VIA EMAIL

August 31, 2017

Mr. Alfred M. Pollard
General Counsel
Attention: Comments/RIN 2590-AA70
Federal Housing Finance Agency
400 Seventh Street SW, Eighth Floor
Washington, D.C. 20219
RegComments@fhfa.gov

RE: Notice of Proposed Rulemaking, Federal Home Loan Bank Capital Requirements, Request for Comments, RIN 2590-AA70

Dear Mr. Pollard:

The Federal Home Loan Banks (the "FHLBanks") appreciate the opportunity to comment on the Federal Housing Finance Agency's ("FHFA") notice of proposed rulemaking on Federal Home Loan Bank Capital Requirements (the "Proposed Rule"). Set forth below are our comments on the Proposed Rule.

EXECUTIVE SUMMARY OF COMMENTS

1. Extended Implementation. The FHLBanks request that the FHFA provide an effective date for the final rule that is at least one year, and preferably 18 months, after publication. The FHLBanks require this additional time to adjust their systems, controls, processes and procedures, to fully evaluate their methodologies, and to develop and validate any models needed to implement the new rule.

2. Equitable Treatment of All GSEs. The FHLBanks believe that all government sponsored enterprises ("GSE") should be treated the same under the final rule as they are under the current rule. All exceptions and special limits under the Proposed Rule that would apply only to GSEs that are operating with capital support or other direct financial assistance from the U.S. government, including the special limit for GSEs on unsecured extensions of credit in section 1277.7(c), should apply instead to all GSEs. GSEs operate under close oversight of Federal regulators and within narrowly defined statutory provisions that help ensure their continued safety and soundness. In many cases, GSEs also have access to direct Federal assistance, if necessary, to support the continuation of their public missions in times of financial distress, thereby reducing the risk associated with their obligations.

3. Treatment of Private Label Mortgage Backed Securities. The FHLBanks believe that the credit risk percentage requirements (CRPR) assigned to collateralized mortgage obligations (CMOs) are significantly above the corresponding risks posed by such assets. These instruments are often structured with senior and subordinate tranches, but closely align in their performance with pass-through residential mortgage securities. The CRPRs for CMOs in the Proposed Rule are the same as those for subordinated classes of mortgage backed securities in the current rule, which change appears to be overly conservative and punitive given that subordinated tranches absorb losses prior to senior tranches. For example, the 100% CRPR for the FHFA CMO 7 category seems to assume a default similar to that of an unsecured obligation, where no recovery is anticipated, as opposed to an instrument secured by residential mortgage loans. This excessive CRPR is not reflective of current market valuations or the historical performance of these securities. The FHLBanks request the FHFA to reconsider the CRPRs for CMOs in categories three through seven in Table 1.4 of the Proposed Rule, and equalize their treatment with that of pass-through residential mortgage securities in Table 1.4 of the Proposed Rule unless the securities exhibit the characteristics of a subordinated tranche and the performance of an unsecured investment. Additionally, language further clarifying that FHLBanks' internal credit ratings should be based on future potential losses to an FHLBank as compared to its amortized cost would be helpful where the FHLBanks have private-label mortgage-backed securities (PLMBS) with other-than-temporary-impairment. Significant differences in FHFA ratings are possible between an internal rating similar to a nationally recognized statistical ratings organization (NRSRO) methodology (one implicitly based on potential future losses of principal relative to par) as compared to an internal rating based on potential losses relative to amortized cost. Differences in interpretation may result in examination uncertainty.

4. FHLBank Internal Credit Ratings Process. The FHLBanks request that the FHFA delete the provision that would allow the FHFA, on a case-by-case basis, to direct an FHLBank to change the calculated credit risk capital charge for certain assets to remedy any deficiency that FHFA identifies with respect to an FHLBank's internal credit rating methodology for such assets. The FHLBanks believe a more productive remedy for any such deficiencies would be for the FHFA to address them through its existing supervisory authority to direct changes in an FHLBank's methodology and processes, rather than a direction to change a calculated credit risk capital charge for an asset on an individual basis.

