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Capital for Communities –
Opportunities for People℠

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Alfred M. Pollard
General Counsel
Federal Housing Finance Agency, Fourth Floor
1700 G Street, NW.
Washington, DC 20552

E-mail: RegComments@fhfa.gov

ATTN: Comments/RIN 2590-AA39

Dear Mr. Pollard:

On behalf of Community Reinvestment Fund, Inc. ("CRF"), I appreciate this opportunity to share our views on the Federal Housing Finance Agency's ("FHFA" or "the Agency") Advanced Notice of Proposed Rulemaking ("ANPR") regarding Federal Home Loan Bank Membership published in the *Federal Register* on December 27, 2010.

BACKGROUND

CRF is the nation's leader in accessing the capital markets to support community development financing activities. As a national CDFI, we access capital from private markets for local community development lenders by operating a secondary market for their loans amd by accessing New Markets Tax Credit investors. Since its inception, CRF and its affiliates have delivered in excess of $1.2 billion in loan capital to more than 700 communities across the country. This lending has, in turn, leveraged an additional $1.2 billion in additional funds. Working with 157 local lending partners, we have funded a total of 2,297 loans in 46 states and the District of Columbia. Working through our local lending partners, CRF has directly assisted more than 389,000 people, including funding 17,427 homes, financing 1,300 small businesses, creating or retaining 44,000 jobs, and funding community facilities that serve 308,000 people.

CRF also played an instrumental role in designing the New Market Tax Credit (NMTC) legislation and we have developed our own NMTC program that delivers the benefits of the tax credit to small operating businesses. To date, CRF has funded 366 NMTC loans deployng a total of $630 million in 187 cities in 34 states. Our strong track record of originating and managing NMTC investments is evidenced by the number of NMTC investments in our portfolio. According to the CDFI Fund's report entitled, "NMTC Program: Activities Financed Through 2007", CRF's portfolio of 186 QALICBs was more than 15 times larger than the average CDE portfolio of 12 QALICBs. The CDE with the second largest portfolio included 71 QALICBs or only 38% the size of our portfolio. As of December 31, 2010, CRF's portfolio had grown to 330 QALICBs.

Our wholly-owned affiliate, National New Markets Tax Credit Fund, Inc., is one of the country's largest allocatees and has received NMTC allocations totaling $674.5 million and is currently developing the pipeline for our I$77 million allocation just received. In addition, two major banks suballocated $73.2 million of their NMTC allocations to CRF asking us to deploy the funds to small business borrowers

With these allocations CRF has delivered hundreds of NMTC loans with flexible terms to support business lending and community facilities. The businesses financed through CRF's NMTC business lending activities are highly diverse and distributed across more than 120 Standard Industry Classification Codes. Many are owned by minority or women entrepreneurs who have built security for their families and their employees because they had access to favorable NMTC loan terms. Others are nonprofit businesses operating charter schools, child care centers and health care facilities serving the needs of low-income people and residents of low-income communities.

COMMENTS ON MEMBERSHIP REGULATIONS

We commend the Federal Housing Finance Agency's efforts to ensure consistency between current regulatory standards and the FHLB System's housing and community development mission. However, we believe it is important to reiterate our comments expressed in an earlier comment letter regarding Federal Home Loan Bank Membership criteria for Community Development Financial Insitutions ("CDFIs").[1] In that letter, we explained that CDFIs encompass a wide range of organizations that are diverse in both their structures and activities. Membership rules for CDFIs must balance the need for a sound regulatory structure with the diverse nature of this industry. In addition, CDFIs are unique from other types of institutions eligible for membership in the FHLB System in that they must have a *primary mission* of community development. Thus, by virtue of their mission, they are engaged in financing activities that further the goals of the FHLB System.

Changes to existing regulations *must* facilitate membership of CDFIs in the FHLB System and their ability to use the resources of the Banks to carry out their community development mission. We are particularly concerned that this regulatory review not increase the difficulty of CDFIs seeking to become members of the FHLB System. We ask FHFA to remain vigilant for any unintended consequences that any changes in rules may have on the ability of CDFIs to gain entry and to participate in the System. CDFIs have only been eligible to become Home Loan Bank members since 2008 and a very small number have been admitted to date. Below, we offer our responses to select questions related to the three general membership requirements as well as several related provisions or issues.

[1] See CRF's Letter to Alfred M. Pollard, General Counsel, Federal Housing Finance Agency, on Federal Home Loan Bank Membership for Community Development Financial Institutions, July 14, 2009.

