NATIONAL ASSOCIATION OF HOME BUILDERS

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SENIOR VICE PRESIDENT
HOUSING FINANCE AND LAND DEVELOPMENT

August 31, 2009

Federal Housing Finance Agency
1700 G Street, NW
Washington, DC 20552

Attention: Public Comment – RIN 2590-AA17 (Prior Approval for Enterprise Products)

Dear Madam or Sir:

On behalf of more than 200,000 members of the National Association of Home Builders (NAHB), I am pleased to respond to the request for comments by the Federal Housing Finance Agency (FHFA) on the Interim Final Rule (Interim Rule) governing the prior approval process for new product offerings by Fannie Mae and Freddie Mac (Enterprises). The Interim Rule implements the process and standards for prior approval of the Enterprises' products and activities as mandated in Section 1321 of the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (Safety and Soundness Act) as amended by Section 1123 of the Housing and Economic Recovery Act of 2008 (HERA), enacted on July 30, 2008. HERA requires the Enterprises to provide prior written notification to FHFA of a new activity and to obtain prior approval from FHFA for a new product pursuant to specific statutory time periods for review and standards for approval.

Background

HERA requires the Enterprises to submit a written request for prior approval of any new product. As part of the new product approval process, HERA provides for a 30-day public notice and comment period. FHFA must approve or deny a new product no later than 30 days after the close of the comment period. A product may only be approved if it is authorized by the Enterprise's charter, is in the public interest and is consistent with the safety and soundness of the Enterprise or the mortgage finance system. HERA does not define the term product, except by exclusions which include the Enterprises' automated loan underwriting systems; modifications to terms, conditions or underwriting criteria for mortgages purchased or guaranteed by the Enterprises; and, activities that are substantially similar to other activities as determined by FHFA. HERA also requires written notification to FHFA for activities that an

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Enterprise considers is not a new product and provides for an expedited review process whereby FHFA has 15 days to determine if the activity is subject to the new product approval process.

The legislation directs FHFA to develop forms and procedures to establish these processes. Accordingly, the Interim Rule provides a form that the Enterprises are required to complete for submitting information to FHFA to facilitate its consideration of new activities and new products. While the Interim Rule generally is consistent with the prior approval framework specified in the statute, NAHB is concerned that some aspects of the process established by the Rule are overly burdensome which could stifle product innovation and the ability of the Enterprises to promptly respond to changing market conditions.

Interim Rule

The Interim Rule requires the Enterprises to submit a Notice of New Activity (NNA) form to provide information on activities that may be a new activity or new product for FHFA review and approval prior to commencing such activity. New activities include a significant expansion or alteration of an existing activity or product as well as activities that could be determined to be a new product. The rule also requires an NNA submission for activities that are not new products, but merit safety and soundness review. As part of the submission, the Enterprises must provide detailed information on whether the activity is or is not to be considered a new product, including factors that FHFA will consider in determining whether the activity is "substantially similar" to existing activities and products and therefore excluded from the new product approval process. These factors include whether the activity:

1. Is a product;
2. Is authorized under the applicable authorizing statute;
3. Represents an upgrade to the way an approved product is delivered;
4. Poses a significant change in risk to the Enterprise or the mortgage finance system from a previously approved product or activity;
5. Involves a significant change in terms, conditions, or limitations expressly contained in any prior approval granted under this part;
6. Poses a significant change in its effect on the public interest compared to a previously approved product or activity;
7. Poses a significant change from a previously approved product or activity and if so, does a tradeoff exist in the composite of risk, public interest, and safety and soundness elements in the proposed new activity;
8. Is likely to have significantly more enterprise resources dedicated to it;
9. Requires approval by regulators other than FHFA, including Federal, State, or local regulators;
10. Involves new classes or types of borrowers, investors, or counterparties;
11. Involves new classes or types of collateral; or,
12. Such other factor as the FHFA Director determines to be appropriate.