5. Treatment of Derivatives Contracts. The FHLBanks have a number of comments related to the Proposed Rule's treatment of derivatives contracts. Specifically, the credit risk capital requirement for cleared derivatives should be clarified so that their current credit exposure is a de minimis amount and that the initial margin model utilized by the derivatives clearing organization (DCO) may be used to determine the potential future exposure. In addition, since potential future fluctuations in value in a cleared derivatives contract are secured through the initial margin collected by the DCO from both trading counterparties to the contract, including both potential future exposure and excess collateral (initial margin) in the credit risk capital charge is unnecessary, and should be eliminated. The adjustments for collateral held for uncleared derivatives should be applied directly to the current or future exposure, and not be subject to the applicable CRPR based on the type of collateral posted. The FHLBanks also believe that the final rule should retain the treatment in the current rule for derivatives contracts with members, in which the CRPRs are the same as for advances, since these derivatives contracts are fully collateralized similar to advances.

6. Treatment of Multifamily and Commercial Mortgage Backed Securities. The FHLBanks request that the final rule treat multifamily residential mortgage backed securities consistent with the treatment of those securities consisting of loans secured by one-to-four dwelling units. This treatment would be consistent with the FHLBanks' housing mission, the promotion of affordable housing, and the characteristics of, and risks associated with, the underlying assets. The FHLBanks also recommend that commercial mortgage-backed securities (CMBS) should be treated as a separate category of assets with a table of CRPRs reflecting the better loss history for these collateralized obligations than for unsecured or subordinated securities.

7. Treatment of Advances. While modest in impact, the FHLBanks do not believe that the increase in CRPRs for advances in Table 1.1 of the Proposed Rule is justified given the historic performance, enhanced rights and protections under the FHLBank Act, and absence of loss with respect to advances. On the contrary, these factors would indicate that the CRPRs for advances should be reduced. In addition, substantial increases in the CRPRs for longer-term advances seem inconsistent with the FHLBanks' public mission to provide a consistent source of liquidity to members to support lending in their communities. The FHLBanks recommend that the final rule readopt the CRPRs for advances stated in the current rule.

8. Operational Risk Capital Requirement. The FHLBanks request that the FHFA remove the lower bound in section 1277.6(b) of the Proposed Rule on the operational risk capital requirement equal to 10 percent of the sum of an FHLBank's credit risk and market risk capital requirements if the FHLBank provides an alternative methodology for assessing and quantifying an operational risk capital requirement. We believe that such lower bound is unnecessary if the operational risk capital requirement methodology has been reviewed and approved by the FHFA. Alternatively, should the FHFA determine to retain this lower bound, and the operational risk capital requirement of 30 percent in the absence of an alternative methodology, the FHFA should provide additional analytical support in the final rule for its choice of these percentages.

9. Miscellaneous Comments. The FHLBanks suggest a number of revisions to the Proposed Rule to further clarify its meaning: (i) add definitions for "internal cash flow model" and "internal market risk model" in section 1277.5(a)(2); (ii) revise the reference to the appropriate historical observation period for an internal market risk model in section 1277.5(b)(4)(ii) from "1978" to "1992" to be consistent with prior FHFA guidance; (iii) clarify that "remaining maturity" for purposes of Table 1.2 means the weighted average life of such asset, as opposed to contractual maturity; (iv) revise section 1277.7(e)(2) to make reporting of total secured and unsecured extensions of credit quarterly as opposed to monthly, which would be consistent with current reporting requirements and other changes in the Proposed Rule revising reporting requirements from monthly to quarterly.

EXPLANATION OF COMMENTS

1. Extended Implementation Timeline

The FHLBanks request additional time before the final rule becomes effective after issuance by the FHFA. At a minimum, the FHLBanks request at least one year, and preferably 18 months, before effectiveness of the final rule to update their systems, internal controls, processes and procedures, and to validate their internal ratings methodologies and models. The replacement of NRSRO ratings likely may involve the creation or identification, validation, and implementation of new credit methodologies and models, which under current governance standards could take one year or longer to fully implement. Additionally, system updates will be needed to implement changes to credit rating scales, asset categorizations, and exposure calculations. The FHLBanks also need additional implementation time to update their compliance systems to reflect the new requirements. Providing an adequate implementation period permits the FHLBanks to ensure that they have time to make the necessary changes to be in full compliance with the provisions of the final rule.

