these Members collectively have received fees from the FHLBanks of \$616 million for managing the credit risks of their loans; that is, for every dollar of loss actually realized by Members, they have received \$23.88 of fees. While the MPP Program uses a somewhat different fee structure, the historical performance of MPP loans is

[5] Excludes MPF Xtra loans.

substantially similar to that of MPF loans. These statistics help explain why the AMA Programs are so popular with Members.

## III. Lessons from the FHLBank AMA Programs.

The high quality of AMA Program loans is a result of the structure of the programs and the incentives they create. Members share in the credit risk of the loans they underwrite and have an incentive to originate only high-quality loans and to service them according to the highest standards. These programs enable Members to maintain positive, long-term relationships with their customers throughout the lives of their mortgage loans. These programs offer several lessons to be considered when developing a risk retention program for the U.S. housing finance market.

A. Rewarding Credit Quality, not Mortgage Volume, Will Allow Community Lenders to More Effectively Compete.

Members of all sizes have found value in the AMA Programs' risk retention structure. Large and mid-sized Members typically have sold the programs their highest quality mortgage loans that will generate the most credit enhancement fee income. While larger Members have found the programs useful to their mortgage business, many smaller Members have found them critical. As described earlier, the AMA Programs often have been the only way smaller lenders can be competitive and offer long-term, fixed-rate mortgages to consumers within their communities.

Historically, community banks, thrifts and credit unions have been an important component in the growth and development of the American middle-class by offering long-term, fixed-rate mortgages that have been the bedrock of American homeownership since the 1930s. However, due to the development of the secondary mortgage market over the past 25 years, community lenders have become increasingly disenfranchised as larger mortgage originators, including Fannie Mae and Freddie Mac grew to dominate the secondary market and capture most of the profits. Fannie Mae's and Freddie Mac's pricing structure rewards mortgage volume, rather than mortgage quality. As a result, smaller financial institutions have had difficulty competing in the origination market despite the excellent credit quality of their loans. The AMA Programs have succeeded because they have allowed community lenders to continue doing what they do best – serving their local customers. These lenders have no problem retaining the credit risk of their customers because they know them well and are therefore better able to underwrite them appropriately. The pricing structure of the programs rewards their credit expertise and customer service. The pricing paid to Members is competitive regardless of the level of production. The combination of the excellent underwriting performed by community lenders together with the rewards involved in the AMA Programs (competitive upfront pricing and delayed compensation paid to community lenders based on quality loan performance) has led to their success.

Assuming the Congressional impetus for the risk retention requirement was to give incentives to lenders to originate higher quality loans by keeping a certain amount of "skin in the game," then the lenders should be rewarded for their credit expertise. The current structure of the secondary mortgage market thwarts this effort by continuing to reward mortgage volume, making it difficult for smaller lenders to compete. As efforts continue to revamp and rethink the American housing finance system, thought should be given to how to broaden the market and increase choices for homebuyers by allowing community financial institutions to once again compete effectively in this important market.

B. <u>Mortgage Credit Risk Should Be Distributed Among Multiple Parties, Not Concentrated.</u>

A central weakness of the current secondary mortgage market, as dominated by Fannie Mae and Freddie Mac, is how it concentrates the credit risks of most U.S. mortgages into these two entities – with disastrous results, as the financial crisis has demonstrated. These weaknesses would be perpetuated under the Proposed Rule, which concentrates the credit risk associated with pooled mortgage assets in only a few companies. Because large-volume mortgage originators receive the best prices in the secondary market, U.S. mortgage credit risk tends to be concentrated in only a few large financial institutions. Fannie Mae and Freddie Mac currently account for more than $5 trillion of mortgage credit risk. Under the Proposed Rule, the credit risk for a pool of securitized assets would be held by the securitizer of the pool with the possible sharing of the risk with a few large originators. If one such entity failed, the effect on the market, and possibly taxpayers, could be substantial.

By contrast, the structure of the AMA programs has distributed the credit risk of approximately $235 billion of mortgages among thousands of smaller, well-regulated community lenders, thereby reducing the risks to American taxpayers. Given the low level of losses, we believe this is a much sounder approach.

C. <u>The Five Percent Risk Retention Requirement May Be Too Simplistic.</u>

Rather than using a flat 5% risk retention requirement for all mortgages, as provided for in the Proposed Rule, the AMA Programs use a more sophisticated and nuanced approach. The credit characteristics of each borrower and each loan is evaluated individually on a loan-by-loan basis, then appropriate pool level adjustments are made, to determine the amount of credit enhancement, or risk retention, the Member must provide to equal the loss absorption level of an investment grade mortgage-backed security. For most loans originated by community lenders, a 5% risk retention requirement will either be more or less than is needed to ensure loan performance. If the requirement is too high, the interest rate on the mortgage may be unnecessarily high. If it is too little, taxpayers could again be exposed.