The description must also address the factors that FHFA may consider to determine if the proposed new activity is in the public interest, including:

1. The degree to which the new product might reasonably be expected to advance any of the purposes of the Enterprise's charter;
2. The degree to which the new product serves underserved markets;
3. The degree to which the new product is being supplied or could be supplied by non-government-sponsored enterprise (GSE) firms;
4. Other alternatives for providing the new product;
5. The degree to which the new product promotes competition in the marketplace or, to the contrary, would result in less competition and greater concentration of economic activity or risk;
6. The degree to which Enterprise provision of the new product overcomes natural market barriers or inefficiencies;
7. The degree to which Enterprise provision of the new product might raise or mitigate systemic risks to the mortgage, mortgage finance or other financial markets;
8. The degree to which the new product furthers fair housing; and,
9. Such other factors determined appropriate by the FHFA Director.

The NNA Form also requires the following detailed information about the activity:

- Business rationale and intended market;
- Unusual or unique characteristics;
- Projected size and start date of the new activity;
- Units and personnel with responsibility over the new activity;
- Legal opinion on whether the activity complies with the Enterprise's charter, does or does not constitute a new product and other legal matters;
- Other regulatory applications;
- Relationships with non-secondary market participants;
- Business requirements, including systems for data processing, accounting and performance tracking;
- Acquisition;
- Accounting treatment;
- Tax implications;
- Earnings and capital implications;
- Risk implications;
- Performance reports and risk controls; and,
- Other safety and soundness implications.

A notice will not be considered completed until all of the information required by the NNA form, along with any follow up information requested by FHFA, has been submitted.

FHFA will notify the Enterprise when the NNA form is deemed complete and accepted for review. FHFA will then determine if the new activity is a new product and will then publish the proposal in the Federal Register for a 30 day public notice and comment period. FHFA will make a determination whether to approve or deny the new product within 30 days of the close of the comment period. If the activity is deemed not to be a new product, the Enterprise may not commence the activity until 15 days since notification of the completed NNA Form.

Pursuant to the Interim Rule, all information provided in the NNA form or by commenters will be considered public. However, an Enterprise or commenter to may request confidential treatment by providing a detailed explanation of the request and the information specified in the Rule. The Rule also provides for temporary and conditional approvals as required by HERA. Additionally, the rule provides that if a new product is approved for one of the Enterprises, the other Enterprise may also offer that new product subject to submitting an NNA request and approval.

The Interim Rule also sets forth certification requirements, grounds to nullify an approval and penalties for failure to comply. The NNA must be certified by an executive officer of the Enterprise. If FHFA discovers material misrepresentations or omissions, the approval will be nullified and persons responsible will be subject to enforcement action, civil money and criminal penalties.

NAHB Comments

NAHB supports a product approval process which ensures that the Enterprises are operating within their charters and undertaking activities in a safe and sound manner. The product approval process should also accommodate innovation and prompt responses to market needs. The key challenge in developing a product approval process is to ensure rigorous charter and safety and soundness compliance while facilitating the ability of the Enterprises to continue to engage in product innovations to address market needs in a timely manner.

Congress recognized the need to establish a workable new product approval process for the Enterprises one that would provide notice and review of new product offerings, while permitting the Enterprises to respond in a timely manner to market demands. This intent is clearly stated in the House Financial Services Committee Report on H.R. 1427 (H. Rept. 110-142) which passed the House in May 2007 and was ultimately enacted in HERA. The report states:

> "The Committee believes that the legislation provides the Agency with the flexibility to establish a workable system that will provide predictability as to what offerings or changes to existing offerings rise to the level of a new product that will be subject to notice and approval, addressing both the need to provide notice to market participants of new products and the need for the enterprises to respond in a timely manner to market demands. The Committee intends that the Agency will look to similar processes

> developed by the federal bank regulatory agencies in establishing procedures to minimize unnecessary burden on the enterprises and originating institutions while fulfilling the objectives of the provision."

NAHB believes that the process established by the Interim Rule does not adequately achieve these objectives. The Interim Rule fails to provide predictability on the types of activities that are required to undergo an NNA submission and review; nor does it allow the Enterprises to promptly respond to changing market conditions. We urge further clarification on the activities subject to an NNA submission as well as when the statutory review period can begin. Further, we believe the prior approval process required under the Interim Rule is excessively cumbersome. We are concerned that the sheer volume of information required to be submitted under the Interim Rule will constrain innovation and the ability of the Enterprises to respond to market demands. Finally, NAHB is concerned that the enforcement penalties for non-compliance with the Rule are applicable to some activities that do not merit such censure. Our specific comments and recommendations follow.