2. Equitable Treatment of All GSEs

The FHLBanks believe that the FHFA should broaden the exceptions and special limits in sections 1277.4(f)(3), 1277.4(g)(2)(i) and 1277.7(c) of the Proposed Rule that are applicable only to GSEs operating with capital support or other form of direct financial assistance from the Federal government to include all GSEs. GSEs are subject to robust Federal regulation and oversight, and operate within carefully defined and circumscribed limits that reduce the risk of such entities and their obligations. Many of the GSEs have existing relationships with the Federal government that would provide for financial support, if necessary, for the GSE to continue its public mission in the event of financial distress. The FHLBanks believe that it is not appropriate to differentiate among the GSEs based upon the existence of outstanding capital support or other financial assistance programs that were put in place during the most recent financial crisis to support the operations of certain GSEs. The GSEs, including the FHLBanks, which were able to continue to operate throughout the financial crisis without such support, should not be penalized for their financial stewardship.

The FHLBanks believe that the restriction in the proposed regulation on investments in GSE obligations where the GSE is not subject to direct support from the Federal Government is a significant departure from the current standards applicable to FHLBank investments in GSE securities under existing 12 C.F.R. 932.9. The current regulatory provision was developed through several significant public rulemaking steps due to the potential impact of limiting an FHLBank's investment in a GSE's obligations to 15% or less of an FHLBank's capital as originally proposed by the Federal Housing Finance Board (Finance Board). When adopting the final regulation with the current GSE unsecured credit limit, the Finance Board affirmed that further limiting the FHLBanks' extensions of unsecured credit to GSEs may have disrupted the FHLBanks' investment strategies. Additionally, in adopting its final regulation with the current GSE limit, the Finance Board specifically expressed that it did not have safety and soundness concerns relating to extensions of unsecured credit to a GSE. *See* 66 FR 66718, 66722. As was noted in 2001, lowering the GSE unsecured limits as now proposed would similarly disrupt the FHLBanks' investment strategies--particularly given the limited asset classes in which the FHLBanks are permitted to invest. The current regulatory limits have been in place for over 15 years, have operated effectively and have not

resulted in increased risk for the FHLBanks. Consequently, the FHLBanks believe that it is not necessary to change the existing limits for GSE securities as set forth in the proposed rule.

Footnote 68 in the preamble to the Proposed Rule cites eligible collateral haircuts in the uncleared margin rules as support for differentiating between the extension of unsecured credit by GSEs operating with and without capital support or other financial assistance from the United States. The FHLBanks acknowledge the reasons cited by the prudential regulators for differentiating the haircuts for GSEs operating with and without capital support or other financial assistance from the United States, but do not believe that there should be a direct link between collateral haircuts for uncleared derivatives (to mitigate price volatility) and the extension of unsecured credit (to limit credit exposure). Furthermore, the magnitude of the haircut differences among the GSEs in the uncleared margin rules (i.e., 0.5, 2.0, and 4.0 versus 1.0, 4.0, and 8.0) do not justify an unsecured limit of only 15% of FHLBank capital for GSEs operating without capital support or other financial assistance from the United States compared to 100% of Bank capital for GSEs operating with such capital support or other financial assistance from the United States.

To the extent the FHFA does not provide an exception in the final rule for all GSEs, the FHLBanks believe, at a minimum, the exception for GSEs operating with government capital support or other direct financial assistance should apply to successors of such GSEs to the extent such capital support or financial assistance remains in place for such successor. In addition, the exception should remain in place for outstanding securities or other obligations of the GSE to the extent such securities and obligations remain subject to Federal government support, even if the GSE no longer has capital support or direct financial assistance going forward.

