Housing Finance & Regulatory Affairs
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Sandra Thompson
Director
Federal Housing Finance Agency
Office of the Director
400 7th Street, S.W.
10th Floor
Washington, D.C. 20219

Re: FHLBank System at 100: Focusing on the Future

Submitted via email to: https://www.fhfa.gov/AboutUs/Contact/Pages/Request-for-Information-Form.aspx

Dear Director Thompson:

On behalf of the National Association of Home Builders of the United States (NAHB), I welcome the opportunity to submit comments to the Federal Housing Finance Agency (FHFA) regarding the request for feedback on how to ensure the Federal Home Loan Banks "remain positioned to meet the needs of today and tomorrow." The Federal Home Loan Banks (FHLBanks) have been key components of the housing finance system since the FHLBank System was chartered as a government-sponsored enterprise (GSE) by Congress in 1932. Both the housing finance system and the banking system have evolved significantly over the last 90 years. As the FHLBanks approach their centennial, it is an opportune time for stakeholders to reflect on the role or potential role of the FHLBanks and consider whether their purpose, structure and activities should be revised.

NAHB is a Washington, D.C.-based trade association representing more than 140,000 members involved in the development and construction of for-sale single-family homes, including homes for first-time and low- and moderate-income homebuyers, as well as the construction, ownership and management of multifamily rental housing, including affordable rental housing. The ability of the home building industry to meet the demand for housing, including addressing affordable housing needs, and significantly contribute to the nation's economic growth is dependent on an efficiently operating housing finance system. The nation's housing finance system must offer home buyers in all geographic areas access to affordable mortgage financing at reasonable interest rates through all economic conditions and provide financing for multifamily housing development to support affordable rental opportunities.

Background

The FHLBanks are a critical and reliable component of the housing finance system. In their unique role they provide many resources to their member banks that allow them to support homeownership, rental opportunities, and economic development in their communities. Foremost, the FHLBanks are a source of liquidity to their member banks through "advances," low-cost loans that finance housing and community development activities. Advances to member banks, collateralized predominantly by home mortgage loans, are a primary member service as well as a key contributor to the profits of each FHLBank. Importantly, the FHLBanks provide a secondary market outlet for mortgage loans originated by their members to mitigate interest rate and prepayment risk. Further, each FHLBank is required to set aside a portion of its profits to reinvest in families and communities in its region through grants and below market rate loans.

NAHB always has been a reliable supporter of the FHLBanks and their specific GSE mission to provide liquidity to the housing finance industry for mortgages and community development. We believe the FHLBanks are particularly important to the success of smaller, community banks, offering access to products and services that often are not available to them from other sources that prefer to serve large financial institutions and thereby allowing smaller banks to compete with large ones. A significant portion of NAHB's single-family home builders and multifamily developers rely on their community banks for financial services, including acquisition, development and construction (AD&C) financing.

NAHB welcomes this comprehensive review. We believe it is an opportunity to affirm the relevance of the FHLBanks and their mission while allowing stakeholders to identify areas for reconsideration that may enhance and strengthen the FHLBanks' role in an evolving housing market.

Benefits of the FHLBanks

Collateralized Advances

Any revisions to the FHLBank System should not disrupt the primary benefit to FHLBank members of collateralized advances to support funding of mortgage loans and housing- and community-related development. The level of advances by the FHLBanks appropriately ebbs and flows demonstrating the value of advances to provide a countercyclical balance to liquidity requirements in the mortgage market. Advances by FHLBanks are available to member banks when other sources are not willing or able to provide the level of funding required by the market. The FHLBanks have demonstrated they are a stabilizing force during times of market distress, due in large part to their advances.

Advances also are a key source of income to the FHLBanks. Interest paid on advances fund the FHLBanks' activities and is a determining factor of the FHLBanks' annual profits and subsequent contributions to the Affordable Housing Program (AHP).

We urge FHFA not to undertake any changes that will diminish the favorable cost of funds for the FHLBanks that allows them to provide low-cost financing to their member banks for their housing activities or impair their role in providing liquidity to construction and mortgage lending. NAHB also urges FHFA not to limit the size or type of member institution that has access to advances.

Eligible Collateral

Residential mortgage loans are the principal form of collateral pledged for advances. Other eligible collateral includes securities backed by residential loans, certain U.S. government and government agency securities, cash, deposits in the FHLBanks, and other real estate related collateral (ORERC) such as commercial real estate loans. Community Financial Institutions are allowed additional forms of eligible collateral including small business and small farm loans. The amount advanced on the pledged collateral is discounted based on the perceived risk of the collateral. The more liquid and the more easily valued the collateral, the smaller the "haircut."