TEN PERCENT REQUIREMENT

This rule requires new members to have at least 10% of their total assets in "residential mortgage loans"[2] based on their most recent financial report at the time they apply for membership. To eliminate the possibility of members reducing their holdings of residential mortgage assets after joining the System, FHFA is considering amending the regulations to make compliance with this rule an ongoing requirement. Any such change in the regulations would require the Agency to determine how the Banks should measure ongoing compliance. The Agency is also considering whether it would be appropriate to extend this requirement to other types of applicants, specifically to insurance companies and CDFIs. Currently, all insured non-depository institutions (insurance companies and CDFIs) are required to have mortgage related assets that reflect a commitment to housing finance.

Question Two: Should FHFA amend §§ 1263.6(b) and 1263.10 of its regulations to subject insurance company and CDFI applicants to the 10 percent residential mortgage loans requirement?

In my opinion, the 10 percent rule should ***not*** be applied to CDFIs. First, CDFIs are mission driven organizations established to respond to the credit needs of borrowers in low- and moderate-income communities they serve. To address these needs, CDFIs provide a range of credit products, including but not limited to, residential mortgage loans. CDFIs typically provide "gap" financing – or the types of credit and investment products that are not otherwise available in underserved communities. Whether a CDFI holds a certain percentage of of its assets in residential mortgage loans depends on the type of financing products needed in a community. Competition from other CDFIs or other credit providers (such as predatory lenders) may cause the volume and dollar value of a CDFI's residential mortgage assets to fluctuate. We believe this fluctuation is a healthy phenomena and that the FHLB System's mission is broad enough to encompass and support the CDFI business model – one that focuses on customizing and delivering financial products to fill gaps left by conventional financial institutions. Regulations governing membership should preserve that flexibility for CDFIs to develop and deliver financing products that are appropriate for borrowers in the particular low- and moderate-income communities they serve.

Secondly, as a national CDFI, CRF plays a special role in providing liquidity to our lending partners who source the affordable housing and community development loans we make in underserved communities. Our business model requires us to expand and contract our balance sheet as we channel private capital to support housing and community development activities. In any given year, CRF's holdings of affordable housing loans may vary based on local demand and general market conditions. If FHFA requires CDFIs to hold a specific percentage of their assets in

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[2] 1263.10. The term "residential mortgage loans" includes: (1) Home mortgage loans; (2) funded residential construction loans; (3) loans secured by manufactured housing; (4) loans secured by junior liens on one-to-four family property or multifamily property; (5) certain mortgage pass-through securities; (6) certain mortgage debt securities; (7) home mortgage loans secured by a leasehold interest; and (8) loans that finance properties or activities that would satisfy the requirements for the Community Investment Program or a community investment cash advance program. 12 CFR 1263.1.

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residential mortgage loans we might meet the standard one year but not the next. Moreover, imposing a strict 10 percent rule on CDFIs, like CRF, would undermine the very purpose for which CDFIs were established as well as their ability to carry out the mission of the FHLB Banks. We respectfully urge the FHFA to adopt a more flexible to the ten percent requirement based on an assessment of a CDFI's commitment to housing finance that takes into account a number of factors – such as the nature of its financing activities and any benefits such activities provide to the housing finance market. Furthermore, this assessment should be based on a long-term analysis over at least three years rather than an annual compliance period.

Question Three: If FHFA does not subject insurance company and CDFI applicants to the 10 percent requirement, should FHFA amend § 1263.6(c) of its regulations, which currently requires all such applicants to have mortgage related assets that reflect a commitment to housing finance, to establish levels of mortgage-related assets that may be deemed to constitute a sufficient commitment to housing finance.

For the reasons cited in Question #2, we *oppose* requiring CDFIs to hold specific levels of mortgage-related assets in order to demonstrate a sufficient commitment to housing finance. CDFIs differ in terms of size and types of financial products that they offer; imposing a "one-size" fits all requirement reduces their ability to develop the types of innovative credit products most urgently needed in their Target Market communities. CDFIs have a primary mission of community development and as such this mission informs both the purpose and the nature of their activities. This mission focus ensures that CDFIs directly support and further the housing finance and community development mission of the FHLB System. We recommend FHFA maintain the current, more flexible approach to the ten percent requirement for CDFIs as it better reflects the diversity of these institutions and the range of affordable housing and community development activities they finance in low- and moderate-income communities.