3. Treatment of PLMBS.

a) *CRPRs for CMOs*

The CRPRs for CMOs in Table 1.4 of the Proposed Rule are overly conservative and disproportionately high in relation to the risk posed by these assets. The proposed CRPRs for CMO credit rating categories are the same as the previous CRPRs for "subordinated classes of mortgage assets." The preamble to the Proposed Rule states that the percentage factors to be used for CMOs are based on historical loss experiences for subordinated mortgage classes. Subordinated mortgage classes are the classes that would take losses first in a transaction, and prior to the more senior classes. The FHLBanks do not invest in these riskier, subordinated tranches of PLMBS. As a result, the factors that are being assigned to the credit risk categories are overstated for CMOs owned by the FHLBanks. This can be seen in the last category, or FHFA CMO 7, in Table 1.4, which assumes a 100% CRPR implying a 100% loss on the asset. This implies that, under the assumed 99.9% confidence level stress case, there would be zero return of amortized cost, which does not seem plausible for other than subordinated tranches, which are not characteristic of the PLMBS historically purchased by the FHLBanks. The performance and market value of the CMOs held by the FHLBanks closely align with pass-through residential mortgage securities, which enjoy significantly more favorable treatment under the Proposed Rule. Accordingly, the FHLBanks request the FHFA to reconsider the CRPRs for CMOs in categories three through seven in Table 1.4 of the Proposed Rule, and equalize their treatment with that of pass-through residential mortgage securities in Table 1.4 of the Proposed Rule unless the

securities exhibit the characteristics of a subordinated tranche and the performance of an unsecured investment.

b) *Credit Risk Capital Charges for Residential Mortgage Securities*

Section 1277.4 (g)(iii) of the Proposed Rule should be revised in the final rule to include the bold language below:

> Each Bank shall align its various internal credit ratings, **which should at least in part be related to its potential future losses**, to the appropriate categories of FHFA Credit Rating included in Table 1.4 to §1277.4. In doing so, each Bank shall ensure that the credit risk associated with any asset assigned to categories FHFA RMA 1 through 4 or FHFA CMO 1 through 4 is no greater than that associated with an instrument that would be deemed to be of "investment quality," as that term is defined by 12 C.F.R 1267.1. FHFA Categories 3 through 1 shall include assets of progressively higher credit quality than Category 4, and FHFA Categories 5 through 7 shall include assets of progressively lower credit quality.

The bolded language above would clarify that the FHLBanks' internal credit ratings should be based on potential future losses to an FHLBank. Generally, risk-based capital is the required capital to protect against future potential losses to an entity under the 99.9% confidence level stress scenario assumed by the FHFA. Conceptually, the best measure to determine this for residential mortgage securities with other-than-temporary-impairment is to compare the future potential losses to the FHLBank to such security's amortized cost rather than the risk categorization based on the full face value of the security. In essence, the FHLBank has already reserved (or has actually absorbed losses with) capital against securities previously written down with other-than-temporary-impairment. The FHLBanks also note that the future risk of securities is reduced by losses that have already been absorbed through net income, and the rating classification process should net losses that have already been incurred from the assessment of potential future losses in mapping securities among the various FHFA RMA or FHFA CMO categories.

4. <u>FHLBank Internal Credit Ratings Process</u>

The FHLBanks request that the FHFA delete the provision in sections 1277.4(f)(4) and 1277.4(g)(2)(iii) that would allow the FHFA, on a case-by-case basis to direct an FHLBank to change the calculated credit risk capital charge for certain assets to remedy any deficiency that FHFA identifies with respect to an FHLBank's internal credit rating methodology for such assets. The FHLBanks believe a more productive remedy for any such deficiencies would be for the FHFA to address them through its existing supervisory authority to direct a change in an FHLBank's methodology and processes, rather than a direction to change a calculated credit risk capital charge for an asset on an individual basis. This approach would help ensure consistency across FHLBanks by focusing on methodological changes rather than focusing on specific assets.

5. Treatment of Derivatives Contracts

a) *Calculation of CCE and PFE for Cleared Derivatives.*

The FHLBanks request that section 1277.4(i) of the Proposed Rule expressly include a methodology for the calculation of credit exposures for cleared derivatives contracts. Specifically, section 1277.4(i)(1) should clarify that for the purpose of determining current credit exposure the mark-to-market for cleared derivatives contracts equals a de minimis amount. In addition, section 1277.4(i)(2) should identify that an initial margin model used by a DCO either meets the requirements of section 1221.8 or could be used to determine potential future credit exposure.