The amount of credit enhancement required for AMA Program loans has varied greatly depending on the underlying credit characteristics of each borrower and loan. Because specific loan-level data is available for each AMA Program loan, uncertainties about the risk of that loan are reduced and the amount of credit enhancement can be determined with greater assurance. For example, loans historically have averaged approximately 2% to 3% risk retention by Members (credit enhancement) for MPP pools and MPF loans, provided however, that in some instances for individual MPF loans, credit enhancement amounts have exceeded 5%. Changes in housing market conditions are also considered in establishing credit enhancement levels because the model used to establish credit enhancement levels is periodically updated to reflect changing housing market conditions. Consequently, as housing market conditions have become more stressed in recent years, the amounts of AMA Program credit enhancement have increased.

D. Accounting Rules Should Be Considered.

Some accounting issues could arise from the requirement that securitization sponsors must retain 5% risk in the underlying asset pool. First, Generally Accepted Accounting Principles ("GAAP") typically require a true sale at law opinion when a mortgage loan is sold and the seller retains a portion of the risk. This can be prohibitively expensive, particularly for smaller financial institutions. It may be beneficial to have guidance from the Financial Accounting Standards Board ("FASB") clarifying that the true sale test is deemed to be satisfied if the credit enhancements, in the form of retained risk, are considered remote or insignificant.

Additionally, if a financial institution is required to retain a participating interest (in this case, the 5% risk retention) when transferring mortgage loans, then the retained participating interest must meet the definition of a "participating interest" under GAAP to be eligible for sales accounting treatment. In particular, the participating interest must share losses on a pro-rata basis as well as meet certain other conditions. If the transferor has a participating interest in which it retains a first loss position, then the transfer will be recorded as a secured borrowing. The Proposed Rule specifies several options for the form in which a securitization sponsor may retain the required credit risk in the underlying asset pool, including a 5% "vertical slice" of each tranche of the securities, a 5% "horizontal" first-loss position, an "L-shaped interest," a "seller's interest" and a representative sample. Thought should be given to the different accounting treatment for each of these options.

Another accounting issue involves the conditions under which credit enhancements from a mortgage seller could be viewed as credit derivatives. Many mortgage lenders are prohibited from creating credit derivatives. Under GAAP, a credit enhancement is exempt from derivative accounting rules if it meets the conditions of a financial guarantee or if the credit enhancement is provided in the form of subordination, such as the subordination of one beneficial interest to another tranche of a securitization (thereby redistributing credit risk). However, certain transaction structures are not exempted from derivatives accounting treatment – for example, a case in which the transferor/holder owns an interest in a single-tranche securitization vehicle; therefore, the subordination of one tranche to another is not relevant. The key condition is that the mortgage lender continues to be exposed to the credit risk of non-payment on the mortgage loan beginning at inception of the financial guarantee contract and throughout its term. Again, it would be helpful to have FASB guidance addressing this situation and clearly stating that a financial guarantee rather than a credit derivative exists for this transaction structure.

## IV. Concerns Regarding Potential Effects of the Proposed Rule.

A. The QRM Definition Is Likely to Create Unnecessary Costs for Creditworthy Borrowers.

We share the concerns expressed by a growing number of U.S. Senators and Congressmen, as well as a diverse group of financial, real estate and consumer organizations, that the Proposed Rule's Qualified Residential Mortgage ("QRM") exception, requiring a minimum 20% down payment or equity, could significantly harm the ability of creditworthy borrowers to obtain mortgage financing while also impeding the fragile recovery in the housing and housing finance industries. The proposed QRM requirements include, among other things, a high minimum down payment and a narrow debt to income ratio. These strict criteria appear likely to disqualify all but the most affluent borrowers. Thus, the cost of credit for creditworthy low and middle-income borrowers, whose loans do not meet the QRM standards, would likely increase substantially without necessarily improving loan performance. The historical performance of MPF loans, which have used broader underwriting criteria, demonstrates that loan originators that carefully assess the individual creditworthiness of each borrower do not need to use the strict, one-size-fits-all approach of the Proposed Rule's QRM definition.

Well underwritten loans, regardless of down payment, were not the cause of the mortgage crisis. During consideration of the Dodd-Frank legislation, Congress considered and rejected a down payment requirement because it determined that the cost of excluding responsible middle-class families would exceed the modest improvement in default rates. An expanded QRM definition could counteract the above effects, and allow middle and lower income consumers continued access to homeownership, consistent with prudent loan origination practices. We therefore urge the Agencies to consider lower down payment loans that have mortgage insurance as qualifying for the QRM exception.