"MAKES LONG-TERM HOME MORTGAGE LOANS" REQUIREMENT

An institution seeking to join a Bank is required to "demonstrate that it originates or purchases long-term home mortgage loans" based on its most recent financial report at the time of application. FHFA is considering making this rule an ongoing requirement so that members do not reduce or cease to make long-term mortgage loans. To implement fully such a requirement, FHFA would have to develop a benchmark for measuring compliance, such as specifying that a certain percentage of an institution's assets or a minimum dollar volume of its loans consist of long-term home mortgage loans. Neither the statute nor the regulations provide a quantifiable benchmark for this requirement. Any benchmark based on a percentage of an institution's assets would have to be smaller than the 10 % rule discussed above because of the differing definitions of "residential mortgage loans" and "long-term home loans."[3]

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[3] 12 U.S.C. 1422(4), (5); 12 CFR 1263.1. The term 'home mortgage loan" includes primarily the following: (1) First mortgage loans secured by one to- four family property, multifamily property, or combination business or farm property where at least 50 percent of the total appraised value is attributable to the residential portion of the property; and (2) mortgage pass-through securities that represent an undivided ownership interest in the above types of loans or

Long-term mortgage loans are more narrowly defined to mean a loan (or an interest in a loan) that is secured by a first-lien on one-to-four family or multifamily property. FHFA is also weighing whether to develop separate standards for different classes of eligible institutions based on their respective business models and varying levels of engagement in residential mortgage finance. A similar argument could be made for establishing separate standards for different types of institutions within a class of eligible institutions.

Question Four: Should FHFA revise § 1263.9 of its regulations to require that an institution that is admitted to membership must comply with the "makes long-term home mortgage loans" requirement both at the time that it is admitted for membership and for the duration of the time that it remains a member?

CRF supports the principle that members of the FHLB System should be required to meet the "makes long-term home mortgage loans" requirement on a ongoing basis with the following caveat: standards for this requirement should be developed for each class of eligible institutions and, where appropriate, for different types of institutions within a given class so as to take into account the nature of an institution's or a class of institutions' business model and respective activities.

Question Five: Should FHFA replace the existing standard, which requires only that an institution demonstrate that it originates or purchases home mortgage loans, with one or more quantifiable standards, such as by requiring applicants and members to have a specified portion of their assets invested in long-term home mortgage loans or by meeting a minimum dollar volume of originations and purchases of such loans?

We strongly favor maintaing the existing standard for CDFIs whereby an institution demonstrates only that it orginates or purchases home mortgage loans. Establishing quantifiable standards for meeting this requirement would severely limit the ability of CDFIs to join or maintain membership in a Bank. As we stated above, CDFIs have a primary mission of housing finance and community development and therefore their activities are dedicated to and aligned with the fundamental mission of the System. The value CDFIs bring is the ability to "fill the credit or investment gaps" in their Target Markets. As the financing needs of borrowers in their communities evolve, CDFIs respond by offering new credit product tailored to those needs. Requiring CDFIs to hold a specific portion of their assets in long-term home mortgages or to originate or purchase a minimum dollar volume of such loans, reduces their ability to fill these financing gaps in their communities. The CDFI business model requires a high degree of flexibility that runs counter to a quantitative benchmark approach. Furthermore, the highly customized nature of CDFI financing activities has intentionally created an industry so diverse it would be extremely difficult to set a single standard that would be appropriate for all CDFIs.

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in securities that represent an undivided ownership interest in such loans. The regulations also define "long-term" to mean term to maturity of five years or greater.

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Question Six: If FHFA were to adopt a standard based on a minimum percentage of long-term home mortgage loans, what would be an appropriate level of long-term home mortgage loans or mortgage-backed securities to be held by depository institutions, insurance companies, or CDFIs, respectively?

CRF opposes the adoption of a standard that would require CDFIs to hold a minimum percentage of long-term home mortgage loans. Instead, we favor retaining the current standard whereby a CDFI need only demonstrate that it orginates or purchases home mortgage loans. This preserves flexibility for CDFIs to respond to the dynamic credit needs of borrowers in their communities.

Question Seven: If FHFA were to replace the existing regulatory requirement with a quantifiable standard, should FHFA apply one standard to all eligible institutions and members, or separate standards for the three distinct categories of institutions that are eligible for membership?

We reiterate our opposition to quantifiable standard for CDFIs to meet the "makes long-term home mortgage loans" requirement. However, if FHFA choses to adopt such a standard, it should only be applied to depository institutions and insurance firms and not to CDFIs for the reasons cited above. CDFIs are distinct from the other classes of eligible institutions in that they have a primary mission of community development and their business model are designed to support the same housing finance and community development mission of the FHLB System. Hence, they should not be held to standards developed for institutions with different missions and whose business models are not designed to further housing and community development activities.

Question Eight: If FHFA were to establish separate quantifiable standards for the separate categories of eligible institutions, should it also establish separate sub-categories for different types of institutions within each category, such as for life insurance companies and property and casualty insurance companies?