The preamble to the Proposed Rule states, ". . . section 1277.4(e)(4)(ii) of the proposed rule would impose a capital charge of 0.16 percent times the sum of a Bank's marked-to-market exposure on the cleared derivatives contract, plus its potential future exposure on the contract, plus the amount of any collateral posted by the Bank and held by the clearing organization that exceeds the amount of the Bank's current obligation to the clearing organization under the contract." Footnote 30 in the preamble clarifies that for cleared derivatives the current exposure would often be zero or small since most DCOs effectively settle derivatives contracts at the end of each day. Section 1277.4(i)(1) of the Proposed Rule prescribes a methodology for the calculation of credit exposures for derivatives contracts for (i) single derivatives contracts (i.e., no eligible master netting agreement) and (ii) derivatives contracts subject to an eligible master netting agreement. Since cleared derivatives contracts are different from uncleared derivatives contracts (in which the distinction between single contracts and contracts subject to an eligible master netting agreement remains appropriate), the FHLBanks request that section 1277.4(i)(1)(i) of the Proposed Rule be modified to specify that the mark-to-market value for cleared derivatives contracts is de minimis. This will eliminate any perceived inconsistencies or misunderstandings with respect to the calculation of current credit exposure for cleared derivatives between the rule text and the preamble, and among DCOs.

Section 1277.4(i)(2) of the Proposed Rule specifies alternatives for determining potential future credit exposure, which applies to both cleared and uncleared derivatives contracts. Section 1277.4(i)(2)(i) provides for the use of an initial margin model that meets the requirements of section 1221.8 of the FHFA regulations. However, the initial margin requirements for cleared derivatives contracts are determined by the DCO in accordance with regulations of the Commodity Futures Trading Commission, which are not subject to section 1221.8. As a result, the FHLBanks would be required to use the provision in section 1277.4(i)(2)(ii) (i.e., Appendix A to Part 1221) to determine potential future credit exposure. The FHLBanks request that section 1277.4(i)(2)(i) of the Proposed Rule explicitly permit the use of a DCO's initial margin model.

b) *Cleared Derivatives Calculation of Credit Risk Capital Requirement*

The FHLBanks request clarification of section 1277.4(e)(4)(ii)(C) of the Proposed Rule, which states that the credit risk capital charge for a cleared derivatives contract shall include "[t]he amount of collateral that the Bank has posted to, and is held by, the derivatives clearing organization, but only to the extent the amount exceeds the Bank's current credit

exposure to the derivatives clearing organization." Since variation margin payments typically are not held as collateral by the DCO, but may be considered daily settlement of payments due on the derivatives contract, the amount of collateral posted and held by the DCO will be equal to the DCO's initial margin requirement for the FHLBank. Initial margin is required by law to be posted by both parties to a cleared derivatives contract to protect the DCO, and by extension, the parties to the contract, from fluctuations in the future value of the contract. In this sense, initial margin performs a similar risk mitigation and protection function as the calculation and capitalization of the potential future credit exposure for the derivatives contract. The initial margin is required to be held by the DCO under strict legal requirements including segregation, control and investment limitations that act to protect the initial margin from loss. The FHLBanks do not believe that the credit risk capital charge should include both potential future exposure, and the initial margin required and held by the DCO as collateral, and request that the final rule be amended to remove the credit risk capital charge relating to the collateral, and instead rely solely on the potential future credit exposure based on the initial margin posted for the transaction. To the extent this capital charge only relates to "excess" collateral that may be required by a futures commission merchant (FCM) in addition to that required as initial margin by the DCO, or due to timing differences in the transfer of collateral, this limitation should be made explicit in the final rule.

In addition, the FHLBanks interpret the exception for cleared derivatives transactions in section 1277.7(g)(2) of the Proposed Rule dealing with unsecured exposure to include the posted collateral also, and suggest making this clear in the preamble to the final rule.