Clarification of Activities Subject to Notice of New Activity Submission

Section 1253.2 of the Interim Rule defines a ***new activity*** as "any business line, business practice, or service, including guarantee, financial instrument, consulting or marketing, that is to be undertaken by the Enterprise either on a standalone basis or as an incident to providing one or more Enterprise products to the market and which was: (a) not initially engaged in prior to July 30, 2008; (b) commenced by the Enterprise prior to July 30, 2008, but after which the Enterprise ceased to engage in and presently intends to resume; or, offered or engaged in prior to July 30, 2008, but in a significantly different manner in terms of the activity's effect on the public interest or risk to the Enterprise or the mortgage or financial system." The definition excludes business practices or transactions that are incidental to the administration of internal business affairs, or business practices or services that are *de minimis* in scope, volume, risk or duration. The instructions to the NNA form expand on this definition, stating that "a new activity may include alteration of an existing activity in such a manner as to affect significantly the risk, management, capital effect, operational controls, legal effect, anticipated business impact on the Enterprise (dollar effect), and accounting or taxation for such activity."

NAHB believes this definition is extremely broad. Taken literally any activity undertaken by the Enterprises could meet this definition and therefore would require a NNA submission and review. Clearly this is not what Congress intended when it sought to establish a prior approval process "that will provide predictability as to what offerings or changes to existing offerings rise to the level of a new product that will be subject to notice and approval" as noted in the reference to H. Rept. 110-142 above.

We believe that Congress meant the new product approval process to apply to activities that are clearly beyond the scope of existing activities and products. This is consistent with the activity approval processes for national banks and federal savings associations. In general, these

institutions may engage in activities that are expressly authorized by statute or that are incidental to expressly authorized activities without prior approval of their regulator. We note that the Office of the Comptroller of the Currency (OCC) and the Office of Thrift Supervision (OTS) publish activities that are permissible for the institutions they regulate. However, substantial changes to assets or activities may require prior approval before implementing the change. For example, a national bank must obtain prior approval from the OCC for a change in asset composition (12 CFR 5.53). Further, banks seeking approval of an activity or transaction that is novel, precedential or highly complex must have a pre-filing meeting with appropriate OCC staff prior to submitting the application to review the issues raised and to facilitate preparation of the application and submission of the required information.

NAHB acknowledges that there is no statutory prescription of permissible activities or products for the Enterprises, nor do we believe that such a prescription is appropriate. We reference the procedures of the banking agencies to emphasize that their prior approval processes are conducted on an exceptions basis, not for routine or previously approved activities. We believe that Congress anticipated a similar exceptions-based activity notice submission when it directed FHFA to "look to similar processes developed by the federal bank regulatory agencies in establishing procedures to minimize unnecessary burden on the enterprises and originating institutions while fulfilling the objectives of the provision." (H. Rept. 110-142)

NAHB urges FHFA to use the examination process to identify which activities meet the new activity definition that fall under the NNA submission requirements. We note that the instructions to the NNA form, state that "The Enterprises will work with examiners to assume clarity regarding whether an activity is new and fits within the Notice of New Activity (NNA) submission requirement." This statement is almost an aside in the instructions. NAHB believes that greater emphasis should be put on working with examiners ***before*** an NNA is filed. This process would be similar to the pre-filing meetings under OCC procedures.

New Activity Notice Submission Process

The preamble to the Interim Rule and the instructions for the NNA form state that the same form will be used to determine whether an activity is or is not a new product, an expansion of an existing product or activity, as well as to provide information on activities that are not new products but merit safety and soundness review. In explaining the single form process, FHFA states in the preamble that it "does not believe that it is practical to require an Enterprise to identify a new product – as distinct from a new activity that is not a new product – in advance for purposes of determining which type of submission to make to the agency." Thus, FHFA requires the Enterprise to make a single form submission, the NNA form, and FHFA will determine whether or not the activity is a new product that must be published for public notice and comment. If the new activity is not a new product, the information in the submission will be used by FHFA in safety and soundness reviews as part of the Agency's routine supervisory program.

