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Submitted via E-Mail

November 26, 2008

Ms. Jennifer J. Johnson
Secretary
Board of Governors of the
Federal Reserve System
20th Street & Constitution Ave., NW
Washington, DC 20551

Office of the Comptroller of the Currency
250 E Street, SW
Mail Stop 1-5
Washington, DC 20219

Mr. Robert E. Feldman
Executive Secretary
Attention: Comments/Legal ESS
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429

Regulation Comments
Chief Counsel's Office
Office of Thrift Supervision
1700 G Street, NW
Washington, DC 20552
Attention: OTS-2008-0014

Re: Minimum Capital Ratios: Capital Adequacy Guidelines; Capital Maintenance; Capital: Treatment of Certain Claims on, or Guaranteed by, the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac); 73 Federal Register 63656; October 27, 2008; **OCC:** Docket ID: OCC-2008-0016, RIN 1557-AD18; **FRB:** Docket No. R-1335; **FDIC:** RIN 3064-AD34; **OTS:** Docket No. 2008-0014, RIN 1550-AC24

Ladies and Gentlemen:

The American Bankers Association (ABA)[1] appreciates the opportunity to comment on the Joint Notice of Proposed Rulemaking (NPR) on Minimum Capital Ratios; Capital Adequacy Guidelines; Capital Maintenance; Capital: Treatment of Certain Claims on, or Guaranteed by, the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac),[2] as issued by the Office of the Comptroller of the Currency (OCC), Board of Governors of the Federal Reserve System (Board), Federal Deposit Insurance Corporation (FDIC), and Office of Thrift Supervision (OTS) (collectively, the "Agencies").

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[1] *The American Bankers Association brings together banks of all sizes and charters into one association. ABA works to enhance the competitiveness of the nation's banking industry and strengthen America's economy and communities. Its members – the majority of which are banks with less than $125 million in assets – represent over 95 percent of the industry's $13.6 trillion in assets and employ over two million men and women.*

[2] 73 *Fed. Reg*. 63656 (October 27, 2008).

On September 6, 2008, the Federal Housing Finance Agency placed Fannie Mae and Freddie Mac into conservatorship. The next day, the U.S. Department of Treasury (Treasury) announced the establishment of the Government-Sponsored Enterprise (GSE) Credit Facility to ensure credit availability to Fannie Mae and Freddie Mac and entered into senior preferred stock purchase agreements (the Agreement or Agreements) with both Fannie Mae and Freddie Mac. These steps provide protection to the holders of senior debt, subordinated debt, and mortgage-backed securities (MBS) issued or guaranteed by these two entities. The Agreements enhance market stability by providing additional security to debt holders and improve mortgage affordability by providing additional confidence to investors in MBS guaranteed by Fannie Mae and Freddie Mac. The Agencies note that Treasury, in taking these actions, stated that they were necessary to address ambiguities created by the U.S. Government in the Congressional charters of Fannie Mae and Freddie Mac that created a market perception of government backing.

Current general risk-based capital rules for each of the Agencies provide that claims on, and the portion of claims guaranteed by, U.S. government-sponsored agencies receive a 20 percent risk weight. In light of the financial support provided under the Agreements, the Agencies believe a reduced 10 percent risk weight is appropriate for such claims to reflect their reduced credit risk under the Agreements. Thus, the Agencies propose to amend their general risk-based capital rules to permit banks, bank holding companies, and savings associations the option of assigning a 10 percent risk weight to claims on, or guaranteed by, Fannie Mae or Freddie Mac. The 10 percent risk weight option would apply so long as an Agreement remains in effect with the respective entity.

The Agencies also specifically request comment on the potential effects of this proposal on other banking organization claims on GSEs, such as Federal Home Loan Bank debt.

The Agencies note that the proposed rule would be elective.

The ABA's views on the proposal may be summarized as follows:

- We support reducing the risk weights for Fannie Mae and Freddie Mac debt and guaranteed mortgage backed securities. A lower risk weight is appropriate in light of the support provided by the U.S. Government for the debt of these GSEs.

- The ABA strongly recommends that the Agencies apply a comparable risk weight to Federal Home Loan Bank (FHLB) debt and guarantees. This would provide parity of treatment and avoid unintended consequences for the Home Loan Banks and their members.

- The ABA recommends that the Farm Credit System <u>not be included</u> in the proposal to assign a 10 percent risk weight on Farm Credit System bonds.

