December 22, 2016

Federal Housing Finance Agency
400 Seventh Street, SW, 8th Floor
Washington, DC 20219

Re: Comments/RIN 2590-AA78

Ladies and Gentlemen:

The National Association of Securities Professionals ("NASP") is the premier organization that assists people of color and women achieve inclusion in the financial services industry. As such, we welcome the proposed Minority and Women Inclusion Amendments (the "Amendments") being proposed by the Federal Housing Finance Agency ("FHFA" or the "Agency"). We are grateful for the opportunity being afforded to us and the public at large to comment on the Amendments. Our organization, and its members (primarily broker-dealers, asset managers, consultants, lawyers, and investment bankers) have a long, if not frustrating history of engaging the regulated entities on the subject of inclusion in their businesses. For some, this engagement even precedes the Financial Institutions Reform, Recovery and Enforcement Act of 1989 ("FIRREA"), which was the first of many legislative Acts of Congress that sought to address diversity and inclusion as they relate to federal agencies doing business with, among other industries, the financial services industry. Through the years, we have also worked closely with various elements of the federal government to keep the government and its instrumentalities informed of the challenges that our members face in trying to shatter the barriers to inclusion. Please note that we do not refer to those barriers as "glass ceilings". This is because, firstly, glass is often transparent, and so many of the practices that thwart inclusion continue to exist because of a lack of transparency, and secondly, because for a ceiling to prevent one's rise one needs to be near the top of an edifice, and that is surely not true as regards minorities, women and the disabled as they deal with the regulated entities.

In light of the foregoing, we do believe that we can offer some meaningful comments based upon the experiences of our constituent members, and we will seek to do so in a concise manner. In addition, we have attached to this comment letter a sampling of the practices relayed to us by our members that illustrate some of the degrees through which the regulated entities have gone to avoid inclusion, and to operate at times in a manner that is antithetical to the spirit of section 1116 ("Section 1116") of the Housing and Economic Recovery Act of 2008 ("HERA").

However, our past frustrations have in no way dampened our willingness to work with FHFA and the regulated entities to achieve the joint goals of (i) creating a culture of diversity and inclusion, and (ii) achieving higher levels of operational efficiency and profitability for the regulated entities. Therefore, we are in full support of the goals of the Amendments, especially as they seek to ensure the fulfillment of the spirit of Section 1116.

Because it is the most important part of the Amendments, we begin by saying that we believe that the new requirement that each regulated entity's board of directors adopt and set forth a "Strategic Plan" to implement Section 1116's mandate to include and utilize minorities, women, individuals with disabilities, and businesses owned by such, in all business and activities of the regulated entities, at all levels to the maximum extent possible consistent with financially safe and sound business practices, is surely a step in the right direction to creating a culture of diversity within the regulated entities. Almost as important to removing inclusion from the wings and bringing it to the core of each regulated entity's OMWI office is a plan to provide each such office with the resources and authority to adequately implement the related Strategic Plan. Yet, we do find that there are some major ingredients missing from this recipe that is designed to create a culture of inclusion.

The first is money. The decision makers at the regulated entities are people that have been, or will be, a part of the Wall Street culture that cares foremost about dollars and cents, especially as such is reflected in their salaries, bonuses and commissions. Not acknowledging what motivates decision makers will doom any well-meaning initiative to failure. Without financial rewards and punishments related to meeting inclusion goals set by the boards and the OMWI offices, the mandates will be hollow rhetoric to the day to day decision makers. Therefore, we at NASP believe it to be imperative that the incentive compensation of the regulated entities' managers be tied to the fulfilling of individual, departmental and overall inclusion goals.

The second is disclosure. We, our members, and like entities have repeatedly made the point that the reports made by the regulated entities to FHFA pursuant to Section 1116(d) (especially the elements of such reports that disclose the total amounts spent by the regulated entity on third party vendors and service providers, and the subset of such amount paid to firms owned by minorities, women and the disabled) should be made public on a regular basis, and as soon as practicable. Although the letter of section 1116(d) states that the reports are to be made to the FHFA, the "spirit" is one of disclosure and transparency. Since the beginning of the construction of our modern financial services industry regulatory structure (beginning with the Securities Act of 1933), we have seen time and again that adequate disclosure and transparency are the best tools to regulate market forces and market participants. The regulated entities are market participants that understand the power of disclosure. They also understand the power of being able to operate aspects of their business in the shadows. There can be no substitute for transparency as a tool in the fight for inclusion. Even those elements within any industry or company that would desire to paint all diversity and inclusion initiatives with the same disqualifying "quota" brush, even those elements would be hard pressed to so paint a diversity plan steeped in disclosure and transparency. The FHFA has the opportunity to insist on Strategic Plans that would allow the market to play a strong role in "deciding" what levels of diversity are appropriate for the regulated entities. This is an opportunity for the Agency to lead because the issue of diversity and inclusion disclosure is now on the table at the SEC as well. It is important that companies that operate in a diverse society, managing funds from diverse sources, and seeking to serve diverse constituencies be transparent about their diversity and inclusion status and efforts: the regulated entities are such companies.