To meet these multiple purposes, the Rule requires submission of the substantial documentation and information listed under the description of the Interim Rule above. NAHB notes that the information required to be submitted under the Rule is not specified in HERA. We believe that the massive amount of documentation required by the Rule and the process for submission of this information are unnecessarily burdensome and exceed the prior approval process envisioned by Congress.

We interpret the requirements under HERA to call for separate notification for activities that are not new products. We do not believe that Congress intended for the same information to be required for both submissions. For example, HERA mandates an expedited 15-day review process for activities that are not new products. The sheer volume of documentation required by the single form submission process contravenes the intent of the statute as it would be difficult for FHFA to adequately review the documentation within the 15 day period.

Rather than a single form notification process, NAHB believes there should be separate notification processes and documentation requirements for different purposes. For example, there could be a two-stage process whereby an Enterprise could provide a thorough outline of an activity and FHFA could make a preliminary assessment of whether the activity is a new product, and if so, if it meets the statutory charter compliance, safety and soundness and public interest standards. If the activity is deemed not to be a new product, then the additional paperwork for a new product review would not be required. The preliminary determination would assist an Enterprise in determining whether to devote the resources necessary to proceed with the new product and pursue the submission further, or to abandon the effort. FHFA would retain the right to revise its preliminary determination based upon the full application and/or public comment

The appropriate notification process and initial determination could be made through the examination process. This would be akin to the activity application process required for national banks where the procedures differ based on the type of activity. We also note that notice procedures for national banks include an expedited review process with shorter time frames for healthy banks with high supervisory ratings and a longer standard review process for banks not eligible for an expedited review. NAHB encourages FHFA to consider such a tiered review process for the Enterprises.

Further, NAHB does not believe that the NNA submission form should be required for approval of the expansion of existing activities or products. The instructions to the NNA form state that an NNA submission will be required for an expanded existing activity or product, including an expansion in scope, such as increase in size or risk levels; or, movement from a pilot program to a fully deployed activity or product. We note that the instructions permit an Enterprise to seek clarification on whether the expansion requires an NNA submission. NAHB recommends that such a review should be handled though the examination process. We believe it is unnecessarily burdensome to require an NNA submission, and the substantial documentation this requires, for an expansion of an existing product or activity. If through the examination

process, it is determined that the requested expansion is a new product or new activity, then the activity/product should undergo the appropriate review process.

Notification of Completed Submission

Section 1253.3(b) states that FHFA will determine whether the submission is complete and accepted for review. A Notice will not be considered complete and received for processing until all of the information required by the Notice Form, along with additional information requested by FHFA upon review of the initial submission, has been submitted. Once a Notice is deemed complete, FHFA will notify the Enterprise that the submission has been accepted for review. This starts the clock for the statutory time periods, 15 business days for new activities not considered to be new products and up to sixty days for new product review (including the 30 day public comment period).

NAHB is concerned that the Interim Rule could create unnecessary delays in the back-and-forth requests for additional information, prior to the start of the statutory review periods. We believe that examiners should help expedite the determination of a completed application, rather than having this determination rely on a series of written submissions that would undoubtedly create significant time lags. Once an examiner is satisfied that the information is complete, the statutory clock should begin and there should be no further information requests, except for those that might arise as a result of public comments.

Enforcement Penalties

Section 1253.6 requires certification of an NNA submission by an executive officer of the Enterprise. Under Section 1253.6(b) "any person responsible for any material misrepresentation or omission" in connection with submissions under the rule may be subject to various enforcement remedies, including criminal penalties under 18 U.S.C. 1001, the portion of the U.S. statute that governs penalties for fraud and false statements, which includes up to five years in prison.

HERA's product approval provisions do not direct FHFA to establish criminal penalties. NAHB is concerned that the Interim Rule would apply the penalties of Section 1001 to situations that should not be subject to such penalties, in particular material omissions which previously have not been subject to Section 1001. We urge FHFA to remove the word "omissions" from Section 1253.6(b) of the Rule.

I appreciate this opportunity to comment on behalf of NAHB. Please direct questions regarding this matter to Michelle Hamecs, NAHB's Assistant Vice President for Housing Finance, at 202-266-8425, or via e-mail at mhamecs@nahb.com

Sincerely,

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