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Attention: Comments/Securitization Study

Dear Sirs:

The Independent Community Bankers of America[1] (ICBA) welcomes the opportunity to provide comments for the study on securitization of home mortgage loans purchased or to be purchased from Federal Home Loan Bank (FHLB) system member institutions under the Acquired Member Assets (AMA) programs. Community banks need viable programs and tools to prudently promote homeownership and affordable housing to enhance the stability and economic well-being of communities across the nation. The FHLB AMA programs have helped a number of community banks in this regard. Whatever form the AMA programs take going forward, they must not jeopardize the

[1] *The Independent Community Bankers of America represents nearly 5,000 community banks of all sizes and charter types throughout the United States and is dedicated exclusively to representing the interests of the community banking industry and the communities and customers we serve. ICBA aggregates the power of its members to provide a voice for community banking interests in Washington, resources to enhance community bank education and marketability, and profitability options to help community banks compete in an ever-changing marketplace.*

With nearly 5,000 members, representing more than 20,000 locations nationwide and employing over 300,000 Americans, ICBA members hold $1 trillion in assets, $800 billion in deposits, and $700 billion in loans to consumers, small businesses and the agricultural community. For more information, visit ICBA's website at www.icba.org.

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strength and stability of the FHLBs or members' ready access to competitively priced advances.

Approximately 80 percent of ICBA members are FHLB members. In a recent survey of ICBA members regarding their use of the secondary market for residential mortgages, less than 20 percent of respondents said that they sell loans through FHLB programs, nearly 50 percent sell to Fannie Mae and/or Freddie Mac and nearly 40 percent sold to investors. Approximately 15 percent of the bankers indicated that they do not sell any mortgages, while approximately 25 percent indicated that they sell over 90 percent of their mortgages.

Importance of Advances

Community banks see that the most important benefit that FHLBs offer them is access to funding; advances are the primary reason community banks are FHLB members. ICBA has long held that while the FHLB secondary market programs offer a competitive alternative to other secondary market programs, the advance business must remain the primary business of the FHLBs and any secondary market programs should not jeopardize it. Community banks have access to a variety of other secondary market options, such as Fannie Mae, Freddie Mac and private investors, and are actively using them. There is no ready replacement for advances. Thus, the FHLBs should remain focused on providing advances and any secondary market programs developed by the FHLBs should in no way impede the ability of members to access to attractively priced advances.

Secondary Market Principles

Community banks do benefit by the FHLB secondary market programs, but the programs have faced challenges in remaining an attractive option over the long term. Recently, ICBA has heard from some of its members that Fannie Mae and Freddie Mac offer better pricing than their FHLB program. The FHLBs and their members need to work together to enhance the programs to ensure that they are available to members of all sizes as a competitive secondary market alternative, complementing advances offerings.

As ICBA considers the future of the secondary market for residential mortgages with the conservatorships of Fannie Mae and Freddie Mac, we see several key principles that must be addressed which are appropriate to a debate on the future of similar FHLB programs:

- Community banks need the continued existence of a strong, impartial secondary market for residential mortgages as provided by Fannie Mae, Freddie Mac and the FHLBs.
- The secondary market must not directly compete with the private sector in mortgage originations.
- All lenders should have equitable access regardless of size or volume.

Recent market events demonstrate the important role Fannie Mae and Freddie Mac, and to a lesser extent the FHLBs, have played in providing liquidity and stability to housing finance markets through their secondary market programs. In that regard the secondary market entities need to have the operational flexibility to hold mortgages when market conditions dictate, along with any securitization authorities. The future secondary market for housing finance should continue to have some type of government ties, demonstrating the importance of homeownership to the American public.

FHLB Securitizations
ICBA recognizes that the inability of the FHLBs to securitize mortgages has limited the size of their AMA programs and at times has exposed the FHLBs to increased risk. Securitization could address these problems and provide liquidity, enabling the FHLBs to purchase more mortgages. However, it is difficult to speculate on the potential new risks that the FHLBs would face as they enter the securitization business, particularly if they begin to guarantee securities. We also have concerns about the increased volatility that marking the securities to market as 'held-for-sale" would impose on the FHLBs' financial statements. The result may be the need for the FHLBs to build higher levels of capital, impacting advance rates, dividends and the affordable housing program contributions.

