FHLB CINCINNATI

FHLBI FEDERAL HOME LOAN BANK OF INDIANAPOLIS

October 13, 2016

Federal Housing Finance Agency
Office of Financial Analysis and Modeling
400 Seventh Street SW
Ninth Floor
Washington, D.C. 20219

Re: Single Family Credit Risk Transfer Request for Input
Submitted via Email

To Whom It May Concern:

The Federal Housing Finance Agency (FHFA) has requested feedback on its *Single Family Credit Risk Transfer Request for Input* published on June 29, 2016 (the RFI). The Federal Home Loan Banks of Cincinnati and the Federal Home Loan Bank of Indianapolis ("the FHLBs") support a front-end credit risk transfer (FECRT) program for its participating member institutions and appreciate the opportunity to provide the following views for your consideration.

The FHLBs have been successfully operating a lender risk sharing program, the Lender Risk Account (LRA), in partnership with our member financial institutions for more than 15 years through our Mortgage Purchase Programs (MPP) as authorized under the Acquired Member Asset (AMA) regulation[1] (AMA Programs). The MPP includes a FECRT feature that transfers credit risk to the private sector through the use of originator-provided credit enhancements and, at times, mortgage insurance. The unique risk sharing structure of the MPP, and similar AMA Programs at other FHLBanks, has provided tremendous benefits for our members through competitive upfront pricing and future fee income based on the performance of the loans with over 340 community lenders across the district originating and funding more than 385,000 mortgage loans worth approximately $61 billion. As of June 30, 2016, members participating in the MPP collectively have been paid $56 million of fees from the FHLBs to manage the credit risks of their loans (in lieu of paying guarantee fees to another entity). The current second quarter 2016 balance of our participating financial institutions' LRA is $275 million, available for future performance based incentives.

As the FHFA considers ways to improve FECRT programs of Fannie Mae and Freddie Mac (the Enterprises), we urge the FHFA to consider similar improvements to the FHLBanks' AMA programs, including the MPP. First, the FHLBs should be afforded similar authority as the Enterprises to develop new FECRT programs to mitigate exposure to credit risk in ways that are consistent with the FHFA's credit risk transfer principles[2] described in the RFI. For example, if greater use of credit insurance products, including supplemental mortgage insurance, becomes part of an Enterprise FECRT program, the FHLBs would like the option to use similar structures. The same policy reasons supporting the FHFA's pursuit of increased FECRT programs for the Enterprises apply to our FHLBs. Greater use of such programs by the Enterprises will result in transfer of more mortgage credit risk to the private sector.

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[1] 12 C.F.R. § 955

[2] *See* Credit Risk Transfer Principles starting on page 3 of the RFI (reduce taxpayer risk, economically sensible, continuity of core business, repeatable, scalable, counterparty strength, broad investor base, stability through economic and housing cycles, transparency and level playing field).

Moreover, insurance is an accepted form of credit enhancement in the mortgage market, both at the borrower level, as primary mortgage insurance, and at the investor level, as SMI or pool insurance. Both SMI and pool insurance allow a member and the FHLBs to offset a portion of their risk, reducing the member's required risk-based capital, and thereby providing additional loan capacity. Members are incentivized to underwrite high quality loans since insurance premiums increase as the quality of the loan decreases, thereby diminishing the member's ability to offset its credit risk. The FHFA has recognized that credit risk transfer is an acceptable method of risk management. As part of the FHFA's goals for the Enterprises, the FHFA has significantly increased the targeted amount for credit risk transfers that the Enterprises must complete annually. The Enterprises have used various types of credit insurance, including mortgage insurance, to transfer credit risk to the capital markets. The FHLBs believe that extending this flexibility to the FHLBs would allow them the ability to similarly mitigate risks, and also achieve their regulatory mission goals, and serve members and their communities.

While the operations of the Enterprises and the FHLBs vary in important ways, we each need to ensure that credit risk is managed in a safe and sound manner. All housing GSEs need the ability to manage credit risk with innovation, creativity and flexibility. In today's competitive secondary mortgage market, the GSEs should be on equal footing regarding FECRT programs. An originator's decision to sell to one GSE over another should not be based on the limitation of authority relative to FECRT programs, but rather on universal factors such as loan products, service and pricing. A level GSE playing field with regard to FECRT programs also benefits consumers by creating an environment where originators have access to similar products and multiple loan executions, helping to ensure the lowest possible rate for a mortgage loan. An uneven playing field could also negatively impact the FHLBs' Core Mission Assets[3] and our ability to fulfill our mission.

The foregoing comments are aimed at securing the necessary flexibility so the FHLBs may continue providing mortgage liquidity to our members in support of our housing finance mission and responding to changes in the secondary mortgage market with appropriate product innovation. We appreciate the FHFA's consideration of these views.

Sincerely,

R. Kyle Lawler
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FHLB Indianapolis

[3] 12 CFR § 1265.2