

August 31, 2020

Alfred M. Pollard, General Counsel,

Attention: Comments/RIN 2590-AA95,

Federal Housing Finance Agency

Eighth Floor

400 Seventh Street, SW

Washington, DC 20219

Subject: (RIN) 2590-AA95 FHFA Proposed Rule on Enterprise Regulatory Capital Framework

Mr Pollard:

We welcome the opportunity to comment on the FHFA's proposed capital rule and respond to two of FHFA's questions. Quinn Opportunity Partners LLC is an investment management company with experience investing in large U.S. financial institutions and manages investment vehicles that are security holders of Fannie Mae and Freddie Mac.

Question 1. "Is each of the definitions of CET1 capital, tier 1 capital, and tier 2 capital appropriately formulated and tailored to the Enterprises"?, AND

Question 3. "Should any other capital elements qualify as CET1 capital, additional tier 1 capital, or tier 2 capital elements?"

Response: FHFA's approach of applying Basel framework definitions of tier 1 capital and CET1 capital is a sensible overall approach, but the definition of tier 1 capital should be expanded to include one element that is within the spirit of the Basel and FHFA framework, yet reflects the nature of the GSE's business as monoline guarantors. Specifically, FHFA should consider the nature of the GSE's upfront fee amortization income and credit the amount of unamortized upfront guaranty fees as Tier 1 capital.

When the GSEs receive upfront guaranty fees or charge LLPAs, the benefit is immediate. But the associated income is recognized only over the contractual life of the mortgage. This is consistent with the matching principle of GAAP but masks the economics of the transaction and hides the true loss-absorbing nature of the asset.

Deferred amortization balances will be recorded over time as income. This is the source of a substantial portion of GSE net income from the existing guaranty portfolios. The 10-Ks of Fannie and Freddie both indicate amortization income is approximately 40% of single-family guaranty net income (excluding TCCA).

We highlight that providing tier 1 capital for these balances is not the same as giving credit to the GSEs for future revenue. The FHFA resistance to the latter is sensible because, for example, the GSEs would not realize future G-fees if a loan refinanced with another guarantor or a government agency. In contrast, upfront guaranty fees will always be recorded into income eventually. The prepayment of a mortgage through refinance or paydown instantly recognizes the entire unamortized balance.

And because the benefits inevitably flow into capital over time, unamortized upfront guaranty fees have a loss absorbing nature and should be considered tier 1 capital.

The magnitude of these balances is not clearly delineated in the 10-Ks for Fannie and Freddie, but we note that Fannie's latest 10-Q reported \$33.6 billion of deferred amortization income and Freddie's 10-K reports a \$43.5 billion balance of unamortized premiums. The magnitude of this capital adjustment would likely credit the GSEs with tens of billions of Tier 1 capital.

We also commend similar suggestions on this subject submitted by The Urban Institute.

Thank you for your consideration.

Sincerely,

Patrick Quinn

Managing Partner

Quinn Opportunity Partners LLC

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