We also have some specific wording comments. The term "all business" was not clarified. And even though the word "all" is bolded on page 12 of the proposal, the term is not defined. The problem

with not being more specific is that a lack of specificity allows a regulated entity to define any particular aspect of its business very broadly, thereby allowing it to exclude diverse participants completely from large swaths of its business. For instance, if a regulated entity defined all of its capital markets activities as a single business, as opposed to making each of the multiple profit/cost centers that exist within a capital markets operation a separate "business", diverse individuals and companies can as a result be excluded from whole businesses. As an example, a regulated entity might define its entire short-term funding activity (including multiple transactions types such as overnight funding, term discount note window, regular settle trades and discount note auctions) as one "business activity", and then proceed to meet the letter of the regulation by including minority-, women- and disabled-owned businesses in only one of these transaction types, while effectively excluding them from all other transactions in that "business activity". We believe that adding the phrase, "and transactions" to section 1207.2(b) of the Amendments, such that the pertinent phrase reads "in all businesses, activities, and transactions" will go a long way towards addressing this issue.

Regarding section 1207.21(b)(3) of the Amendments – the discussion section on page 19 indicated that the proposed rule would require the regulated entities to give "consideration to diversity when reviewing and considering contract proposals and hiring service providers". However, in the amendment text, the phrase "service providers" has been omitted. Please consider revising 1207.21(b)(3) to read "Give consideration to minority-, women-, and disabled-owned businesses when reviewing contract proposals and service providers as required under section1207.2(c)."

We also note that neither the definition of "diversity and inclusion strategic plan" (Section 1207.1), nor the section that describes "diversity and strategic planning" (Section 1207.21(d)) includes a mention of companies owned by minorities, women and disabled individuals. We believe that leaving such companies out of the strategic planning processes would be a step backwards along the path of fulfilling the letter and spirit of HERA section 1116.

In summary, while we wholeheartedly support the stated goals of the Amendments, we request that FHFA consider the following proposed changes:

1. Make achieving the diversity goals set forth in the related strategic plans one of the factors used in determining regulated entity executive compensation levels;
2. Require that the regulated entities publicly disclose their annual diversity and inclusion reports;
3. Add the phrase "and transactions" to section 1207.2(b), such that the pertinent phrase reads "in all businesses, activities, and transactions";
4. Revise section 1207.21(b)(3) to include service providers, such that the revised section would read: "Give consideration to minority-, women-, and disabled-owned businesses when reviewing contract proposals and service providers as required under section1207.2(c);"; and
5. Revise Section 1207.1 and 1207.21(d) to include references to minority-, women-, and disabled-owned businesses.

Finally, we again want to thank the Agency for the opportunity to make comments on the proposed Amendments. Attached hereto as Exhibit A is a non-exclusive set of examples of current practices of some of the regulated entities that we believe are antithetical to the spirit of Section 1116, and that should be corrected immediately. We welcome general dialogue regarding Section 1116 and the proposed Amendments, as well as specific dialogue regarding the listed examples and similar matters.

Respectfully Submitted,
Orim Graves, CFA
Executive Director, NASP

Exhibit A

Examples of Exclusionary Practices at the Regulated Entities

Please note that the following is a non-exhaustive list of such practices:

1. **Discount Note Concessions – Federal Home Loan Bank System ("FHLB")**
   Effective March 1, 2016, FHLB implemented two major changes to its discount note ("DN") concessions paid to dealers: (1) it added a two (2) basis point concession for investor orders in the DN auctions, and (2) it reduced the concession on DN window orders to 1.5 basis points (from 3 basis points).

   FHLB uses a 20 dealer group for DN auctions, none of which is a minority-, women- or disabled-owned dealer ("MWD"); all FHLB dealers have DN window access. In other words, MWDs had their fees cut in half while larger firms got a significant increase in their fees.

   Concurrent with the concession changes, FHLB introduced a $100 million capital minimum as a requirement for inclusion in the DN auction group. This requirement excludes all MWDs from participating in DN auctions and sharing in the concessions paid. This arbitrary and capricious capitalization minimum is a facially neutral policy that is intended to have, and succeeds in having, a disparate impact on MWD firms. It merely exacerbated the effect of the above-described fee reduction.

2. **Medium-Term Note Issuance**
   NASP members report, and publicly available data confirm, that each Regulated Entity fails to utilize MWDs, in any significant way, in the public issuance of medium-term notes ("MTNs"). Specifically, Freddie Mac and FHLB accomplish this process of exclusion through the use of pricing mechanisms that embed price discrimination by issuance size in their pricing grids, thus providing favorable pricing to large underwriters and placing MWD underwriters in a disadvantaged position. In addition, FHLB prohibits MWDs from underwriting certain types of structured MTNs such as callable capped floaters and range accrual notes by imposing a prohibitive, arbitrary and capricious minimum capitalization level (that is not at all related to safety and soundness) as a barrier to entry.

3. **Credit Risk Transfer Transactions**
   Freddie Mac and Fannie Mae both have a 100% MWD underwriter inclusion rate in their credit risk transfer transactions, such as Structured Agency Credit Risk Debt Notes (STACRs), Connecticut Avenue Securities (CAS) and Freddie Mac Whole Loan Securities Trust (FWLS). Typically, however, MWDs are paid fixed economics of 1%, compared with 3%-9% of fixed economics paid to other, non-MWD co-managers in these deals. 100% inclusion, 1% utilization. **<u>In other words, larger underwriters are being paid 200% to 900% more than MWD firms for doing the SAME WORK!</u>**

4. **Investment Portfolios**
   Each of the Regulated Entities fails to utilize MWDs as trading counterparts for their investment portfolios in any significant way. While quantitative data is not available due to lack of public disclosure and transparency, NASP members report inconsistent inclusion and minimal utilization by the Regulated Entities in the investment portfolio business areas.