Though AD&C loans are eligible collateral for advances, they are considered "risky" and generally not used by member banks as collateral for advances because the haircut imposed by the FHLBanks is prohibitive. As each

FHLBank serves different types of members, has its own risk tolerance, and measures risk using its own methods, each FHLBank determines its own policies regarding collateral types it will accept and the haircut imposed on different collateral types.

NAHB Recommendation

NAHB believes the FHLBanks could do more to support AD&C financing. A smaller haircut on AD&C collateral pledged for advances might encourage more community banks to originate AD&C loans and potentially increase the availability and affordability of these loans to home builders and developers, thereby increasing the availability and affordability of new homes.

We propose FHFA do a study of the risk posed by AD&C loans to determine whether the weighted average effective haircut on AD&C loans reflects the risk presumed by the FHLBanks. Examining actual losses incurred at member banks on AD&C loans, as well as reviewing the true risk of the other factors that are considered when determining the haircut on AD&C loans, would be a worthwhile exercise and might reveal these loans to be less risky to banks than current haircuts warrant.

Additionally, we propose FHFA encourage the development of a pilot program promoting construction of single-family and multifamily housing affordable to low- and moderate-income families. For example, perhaps the FHLBanks could be permitted to use their retained earnings to reduce or eliminate the required capital for advances collateralized by AD&C loans. Making it easier to utilize AD&C loans as collateral for advances, and encouraging community banks to consider this option, could stimulate AD&C lending for affordable housing development and would be particularly valuable during times of tight credit.

Affordable Housing Program

The AHP of the FHLBanks is an extremely important component of the FHLBank System and is widely acknowledged to play a significant and valuable role in supporting affordable housing nationwide. The FHLBanks contribute 10 percent of their annual profits to the AHP program. The funds may be used by member institutions working with community organizations and housing developers to create rental or homeownership opportunities for lower-income households or grants to help home buyers and homeowners fund down payments, closing costs, counseling, or rehabilitation costs in connection with the purchase or rehabilitation of an owner-occupied home.

Much like the Low-Income Housing Tax Credit, the AHP can be utilized in financing the construction and rehabilitation of affordable rental housing. Its ability to be combined with other federal funding makes it useful to fill funding gaps in capital required for the development of affordable rental housing in high-cost and difficult to develop areas.

NAHB's multifamily developers familiar with the AHP have suggested changes that NAHB believes could improve the program. We hear from NAHB members that when the FHLB System introduced the AHP, the funding was flexible enough that developers could leverage AHP to help attract additional funding sources to their affordable housing developments, especially those in overlooked communities. Over time, the AHP underwriting and compliance requirements have become unduly complex and have become an obstacle to participation despite AHP often being a small portion of a project's capital stack. Currently, in many projects AHP funding often is the last funding put in place due to the rigorous underwriting and fund draw-down criteria. This complexity has led to increased cost as many sponsors must hire consultants to complete AHP applications and meet monitoring requirements. Other potential sponsors are deterred from the program altogether.

NAHB Recommendation

Decreasing the underwriting burden of AHP while aligning compliance with other funding sources will increase efficiency, make AHP less costly to use and expand participation.

We also would like the FHLBanks to create a debt program in their community lending platform that would finance debt at below-market rates. This would allow the loan amounts on each affordable project to increase, thereby making the funding gap smaller between funding sources so AHP funds required to fund the gap would decrease. This would allow the FHLBanks to spread their AHP funds further to support more AHP projects.

Regional and Cooperative Structure of the FHLBank System

NAHB would oppose proposals by FHFA to eliminate the regional structure of the FHLBank System, which we believe is key to the success of the AHP. Having 11 FHLBanks around the country allows each to better tailor products and services to the state, local and community needs within its region. NAHB believes the distribution and utilization of AHP funds would be much less effective if the program was administered from one location.

We also believe the cooperative nature of the FHLBank System has been successful and should remain intact. Although each FHLBank is a separate corporate entity with its own management and board of directors, the cooperative structure that makes the FHLBanks jointly and severally liable for all FHLBank System consolidated debt creates a check and balance system to incent the FHLBanks to operate in a safe and sound manner.

Membership

Over the years, there have been proposals and requests to expand membership eligibility in the FHLBank System. There is understandable debate about whether independent mortgage banks, Real Estate Investment Trusts, and reinsurance companies should be allowed to join and have access to the low-cost funds and other benefits of FHLBank membership. Though membership eligibility is statutory, NAHB believes this review period is an opportunity for FHFA to consider whether the broad housing industry would benefit if additional categories of institutions that meet membership eligibility provisions with regard to mortgage assets and mortgage finance participation should be allowed to join the FHLBank System. Membership eligibility should always be based on whether FHFA and the FHLBanks can appropriately gauge and monitor the safety and soundness of institutions being considered for membership. As banks are originating fewer mortgages and other industry participants are originating the bulk of mortgage loans, broader access to the FHLBanks and their advances would support both the FHLBanks and the mortgage industry.