B. A Narrow QRM Definition Could Harm U.S. Housing Finance.

We are also concerned that a narrow QRM definition, with high down payment requirements and strict debt-to-income ratios, could significantly reduce the overall amount of financing available to creditworthy borrowers and the resultant negative impact on an already fragile housing market. A contraction in mortgage lending could reduce the need for advances from FHLBank Members, decrease the amount of collateral available to secure such advances and result in lower values for available collateral. This could mean that FHLBank Members will constrict the number of loans provided to creditworthy borrowers, particularly impacting borrowers with middle to lower incomes.

## V. The FHLBanks' AMA Programs Should Be Exempted from the Proposed Rule.

As discussed in detail above, the AMA Programs have successfully furthered the mission of the FHLBanks to promote home ownership in a responsible manner. They were established pursuant to regulations issued by the FHFA, which closely supervises and regulates the activities of the AMA Programs. AMA Program loan underwriting guidelines are strict. Each AMA Program loan is originated by a Member and, in most cases serviced by a Member, with incentives to keep loan quality high and to maintain long term positive relationships with their customers. Members participating in the AMA Programs are required to retain a portion of the credit risk of each loan they originate, with the amount of risk retention determined on a loan-by-loan basis based on an objective, third-party assessment of the underwriting risk presented by that loan. The credit performance of loans originated under this risk-sharing structure has demonstrated a consistent superiority over loans sold into the traditional secondary mortgage market.

In administering the AMA Programs, the participating FHLBanks regularly transfer participations in AMA Program loan pools to other participating FHLBanks, primarily to better manage the available capital capacity for such assets among and between FHLBanks. This frees up additional loan capacity, enabling more AMA Program loans to be purchased or funded. We are concerned that the Proposed Rule's definition of an asset-backed security could be interpreted to include such participations and transactions. If so, the AMA Programs could be significantly harmed. Moreover, there is no need to make such transactions subject to the Final Rule because the policy rationale underlying the Proposed Rule, risk retention, is already an integral part of the AMA Programs.

Given the AMA Programs' successful operation for more than a decade and through the current economic and housing crisis, the strict regulatory oversight by the FHFA, and the historically superior credit performance of the AMA Program loans, it would be both unnecessary and detrimental to subject the AMA Programs to the more rigid requirements of the Proposed Rule which, unlike the AMA Programs, provides for the same risk retention amount for all loans, regardless of their individual risk characteristics. Subjecting the AMA Programs to the Proposed Rules would significantly reduce the flexibility of these programs and their ability to customize the fit between the credit risk of each loan and the credit enhancements required of the loan's originator. As a result, many creditworthy borrowers would be unable to obtain loans or would pay too much for loans while other, less creditworthy loans would lack adequate credit enhancement. Therefore, we believe the AMA Programs deserve to be allowed to continue providing their benefits to our Members unaffected by the Proposed Rule and respectfully request that the Agencies create an exemption for them or otherwise clarify that such programs operated by the FHLBanks and closely regulated by the FHFA are not subject to the restrictions of the Proposed Rule.

A. Qualified Homebuyers Would Be Harmed if the AMA Programs are Subject to the Proposed Rule.

The AMA Programs promote the mission of the FHLBanks to enhance the ability of their Members to offer housing finance to consumers at all income levels by structuring credit enhancements that are tailored to the actual risk associated with each individual loan as well as loan pools. The AMA Programs determine individual credit enhancement amounts by use of a sophisticated and nuanced process that calculates both individual loan enhancement and pool level credit enhancements, utilizing a methodology and models that meet FHFA regulatory requirements. This approach provides the flexibility Members need to offer their customers loans at the most competitive rates. Moreover, the historical credit performance of AMA Program loans has convincingly demonstrated that the credit enhancement requirements have been appropriate.

If AMA Programs were subjected to the Proposed Rule's across-the-board 5% risk retention requirement, one of the most attractive features of the AMA Programs would be lost, i.e., the ability to fine tune the risk retention that each Member must hold. Loss of this ability would significantly interfere with the AMA Programs' purpose of making it possible for Members to make loans to a wider range of creditworthy consumers at competitive but fair rates.

B. The Proposed Rule Is Likely to Negatively Affect AMA Program Participation by Member Institutions.

If AMA Programs were subject to the Proposed Rule's requirements, it is likely that fewer Members would use the AMA Programs for two reasons. First, Members would experience less demand for non-QRM loans because many borrowers will be unable to afford the increased costs associated with such loans, so Members would likely originate fewer mortgage loans. Also, Members would likely originate or sell fewer non-QRM loans into AMA Programs because the prices available from large aggregators may be higher than Members could obtain under AMA Programs. AMA Program pricing is not significantly affected by loan quality; rather, loan quality is a factor that reduces the risk retention requirement for AMA Program loans.