Discussion

Reduced Risk Weight to 10 Percent for Claims on, and guaranteed by, Fannie Mae or Freddie Mac

The actions taken in connection with the conservatorships of Fannie Mae and Freddie Mac underscore the extent to which the U.S. Government supports the two companies' debt. A brief review of some of the statements made by the Secretary of the Treasury and other senior government officials illustrate this point.

> [W]e expect that these four steps [*i.e.*, an initial increase in the GSEs' MBS portfolio followed by a gradual reduction to reduce systemic risk; the Preferred Stock Purchase Agreements; a new secured lending credit facility for Fannie Mae, Freddie Mac, and the FHLBanks; and a temporary program to purchase GSE MBS] to provide greater stability and certainty to market participants and to provide long-term clarity to investors in GSE debt and MBS securities….[3]
>
> It is important to remember that as part of the Treasury's actions regarding Fannie Mae and Freddie Mac and in consultation with FHFA, the GSEs entered into a Preferred Stock Purchase Agreement with Treasury that effectively guarantees all debt issued by the GSEs, both existing and to be issued. The U.S. Government stands behind these enterprises, their debt and the mortgage backed securities they guarantee. Their mission is critical to the housing markets in the United States and no one will deny the importance of these institutions in assisting our housing markets in this downturn.[4]
>
> The most important facilities [created to address problems at Fannie Mae and Freddie Mac] are the $100 billion each Senior Preferred Agreements, which ensure that the Enterprises have a positive net worth. This facility is well over three times the statutory minimum capital requirements and lasts until all liabilities are repaid or it is exhausted. Effectively, it is a government guarantee of their debt and MBS. Under this facility, they can grow their portfolios by about $100 billion each, which will further support the market.[5]

These statements indicate a level of support by the U.S. Government that justifies a lower risk weighting for Fannie Mae and Freddie Mac stock. Accordingly, we support a reduction from the current 20 percent risk weight assigned to Fannie Mae and Freddie Mac debt under the Agencies' current rules.

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[3] Statement by Secretary Henry M. Paulson, Jr. on Treasury and Federal Housing Finance Agency Action to Protect Financial Markets and Taxpayers, September 7, 2008 (available at http://www.treas.gov/press/releases/hp1129.htm).

[4] Remarks of Anthony Ryan, Acting Under Secretary for Domestic Finance, to the SIFMA Annual Meeting, October 28, 2008.

[5] Statement of James B. Lockhart, III, Director, Federal Housing Finance Agency Before the Senate Committee on Banking, Housing, and Urban Affairs On "Turmoil in the U.S. Credit Markets: Examining Recent Regulatory Responses," October 23, 2008.

Additionally, we support the Agencies' optional provision of maintaining the status quo, which would be helpful to those individual institutions that determine that the benefit of the reduced risk weighting would be offset by the increased costs of making software changes for the lower risk weight.

Parity for FHLBank obligations

The Agencies should apply a comparable risk weight to the debt of Fannie Mae, Freddie Mac, and the FHLBanks. These GSEs engage in related housing finance missions, and the U.S. Government has supported all three with comparable safety nets. To treat them in a dissimilar fashion ignores these fundamental similarities and will lead to the presumably unintended consequence of creating a perception that there is a greater degree of risk inherent in FHLBank debt.

The Federal Government has similar authorities for Fannie Mae, Freddie Mac, and the FHLBanks. The fact that the FHLBanks have not needed the Federal assistance that was provided to both Fannie Mae and Freddie Mac when they were placed into conservatorship should not obscure this point.

The authority derives from Public Law 110-289, the Housing and Economic Recovery Act of 2008 (HERA), which became law on July 30, 2008. The following overview of the relevant provisions of HERA illustrates the extent to which Fannie Mae, Freddie Mac, and the FHLBanks are subject to comparable supervision:

- Section 1101 established the Federal Housing Finance Agency (FHFA) with express authority over Fannie Mae, Freddie Mac, the Federal Home Loan Banks, and the Office of Finance.

- Section 1102 provides the Director of FHFA with authority over each of these regulated entities to ensure (a) that each operates in a safe and sound manner, including maintenance of adequate capital and internal controls, and (b) that the operations and activities of each fosters liquid, efficient, competitive, and resilient national housing finance markets.

- Section 1110 provides authority for the Director to establish similar risk-based capital requirements and standards for the regulated entities.