Mortgage Purchase Program (MPP) and Mortgage Partnership Finance (MPF) Program

Since 1997, when the FHLBank of Chicago began the MPF as a pilot, the FHLBanks have provided member banks with a secondary market outlet for their conventional and government 1-4 family mortgage loan originations. Nine of the FHLBanks participate in the MPF and two participate in the MPP started a few years later. The programs have slight variations, but are very similar. When selling loans to its FHLBank through the MPP or MPF, the participating FHLBank takes on the interest rate, prepayment and liquidity risk of the mortgage loans. The member bank retains credit risk, although both programs allow the member bank to share the credit risk with the FHLBank and over time receive a monetary benefit based on the credit performance of the loans.

The MPF has many product options that allow members to sell their loans to other investors without a risk sharing structure. For example, the MPF Xtra® product allows member banks to sell loans through the MPF program to the FHLBank of Chicago, which in turn sells the loans to Fannie Mae in a back-to-back transaction. Aggregating larger volumes of loans from across the FHLBanks affords the opportunity for better loan execution. Similar options apply to nonconforming jumbo mortgage loans and government-insured and government-guaranteed mortgage loans. The products are designed to give member banks more alternatives for selling their loans in the secondary market and thereby ensuring funds for additional financing for mortgage loans to home buyers and homeowners.

NAHB Recommendation

NAHB recommends that FHFA encourage the FHLBanks to develop similar secondary market options for multifamily mortgage loans and AD&C loans. Though Fannie Mae and Freddie Mac offer an outlet for multifamily loans, an MPF- or MPP-like program might offer a better execution for sellers, particularly for smaller, community banks. Currently, there is no efficient secondary market for AD&C loans, making this a key opportunity for FHLBanks.

Board Members

Each of the FHLBanks has a Board of Directors consisting of Member Directors, Independent Directors and Public Interest Directors that oversee the operations of each bank. Over the years, many NAHB members have served as Independent Directors and Public Interest Directors on the boards of directors of several FHLBanks. Our members are proud of this service to the FHLBanks. Our members are staunch advocates for housing and possess a valuable perspective on the overall housing market as well as the distinct needs and economies of the communities in which they develop and build homes. Single-family and multifamily home builders and developers work extensively with stakeholders, financial institutions and state and local governments in their communities to assess market needs, understand and follow local regulations, gauge affordability constraints of homebuyers and renters, assess community demographics, and create financing options, in order to understand and respond appropriately to community needs.

As members of FHLBank boards, home builders and developers bring a perspective on housing needs within a FHLBank's district that is beneficial and unmatched.

Recently, FHFA has urged the FHLBanks to create boards of directors that reflect diversity. NAHB applauds FHFA's efforts to focus on improving diversity, equity and inclusion (DEI) within the housing finance ecosystem. NAHB, too, is looking for ways to increase diversity within the home building industry, including creating a DEI Task Force and promoting the building trades to women and minorities.

However, NAHB members who have applied recently to serve on FHLBank boards have expressed concerns that they are not considered acceptable candidates due to the focus on DEI. In many instances, this leaves a FHLBank's board of directors without a director that has private-sector home building experience.

NAHB Recommendation

NAHB recommends FHFA also should prioritize private-sector housing market experience as a qualification for FHLBank board membership. As described above, single-family and multifamily home builders and developers are well-suited to help a FHLBank achieve its mission of providing reliable liquidity to its member institutions where they can best support housing and community investment in their respective communities. As private businesses, they are able to identify and respond quickly to changing market conditions and consumer preferences. NAHB believes this unique insight into regional housing markets can add significant value to any FHLBank's board of directors.

Conclusion

The regulation of the mission and safety and soundness of the FHLBanks should continue to reflect the uniqueness of their statutory mission and their regional and cooperative operating structure. NAHB urges FHFA not to undertake any changes to the FHLBanks that will impair their role in providing liquidity and other products and services to financial institutions in support of affordable development and housing construction to home builders and developers, mortgage financing to home buyers and homeowners and funding options for community and economic development.

Major changes should not be undertaken quickly. The potential for unintended consequences is increased if proposed changes are not fully developed and vetted by stakeholders.

NAHB would like to participate in one or more of the upcoming regional roundtable discussions and we hope there will be a chance to respond to any final recommendations FHFA might propose for the FHLBank System prior to implementation of any changes.

Please contact Rebecca Froass at rfroass@nahb.org for additional information or to answer any questions you may have regarding these comments.

Sincerely,

Jessica R Lynch

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