



July 6, 2010

VIA FEDERAL EXPRESS AND EMAIL (RegComments@FHFA.gov)

Alfred M. Pollard, General Counsel
Attention: Comments/RIN 2590-AA32
Federal Housing Finance Agency
Fourth Floor
1700 G Street, N.W.
Washington DC 20552

Re: Federal Home Loan Bank Investments

Dear Mr. Pollard:

The following represent the views of the Board of Directors of the Federal Home Loan Bank of New York ("FHLBNY") regarding the Federal Housing Finance Agency's ("FHFA") notice of proposed rulemaking and request for comment relating to Federal Home Loan Bank ("FHLBank") investments published in the Federal Register on May 4, 2010.

The FHFA has indicated that it is proposing to reorganize and re-adopt existing investment regulations that apply to the FHLBanks. The FHFA is also proposing to include in the investment regulations limits on the FHLBanks' investment in mortgage-backed securities ("MBS") and certain asset backed securities ("ABS") that are currently set forth in the Financial Management Policy ("FMP"). If the proposed rule is adopted in its current form, the FHFA has said it expects to terminate the FMP as of the effective date of the new rule. In general, the FHLBNY believes that the proposed Rule as published is an appropriate proposal to promote safety and soundness.

We note that the FHFA has acknowledged that some of the FHLBanks' investments in private-label MBS ("PLMBS") have resulted in accounting charges for other-than-temporary-impairment ("OTTI"). As such, the FHFA has specifically requested comments on whether more restrictive limits or other modifications to the MBS investment requirements are needed. We agree with the FHFA's comment that the FHLBanks' OTTI charges are problematic. The FHLBNY shares the same concern expressed by the FHFA regarding the financial condition of some FHLBanks and the negative performance of their PLMBS.

We believe that, because of statutorily required joint and several liability, the MBS investment portfolio at one FHLBank can potentially become a problem for the other FHLBanks. To lessen the risk of adverse consequences to some FHLBanks, we are of the opinion that it is necessary to limit the size of a FHLBank's MBS portfolio and require adequate retained earnings in order to help cushion potential losses.

The FHFA posed a number of specific questions in its May 4, 2010 notice, and our responses to these questions are set forth below.

1. *“Although the proposed rule would retain the FMP provision limiting MBS holdings to 300 percent of a Bank’s capital, FHFA also requests comment on what other measures might offer a prudent limit on MBS holdings that also would mitigate potential future losses from the Banks’ MBS portfolios. Comments on this issue may address both the magnitude of the limit (i.e., 300 percent of capital) and its basis (i.e., capital). For example, because retained earnings can absorb losses without compromising the par value of Bank capital stock, a limit based on a Bank’s retained earnings may offer a more prudent basis for limiting private-label MBS investments.”*

Response: The FHLBNY believes that an overall limit of 3 times capital is still appropriate. However, we also believe that MBS investments should be supported by an adequate level of retained earnings. We share the same opinion as the FHFA that losses from investments should be absorbed by retained earnings to help protect the par value of the FHLBank capital stock investment of members.

To associate retained earnings with investment authority can provide FHLBanks with an incentive to manage risks inherent with MBS securities. It can help reinforce prudent risk taking measures and bolster the need to raise retained earnings to help ensure that each FHLBank's member capital is protected from risk events. We recommend that the level of retained earnings be established at 4% for agency MBS. We relied on the FHFA's minimum capital to assets ratio of 4% to devise the maximum permissible multiple for Agency MBS.

However, the level of retained earnings for PLMBS is more difficult to determine. Therefore, we recommend that the FHFA commence a study to determine the appropriate level of retained earnings necessary to support PLMBS investments.

If the FHFA adopts the final investment regulation containing provisions limiting MBS to some multiple of or relationship to retained earnings, the FHFA should consider a transition period due to the varying levels of retained earnings at individual FHLBanks.

2. *“In addition to the overall limit on MBS investments, FHFA requests comments on whether there should be a separate limit or additional restrictions on the purchase of PLMBS (e.g., a limit of one or two times capital, or a separate limit linked to retained earnings or some other basis). If such provisions are appropriate, FHFA seeks comments on the appropriate magnitude of the limit and its basis, as well as whether the rule should prohibit the purchase of PLMBS.”*

Response: With an overall limit of 3 times capital and appropriate levels of retained earnings assigned to PLMBS and agency MBS, we do not see a need for a separate limit on PLMBS.

3. "In addition to the types of limits contemplated by the questions immediately above, FHFA seeks comments on whether it should restrict purchases of private-label MBS based on collateral characteristics (e.g., restrictions based on whether the underlying mortgages are commercial or residential real estate loans, adjustable-rate loans, interest-only loans, or credit scores below certain levels). If such limits are appropriate, FHFA also would request comments on the types of characteristics and restrictions that should be implemented. For example, FHFA has considered proposing a limit on a Bank's PLMBS purchases that decreases as the amount of relatively risky collateral in the Bank's mortgage pools and portfolio increases. Such restrictions could serve to limit the Bank's exposure to credit losses by reducing purchases of PLMBS with relatively risky collateral."

Response: We believe that the purchase of PLMBS should be limited to that supported by collateral with the highest underwriting standard and external rating, which is prime and "AAA" rated, respectively. The purchase of PLMBS should be further restricted to securities in which the underlying mortgage loans comply with all aspects of the federal banking agencies' *Interagency Guidance on Nontraditional Mortgage Product Risks*, issued on October 4, 2006 (71 FR 58609), and *Statement on Subprime Mortgage Lending*, issued on July 10, 2007 (72 FR 37569).

We do not believe that AMA (MPF/MPP) assets should be part of the investment limit due to the fact that they are governed by separate regulation, and that these assets have performed exceptionally well during the housing crisis.

4. "At one time, the FMP limited the purchase of PLMBS to only those instruments rated in the highest investment grade category. FHFA requests comments on whether it should re-introduce that type of limit as a means to limit the potential risks to the Banks from their MBS portfolios, and whether it would suffice to adopt a ratings requirement only for PLMBS backed by certain types of collateral (e.g., subprime or Alt-A loans)."

Response: Please see our response to Question 3 above.

Thank you for the opportunity to comment. Please do not hesitate to contact me if you have any questions.

Very truly yours,



Michael M. Horn
Chair
Board of Directors of the Federal Home Loan Bank of New York