- Section 1117 provides similar temporary authority of Treasury to purchase obligations and other securities issued by regulated entities, which expressly include Fannie Mae, Freddie Mac, and FHLBank obligations.

- Section 1201 provides that prior to promulgating regulations or taking agency action, the Director shall consider the differences between the FHLBanks on the one hand and Fannie Mae and Freddie Mac on the other with respect to several specific criteria, including the mission of providing liquidity to members and capital structure.

The provisions outlined above show that there is clear authority for Treasury and the FHFA to treat Fannie Mae, Freddie Mac, and the FHLBanks in a comparable manner. If the FHLBanks had been experiencing significant problems at the time Fannie Mae and Freddie Mac were placed into conservatorship, it is reasonable that Treasury would have taken similar action for the FHLBanks.

There is a strong need in the current economic climate to treat Fannie Mae, Freddie Mac, and the FHLBanks comparably, including by assigning consistent risk weights for the debt issued by each. Parity of treatment is essential to avoid unintended consequences of a market perception of different treatment for FHLBanks.

The FHLBanks' bond spreads recently have widened relative to the debt issued by Fannie Mae and Freddie Mac, and access to the term debt market has become expensive and severely constrained. According to the latest information available from the Federal Home Loan Bank Office of Finance (the debt issuing office for all twelve Federal Home Loan Banks), one measure of the differential is the spread between FHLB Global issues[6] and comparable Fannie Mae and Freddie Mac issues. In the roughly two months since Fannie Mae and Freddie Mac were placed into conservatorship, these spreads have widened by as much as 30 basis points – creating a significant funding differential between Fannie Mae and Freddie Mac relative to the Federal Home Loan Banks. Adopting comparable risk weights for claims on, or guaranteed by, the FHLBanks, Fannie Mae, and Freddie Mac would be a positive signal of parity by the Government to the markets and would help address this disparity in pricing. It would also allow continued community bank access to liquidity from the FHLBanks at competitive rates, thereby enabling these banks to meet the home ownership needs of their communities.

<u>Exclusion of the Farm Credit System from the proposal to assign a 10 percent risk weight</u>

The Farm Credit System (FCS) <u>should not be included</u> in the proposal to reduce the risk rating on Farm Credit System bonds held by FDIC insured institutions. That system is <u>not</u> under the regulatory jurisdiction of the FHFA or the safety net provided under HERA. Rather, the FCS is regulated by the Farm Credit Administration, which is an independent regulator and which has long resisted being part of any comprehensive GSE regulatory regime. As a result, the risk to FDIC insured institutions that hold Farm Credit System bonds <u>*may be different*</u> than the risk associated with Federal Home Loan Bank bonds.

Since the Federal Home Loan Bank System, along with Fannie Mae and Freddie Mac, is now regulated by the FHFA and subject to the same safety net provisions, there is comparability in how risk is assessed and supervised. As long as the FCS maintains its status as a separate and independent regulator, the FDIC will have a more difficult time assessing the risk that FCS debt may pose to FDIC-insured institutions that hold their bonds.

When the FHFA placed Fannie and Freddie in conservatorship, the Secretary of the Treasury and the Director of the FHFA made it clear that the government would stand behind those GSEs' debt. At the same time, they also indicated that while such action was not currently

[6] FHLB Global issues are the most easily compared issuances.

necessary or expected with regard to the FHLBanks, such support of the secured liquidity facility would be extended to them as well if necessary. None of the authority mentioned above with respect to the Government-Sponsored Enterprise Credit Facility extends to the FCS. Since the FCS is not regulated by the FHFA and was not included in the authorities extended to the FHFA by HERA, no similar support for the FCS can be inferred or claimed. Thus, we urge the Agencies to not extend the proposed adoption of a 10 percent risk weight to the Farm Credit System.

Conclusion

The ABA appreciates the opportunity to comment on this proposal to decrease the risk weight to 10 percent for claims on, or the portion of the claims guaranteed by, Fannie Mae or Freddie Mac. We also request the Agencies to apply a comparable reduction to the risk weight of FHLBank debt and guarantees. We oppose any such risk weight reduction for Farm Credit System bonds.

Thank you for considering our comments. Should you have any questions, please contact Kathleen P. McTighe at (202) 663-5331 or kmctighe@aba.com.

Sincerely,

K. P. McTighe

Kathleen P. McTighe