CRF does not believe that a quantifiable standard should be applied to CDFIs as we explained in Questions *6 & 7*. If FHFA choses to adopt such standards for depository institutions and/or insuarance companies – it may be appropriate to establish separate standards for sub-categories of organizations within these two classes of eligible institutions.

THE HOME FINANCING POLICY REQUIREMENT

Current regulations require a depository institution seeking to become a member of a Bank to demonstrate that the character of its management and its home financing policy are consistent with sound and economical home financing. Neither the statute nor the regulations define the term "home financing policy" or requires that such policy be articulated in a written document. Under existing regulations, an applicant that is subject to the Community Reinvestment Act ("CRA") is deemed to be in compliance if it has received a CRA rating of "Satisfactory" or better on its most recent CRA performance evaluation. An applicant not subject to CRA must file a written justification with its application explaining why its home financing policy is consistent with the Bank System's housing finance mission. Compliance is assessed only at the time of application for membership.

At present no procedures exist to measure ongoing compliance with this requirement nor are there any qualitative standards to define an acceptable home financing policy. The Agency is weighing whether it should establish more specific standards and make compliance an ongoing requirement for all members. This approach would require FHFA to develop new tests through which Banks could assess their members' ongoing compliance with this rule. In addition, FHFA is weighing whether this policy should take the form of a written document or if members should be allowed to demonstrate compliance through other means. If a written policy is required, the Agency would also need to establish some minimum benchmarks to ensure the provision is applied uniformly throughout the System.

In additon to the form of a new home financing policy standard, FHFA would need to develop the content of such a standard. In lieu of or in addition to the CRA rating, an applicant or member could be required to maintain a specific level of mortgage related assets or mortgage loan originations in order to be deemed in compliance. If FHFA adopts this approach, it would have to be consistent with the 10 percent and the "makes long-term mortgage loans" requirements. Theoretically, an applicant could meet the home financing policy rule if it were in compliance with ongoing quantifiable standards established for the other two requirements. Finally, if the FHFA establishes quantifiable standards for the home financing policy requirement it might need to consider whether those standards should vary by the type of institution reflecting different levels of mortgage lending activity.

<u>Question Nine</u>: Should FHFA revise § 1263.13 of its regulations to require that an institution that is admitted to membership must comply with the "home financing policy" requirement both at the time that it is admitted for membership and for the duration of the time that it remains a member?

Yes. We support mandating ongoing compliance with the Home Financing Policy Requirement for members of the FHLB System so long as the requirement is properly designed for each class of eligible institutions and takes into account the nature of an institution's business model and respective activities. We recommend against quantifiable standards or benchmarks imposed on CDFIs for the reasons we have articulated above. Instead, we support a flexible approach to this requirement that would allow a CDFI to meet this rule either through a written policy or other means that demonstrates that their home financing policy is consistent with sound and economical home financing. The absence of any specific definition of "home financing policy" in both the statute and the regulations provide FHFA with ample latitude offer flexibility to eligible institutions, such as CDFIs, whose mission focuses on meeting the financing needs of borrowers in underserved communities with responsible and appropriate financial products and services.

<u>Question Ten</u>: Should FHFA define the term "home financing policy" and, if so, how should that term be defined? Should it be defined to include only a written policy that describes in narrative fashion the manner and extent to which an applicant's past and current activities and investments support home financing, or should it also be defined to

include certain business practices, such as having specified levels of mortgage related assets above which an acceptable housing finance policy could be presumed?

Given the diverse nature of eligible institutions, we recommend FHFA provide flexibility in defining "home financing policy" so that an applicant or member may meet this test either through a written policy or through business practices, such as having specified levels of mortgage related assets, depending on the nature of it its business activities. This approach is particularly appropriate for CDFIs, who by definiton develop and deliver financial products based on the needs of borrowers in the low-income communities they serve. For some CDFIs a written narrative may be the best way to articulate how their policy is consistent with sound and economical home financing practices in a low-income environment. While other CDFIs may demonstrate the appropriateness of their policy through their business practices and activities as reflected in their financial statements.

Question Eleven: Should the regulations allow the specifics of a home financing policy to vary based on the type of institution? Should FHFA recognize that originating mortgage loans and investing in mortgage loans and mortgage related securities may constitute the core business of certain types of eligible institutions, such as thrift institutions, while those same activities may constitute only an incidental portion of the business of other eligible institutions, such as insurance companies?

Yes, this is precisely the approach we advocate because it recognizes the diversity of the activities conducted by different types of eligible institutions each with their own core business activities.