c) *Uncleared Derivatives Calculation of Credit Risk Capital Requirement*

The Proposed Rule methodology for determining the credit risk capital requirement for uncleared swaps could be improved to better reflect the highly regulated nature of this market. Specifically, the proposed adjustments for collateral held to reduce current credit exposure and potential future credit exposure permitted in section 1277.4(e)(2)(i) of the Proposed Rule should better align with the public policy purpose of holding and posting collateral. The Uncleared Margin Rules ("UMR") issued by federal regulators require financial counterparties to an uncleared derivatives transaction to exchange variation margin to mitigate current exposure, and in certain circumstances, initial margin to mitigate potential future exposure. Accordingly, the adjustments for collateral held should be applied directly to the exposure calculations in section 1277.4(e)(1)(i) and section 1277.4(e)(1)(ii) of the Proposed Rule, and not be subject to the applicable credit risk percentage requirement based on the collateral type pursuant to section 1277.4(e)(2)(i)(C). For example, under the proposed methodology, an FHLBank may reduce the current credit exposure charge by applying the discounted value of any collateral held, provided that a discount amount is applied and equal to at least the minimum discount required under Appendix B to part 1221, subject to the applicable credit risk percentage requirement of the collateral held. In the likely event that cash is held, the applicable credit risk percentage requirement is 0.00%, pursuant to Table 1.3 to section 1277.4. This results in a zero adjustment to current credit exposure. The Proposed Rule, as written, applies a credit risk percentage requirement to the collateral held, which results in a larger adjustment (and lower credit charge) for riskier assets held as collateral. This presumably is unintended and can be addressed by permitting the exposure, current or potential, to be adjusted by the amount of collateral held for that

exposure (without being subject to the applicable credit risk percentage requirement). In regards to current credit exposure, the appropriate credit risk percentage requirement pursuant to section 1277.4(e)(1)(i) would apply to the difference, if any, between current credit exposure per section 1277.4(i)(1) and collateral held. For illustrative purposes, the formulaic interpretation of the proposed rule and the alternate methodology for current credit exposure are presented below.

PROPOSED RULE:
CREDIT RISK CAPITAL REQUIREMENT
= (CCE * $CRPR_{COUNTERPARTY}$) – (COLLATERAL HELD * $CRPR_{COLLATERAL}$)

WHERE
CCE = CURRENT CREDIT EXPOSURE
$CRPR_{COUNTERPARTY}$ = CREDIT RISK PERCENTAGE REQUIREMENT OF COUNTERPARTY PER TABLE 1.2 TO § 1277.4
$CRPR_{COLLATERAL}$ = 0.00% WHEN FOR CASH, TABLE 1.3 TO § 1277.4

ALTERNATIVE:
CREDIT RISK CAPITAL REQUIREMENT
= (CCE – COLLATERAL HELD) * $CRPR_{COUNTERPARTY}$

To the extent that initial margin is posted for uncleared derivatives, a similar methodology as that suggested above for current credit exposure also should be used with respect to the calculation of the credit risk capital requirement for potential future credit exposure.

d) Collateral Valuation

Section 1277.4(e)(1)(iii) of the Proposed Rule should be clarified to state that collateral posted by an FHLBank with respect to a derivatives contract should be valued without reduction for any discounts or haircuts imposed on the collateral by agreement or regulation. Similarly, section 1277.4(e)(2) should be clarified to make clear that collateral received by an FHLBank should be valued after reduction for any discounts or haircuts imposed by agreement or regulation. Moreover, since collateral pledged by an FHLBank is subject to a capital charge as a balance sheet asset, the existing capital charge should only reflect the incremental CRPR, if any, that is attributable to the risk of the custodian or other party that holds the asset to avoid double-counting the risk associated with the asset.

e) *Treatment of Guarantors*

Section 1277.4(e)(2)(ii) specifies that if a derivatives contract is guaranteed by a third-party, then the CRPR "may" be that of the guarantor, rather than the counterparty. On the other hand, section 1277.7(a) of the Proposed Rule states that the guarantor "shall" be considered the counterparty for purposes of determining the unsecured credit limit for the transaction. We suggest revising section 1277.7(a) in the final rule to say "may" consistent with section 1277.4(e)(2)(ii).

f) *Derivatives Contracts with Members*

In addition, the FHLBanks believe that the final rule should retain the treatment in the current rule for derivatives contracts with members, in which the CRPR are the same as for advances, since these derivatives contracts are fully collateralized similar to advances. These exposures with members are typically secured by a lien covering the same assets as those pledged for advances, which is different from normal derivatives contracts with dealer counterparties.