C. The Proposed Rule May Limit the Ability of FHLBanks to Offer Participations in AMA Program Loans to Other FHLBanks.

As mentioned above, participating FHLBanks regularly offer participations in AMA Program loan pools to other participating FHLBanks. Subjecting the AMA Programs to the Proposed Rule likely would severely curtail or eliminate this practice due to: (1) the inability to share the opportunity to invest in AMA assets across FHLBank districts; (2) the inability of FHLBanks with an interest in obtaining additional AMA assets to balance capital availability with FHLBanks that have reached their AMA capital capacity; and (3) a reduction in available lending by our Members. Given that risk retention is a central feature of the AMA Programs, we see no benefit to subjecting the programs to the Proposed Rule's risk retention requirements.

D. Application of the Risk Retention Rule to Securitization of AMA Assets Would Limit the Ability of the FHLBanks to Create Future Programs Affording Members Better Access to the Secondary Market.

If government channels are not available for placing loans in the secondary market, as with the MPF Xtra Program, the FHLBanks may want to channel AMA Program loans to the private market to enable Members to have secondary market access for their originations, including loans that have a low default risk but are not QRMs under the Proposed Rule. If the 5% credit risk retention requirement is applied to FHLBank securitizations, it will substantially increase the costs both to the FHLBanks and to their Members and would not be necessary to fulfill Congress' goal of ensuring that loan quality for asset-backed securities is improved and defaults minimized. FHLBank mortgage loans that could be sold into the private market are of two potential types:

1. Loans that include a risk retention requirement for both the originator and the FHLBanks of which the originator is a Member via a first loss account for which the FHLBanks are responsible and a credit enhancement obligation of the originator of the loan, and in some cases additional enhancement in the form of loan level mortgage insurance (Type 1 Loans);

2. Loans that are originated by FHLBank Members and underwritten and originated using the underwriting guidelines developed by the MPF or MPP providers. Such loans are currently sold to Fannie Mae under the MPF Xtra product. (Type 2 Loans).

Both Type 1 and Type 2 Loans have default rates that are well below the national averages, thus demonstrating that AMA Program underwriting criteria are sufficiently stringent. An additional 5% risk retention requirement for Type 1 Loans or a flat 5% risk retention requirement for all Type 1 Loans that are securitized would constitute an unnecessary, and potentially duplicative cost since such loans already require the originator and the securitizers to have appropriate "skin in the game" and are underwritten under strict AMA Program underwriting guidelines.

Securitizations of Type 2 Loans should also be exempt from the 5% risk retention requirement because such loans are underwritten according to strict guidelines and originated and serviced by Members with strong incentives to make only high quality mortgage loans. As a result, Type 2 Loans have historical default rates that are substantially below national averages.

## VI. Conclusion.

For more than a decade, the FHLBanks have used risk retention as a central component of their AMA Programs enabling their Members to provide safe, traditional mortgage loans, with reasonable terms, to one and a half million creditworthy consumers. The credit quality of these loans far exceeds the national average, proving that risk retention can work if properly structured. Consequently we recommend that the Agencies consider adding into the Proposed Rule a risk retention option that, like the AMA Programs, allows for the determination of the risk needed on a loan-by-loan basis reflecting the credit characteristics of each loan. Doing so will better ensure that loan pricing is based on the quality of the mortgages provided by a lender, rather than on the volume of loans delivered. We also recommend that the QRM definition be expanded so that a wider range of creditworthy borrowers will be able to access mortgage credit upon reasonable terms. Finally, we consider it important that the Proposed Rule does not impair the ability of the FHLBanks to continue their mortgage programs and request either clarification on this point or an exemption so that the AMA Programs can continue serving FHLBank Members and their home buying customers.

We appreciate your consideration of these comments.

Sincerely,

FEDERAL HOME LOAN BANK OF ATLANTA

W. McMullan

W. Wesley McMullan
President and Chief Executive Officer

FEDERAL HOME LOAN BANK OF BOSTON

W. Wesley McMullan
President and Chief Executive Officer

Edward A. Hjerpe III
President and Chief Executive Officer

FEDERAL HOME LOAN BANK OF
CHICAGO

Matthew R. Feldman
President and Chief Executive Officer

FEDERAL HOME LOAN BANK OF
DALLAS

Terry Smith
President and Chief Executive Officer

FEDERAL HOME LOAN BANK OF
INDIANAPOLIS

Milton J. Miller II
President and Chief Executive Officer

FEDERAL HOME LOAN BANK OF
PITTSBURGH

Winthrop Watson
President and Chief Executive Officer

FEDERAL HOME LOAN BANK OF
CINCINNATI

David H. Hehman
President and Chief Executive Officer

FEDERAL HOME LOAN BANK OF
DES MOINES

Richard S. Swanson
President and Chief Executive Officer

FEDERAL HOME LOAN BANK OF
NEW YORK

Alfred A. DelliBovi
President and Chief Executive Officer

FEDERAL HOME LOAN BANK OF
TOPEKA

Andrew J. Jetter
President and Chief Executive Officer