Question Twelve: Should FHFA continue to use an institution's CRA rating as a proxy for compliance with the home financing policy requirement or should FHFA develop an alternative approach to assessing compliance with this requirement? One such alternative could be to develop a quantifiable standard, such as one based on a minimum level of housing related assets, which could be used either alone or in conjunction with the CRA rating, for determining whether an institution has an acceptable home financing policy.

This question pertains to depository institutions and therefore would not directly affect CRF and other CDFIs.

SANCTIONS FOR NONCOMPLIANCE

Question Fourteen: Should FHFA amend the membership regulations to address the possibility that a member might not comply with, or might later fall out of compliance with, one or more of the new ongoing membership requirements after a transition period has expired, and if so, should FHFA require the Banks to terminate that institution's membership, either with or without a grace period, or should FHFA consider lesser sanctions, such as prohibiting further access to Bank services during a specified grace period, before requiring the Banks to terminate the membership of the noncompliant members?

We recommend that FHFA require Banks to provide a one year grace period for members that fall out of compliance with membership requirements. We also strongly support the notion of providing a reasonable transition period for members that do not meet the new membership requirements at the time they are implemented

REGULATORY STRUCTURE

Current membership regulations take a "presumptive compliance" approach such that an eligible institution that satisfies the regulatory standard is presumed to comply with the corresponding statutory requirements and an institution that does not may attempt to rebut the presumption of noncompliance by submitting specified additional information. (Note this is particularly important for CDFIs that are not regulated and are not required to file uniform financial statements.) The regulatory standards related to the 10 percent and the "makes long-term home mortgage loans" are not rebuttable; however applicants may rebut the standards related to "home financing policy," "inspection and regulation," "character of management," and "financial condition." FHFA is considering whether to retain its "presumptive compliance" and "rebuttal" approach or adopt more objective and quantifiable regulatory standards that would provide a "bright line" approach for evaluating eligibility for membership.

Question Fifteen: Should FHFA retain the existing structure of its membership regulations, under which the regulations establish certain standards of "presumptive compliance" and allow an opportunity for institutions that do not meet those standards to rebut the presumption of noncompliance, or should FHFA devise an alternative structure, such as one that incorporates "bright line" tests for each of the various eligibility requirements and does not create presumptions that an institution would be permitted to rebut?[4]

We urge FHFA to retain the "presumptive compliance" and "rebuttal" approach rather than devising an alternative structure based on a series of "bright line" tests for each of the eligibility requirements. In our view, the latter approach would make it more difficult for CDFIs to meet the eligibility requirements as the burden of proof would increase under such "bright line" tests. A "bright line" test would be inappropriate for a CDFI industry that encompasses a wide range of organizations that are diverse in both their structure and activities. Moreover, CDFIs present a very different type of eligible institution as compared with the other two classes (depository institutions and insurance companies). Moving away from "presumptive compliance" would only exacerbate barriers to membership and undermine the intent of section 1206 of the Housing and Economic Recovery Act of 2008 that mandated non-federally insured, certified CDFIs be permitted to join this System. We believe the eligibility rules must balance the need for a rigorous regulatory structure that ensures the strength and viability of the FHLB System with the intent of this legislation.

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[4]In January 2010, FHFA revised its membership regulations to implement statutory amendments authorizing CDFIs to become Bank members. As part of those revisions, FHFA allowed CDFI applicants that could not demonstrate compliance with certain of the specific standards relating to financial condition to provide alternative information demonstrating that they are in sound financial condition. By raising the larger issue of the appropriate regulatory structure for the membership regulations FHFA does not intend to change its policy, as evidenced by the recent revisions, that CDFI applicants are to be given latitude in demonstrating the soundness of their financial condition.

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Question Sixteen: Should FHFA play a role in resolving close membership issues, or leave them to the discretion of the Banks?

FHFA may be able to play a constructive role in resolving membership issues particularly as they pertain to CDFIs – a new class of eligible institutions within the FHLB System. To ensure consistency and to provide a system-wide approach (through peer learning and dissemination of best practices), CRF supports the concept of allowing FHFA to intervene in resolving membership issues at individual Banks.

CONCLUSION

In closing, we appreciate this opportunity to share our views and we commend the leadership and the staff of the Federal Housing Finance Agency for undertaking this comprehensive and thoughtful review of membership regulations. CRF is strongly committed to strengthening the links between membership and the Banks's mission. We look forward to continuing to work together to make CDFIs full particpants in the FHLB System. We would be pleased to answer any questions regarding the comments provided in this letter.

Thank you.

Sincerely,

Frank Altman
President and CEO

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