The FHLBs need to closely control the source of mortgages purchased to ensure the continuation of the nexus requirement that ensures that the assets acquired by the FHLBs have some connection to a system member or housing associate. Members have capital at risk and should not be exposed to mortgage origination activities by parties that have nothing at risk. Also, buying mortgages from highly regulated financial institution members makes it less likely that the FHLBs would unknowingly purchase loans with predatory characteristics. The risk-sharing requirement that was established for the AMA programs has been an important tool in emphasizing the cooperative nature of the system and ensuring that members and housing associates share the credit risk of loans they sell to their FHLB.

While the current AMA programs have been developed by individual FHLBs joining with others, we see merit in exploring the development of a single entity in the system, owned jointly by the FHLBs to pool and securitize residential mortgages. This would enable the FHLBs to concentrate their secondary market expertise, enjoy economies of scale, develop sufficient market presence for their securitizations and provide greater transparency to each FHLB about risk exposure since joint and several liability for consolidated obligations ultimately places each FHLB at risk for the activities of others. If allowed to securitize on a bank-by-bank basis, some may do better than others and enjoy better market reception for their securities and better pricing. This may result in a competitive disadvantage for smaller members that belong to a FHLB that is less successful and who must compete for mortgages against members that have the flexibility to originate mortgages nationally, selling to the FHLB that offers the best pricing. On the other hand, securitizing on a system basis may limit the ability of individual FHLBs to develop products for their particular membership base.

Given the recent challenges that Fannie Mae and Freddie Mac have and are facing and the continued weakness in the housing market, any exploration of securitization and expansion of current AMA programs should be done cautiously and judiciously. The future of Fannie Mae and Freddie Mac is uncertain and their resolution will have a significant impact on the FHLBs, particularly AMA programs. The FHLBs and their regulator must carefully study this evolving environment to see what opportunities and challenges it presents to the FHLBs before significant resources and member capital are committed to expanding AMA programs.

Expertise in Serving Rural Areas

Recently, ICBA has heard a number of complaints from community banks in rural areas about the difficulties they face in selling loans to Fannie Mae and Freddie Mac due to difficulties obtaining suitable comparable properties for appraisals. Often these rural areas have not seen the declining property values as in other parts of the country (nor did they see the steep rapid rises earlier in the cycle). Bankers have complained that appraisals are being rejected due to lack of recent comparable sales, distance between comparables, and/or too many price adjustments. Yet, these are issues that are typical for rural properties: there are fewer properties thus fewer sales, a comparable property may be 20 miles away due to more sparsely populated areas and there are no large developments so there are no blocks of look-alike houses. These are issues that arose in the early 1990s as more community banks started selling loans to the secondary market. ICBA worked closely with Fannie Mae and Freddie Mac then to educate their staff about the characteristics of properties in rural communities and to address them in underwriting standards. Now community banks are again facing these same problems and we are again working with Fannie Mae and Freddie Mac to address them.

The FHLBs that serve a number of members in rural areas quickly adopted the Community Financial Institution authorities regarding collateral acceptance and have gained an understanding about the unique characteristics of rural properties and rural communities. We believe that the FHLBs are in an excellent position to help community banks serving rural areas to gain better secondary market access for their residential mortgages on properties that are not standardized. We urge the FHLBs and the Federal Housing Finance Agency to look at ways to help community banks serving rural areas sell mortgages, both through the existing AMA programs and any new programs.

Summary

The most important product that the FHLBs provide to community banks is advances; the AMA programs are adjunct to advances. FHLB secondary market programs can help community banks make residential mortgages, serving their customers and their communities. Mortgage securitization should be carefully explored as a way of enhancing the FHLBs secondary market programs to ensure their viability and to help in risk management. The FHLBs, through the AMA programs, should look a ways to help community banks in rural areas originate and sell residential mortgages.

We appreciate the opportunity to provide comments for the study. If you have any questions about our views, I may be reached by email at ann.grochala@icba.org or by phone at 202-659-8111.

Sincerely,

/s/

Ann M. Grochala

Vice President, Lending and Accounting Policy