6. Treatment of Multifamily and Commercial Mortgage Backed Securities.

Residential mortgage securities in section 1277.1 of the Proposed Rule means instruments representing an undivided interest in a pool of residential mortgages, and residential mortgages is defined to include only loans secured by residential structures containing one-to-four dwellings. These definitions would not include multi-family properties, or securities backed by such properties, despite the fact that multi-family developments have become increasingly important to housing in the United States since the most recent financial crisis due to issues of affordability and consumer preferences.

The Proposed Rule would treat single-family residential mortgage assets more favorably than multi-family assets, which are included as non-mortgage assets for capital purposes under the Proposed Rule. The FHLBanks request that the final rule be amended to correct this misalignment in treatment of residential housing assets, and treat multi-family mortgage backed securities consistent with the treatment of those securities consisting of loans secured by one-to-four dwelling units. Section 10(a)(3) of the FHLBank Act provides that the FHLBanks may lend against mortgages on residential property, which includes multi-family residences. Similarly, section 1266.1 of the FHFA regulations, dealing with collateral for FHLBank advances, also defines residential real property to include multifamily property.

If the FHFA is not willing to treat multi-family residential mortgage securities the same as single-family mortgage securities, then the FHFA should develop a separate category for these assets that acknowledges the better loss history of such assets compared to other longer-dated, non-mortgage assets covered by Table 1.2 of the Proposed Rule. Similarly, the FHLBanks believe that the FHFA should develop a separate table for CMBS that also reflects the better loss history of these collateralized assets relative to unsecured or subordinated obligations.

7. Treatment of Advances.

While modest in impact, the FHLBanks do not believe that the increase in CRPRs for advances in Table 1.1 of the Proposed Rule is justified given the historic performance and absence of loss with respect to advances. On the contrary, the preamble makes clear that no FHLBank has ever experienced a default on an advance. Moreover, given the enhanced rights and protections established for FHLBank advances by the FHLBank Act, it is not clear that the default rate used for setting the CRPRs for advances should necessarily be that of non-mortgage assets of the highest investment category because advances have superior credit characteristics. In addition, substantial increases in the CRPRs for longer-term advances seem inconsistent with the FHLBanks' public mission to provide a consistent source of liquidity to members to support lending in their

communities. These factors suggest that, if any change should be made to the CRPRs for advances, these figures should be reduced, and not increased. However, if the CRPRs may not be reduced, the FHLBanks recommend that the final rule readopt the CRPRs for advances stated in the current rule.

8. Operational Risk Capital Requirement.

The FHLBanks request that the FHFA remove the lower bound in section 1277.6(b) of the Proposed Rule on the operational risk capital requirement equal to 10 percent of the sum of an FHLBank's credit risk and market risk capital requirements if the FHLBank provides an alternative methodology for assessing and quantifying an operational risk capital requirement. The FHLBanks believe that such lower bound is unnecessary if the operational risk capital requirement methodology has been reviewed and approved by the FHFA. Alternatively, should the FHFA determine to retain this lower bound, and the operational risk capital requirement of 30 percent in the absence of an alternative methodology, the FHFA should provide additional analytical support in the final rule for its choice of these percentages.

9. Miscellaneous Comments.

The FHLBanks suggest a number of revisions to the Proposed Rule to further clarify its meaning: (i) add definitions for "internal cash flow model" and "internal market risk model" in section 1277.5(a)(2); (ii) revise the reference to the appropriate historical observation period for an internal market risk model in section 1277.5(b)(4)(ii) from "1978" to "1992" or other appropriate date to be consistent with prior or anticipated FHFA guidance; (iii) clarify that "remaining maturity" for purposes of Table 1.2 means the weighted average life of such asset, as opposed to contractual maturity; (iv) revise section 1277.7(e)(2) to make reporting of total secured and unsecured extensions of credit quarterly as opposed to monthly, which would be consistent with current reporting requirements and other changes in the Proposed Rule revising reporting requirements from monthly to quarterly.

We appreciate your consideration of these comments.

Sincerely,

FEDERAL HOME LOAN BANK OF ATLANTA

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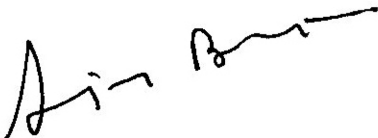

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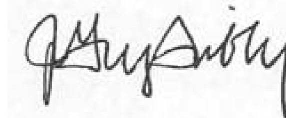

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