FHLBANKS
A NATION OF LOCAL LENDERS

June 23, 2023

Clinton Jones, Esq.
General Counsel
Attention: Comments/RIN 2590–AB10
Federal Housing Finance Agency
Fourth Floor
400 Seventh Street SW
Washington, D.C. 20219

Re: Proposed Rulemaking on Prudential Management and Operations Standards (Comments/RIN 2590–AB10)

Dear Mr. Jones:

On behalf of the Council of Federal Home Loan Banks (the "Council"), and with the unanimous support of the eleven Federal Home Loan Banks (each an "FHLBank") and the Office of Finance (the "OF" and, together with the FHLBanks, the "FHLBank System"), we appreciate this opportunity to comment on the proposed rulemaking of the Federal Housing Finance Agency (the "FHFA") on prudential management and operations standards (the "Proposal"). The Council is a trade association that represents the FHLBank System's views and positions before policymakers.

The FHFA indicates that the Proposal is intended to amend its existing prudential management and operations standards rule (as proposed, the "Rule") to clarify that the FHFA may establish those standards as regulations as well as guidelines, to revise related definitions and make other conforming changes, and to apply to the OF the Rule and some of the existing standards in the appendix to the Rule.

Application of the Statute and the Rule to the OF

We appreciate the FHFA staff's focus on the safety and soundness of the regulated entities and the OF, as well as their thoughtfulness in related rulemaking. The OF, as a joint office of the FHLBanks, is an integral component of the FHLBank System, while at the same time it is a unique organization in light of its functions and its governance structure under the Federal Home Loan Bank Act and applicable FHFA regulations. As further discussed below, we believe that the unique nature of the OF, for purposes of regulation and supervision, has long been recognized by both Congress and the FHFA (and its predecessor agencies). It is our hope that the FHFA will continue to recognize

and be mindful of, as it has in the past, the unique nature of the OF (and many differences between the OF and the regulated entities) for purposes of regulation and supervision, including in connection with its rulemaking.

The Proposal would implement section 1108 of the Housing and Economic Recovery Act of 2008 ("HERA"), codified at 12 U.S.C. § 4513b. Section 1108 of HERA added section 1313B of the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (as amended by HERA, the "Safety and Soundness Act"), which provides the FHFA with the authority to establish standards that address ten subjects relating to the management and operation of the "regulated entities". HERA also amended the Safety and Soundness Act to include a specific definition of "regulated entity," which, for purposes of the Safety and Soundness Act (including section 1313B thereof), means the "(A) Federal National Mortgage Association and any affiliate thereof; (B) the Federal Home Loan Mortgage Corporation and any affiliate thereof; and (C) any Federal Home Loan Bank."[1] The term "regulated entity" as so defined in the Safety and Soundness Act does not include the OF.[2]

We respectfully submit that, in making its determination only to refer to "regulated entity" in 12 U.S.C. § 4513b and not to refer to the OF, Congress expressed a clear intent that the provisions in 12 U.S.C. § 4513b be applied *only* to Fannie Mae and Freddie Mac (and their affiliates) and the FHLBanks, but *not* to the OF. We believe this position is strongly supported by the fact that Congress also amended the Safety and Soundness Act to expressly refer to *both* the regulated entities *and* the OF when it intended to do so.[3] Furthermore, we believe this position is strongly supported by the nature of potential issues that 12 U.S.C. § 4513b seeks to address and remedy (e.g., extraordinary growth by a regulated entity and management of certain risk exposures) and related corrective actions that the statute authorizes the FHFA to take (e.g., limiting average total assets or increasing the ratios of core capital or total capital to assets), none of which is intended to apply to the OF. We also note that 12 U.S.C. §§ 4513b(a)(11) and (b)(2)(B)(iii), cited in the Proposal as giving the FHFA additional authorities in connection with this

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[1] 12 U.S.C. § 4502(20). Similarly, in 12 C.F.R. §1201.1, the FHFA defines the term "regulated entity" to mean "the Federal Home Loan Mortgage Corporation and any affiliate thereof, the Federal National Mortgage Association and any affiliate thereof, and any Federal Home Loan Bank."

[2] 12 U.S.C. § 4502(19) defines the term "Office of Finance" as the "Office of Finance of the Federal Home Loan Bank System (or any successor thereto)."

[3] For example, section 1101 of HERA amended the Safety and Soundness Act to specifically refer to the Director as having general regulatory authority over each "regulated entity *and the Office of Finance*" (emphasis added). See 12 U.S.C. § 4511(b)(2). Similarly, section 1153 of HERA amended the Safety and Soundness Act to provide that any person subject to a removal or prohibition order under that section shall not participate in any manner in the conduct of the affairs of any "regulated entity *or the Office of Finance*" (emphasis added), and to provide that any such person shall not vote for a director, or serve or act as an entity-affiliated party of "a regulated entity or as an officer or director of the *Office of Finance*" (emphasis added). See 12 U.S.C. §§ 4636a(d)(1) and (4). See also 12 U.S.C. § 4636a(e), which contains several references to a "regulated entity *or the Office of Finance*" (emphasis added).

Congressional mandate, likewise apply to "regulated entities" only, but not the OF, by their own terms, and therefore do not support the application of the Rule to the OF.

We acknowledge the FHFA's general regulatory authority over the OF under 12 U.S.C. § 4511(b)(2), and we understand that the FHFA has expressly relied on this general regulatory authority in its prior rulemaking when related statutory provisions do not on their face authorize the FHFA to include the OF in such rulemaking.[4] We respectfully request that the FHFA re-consider its proposal to apply the Rule to the OF.[5] Should the FHFA ultimately decide to apply the Rule to the OF, we request that it clarify in the adopting release that it is relying on its general regulatory authority over the OF, rather than 12 U.S.C. § 4513b (which, as discussed above, we do not believe grants the FHFA that authority). It would also be helpful for the FHFA to more clearly articulate its rationale (as it has done in other situations in its prior rulemaking affecting the OF) as to why applying the Rule to the OF would further the specific purposes of 12 U.S.C. § 4513b with respect to the regulated entities or the purposes of other applicable law, in particular since the Proposal, if adopted, would represent an apparent change in the FHFA's position as related to the OF from its original rulemaking on this subject matter in 2011.

Operation of the Rule and the Standards as Related to the OF

We appreciate the FHFA staff's thoughtful approach in not proposing the application to the OF of all of the ten standards in the appendix to the Rule and in inserting the phrase "as applicable" or similar wording in various sections from a drafting perspective. We respectfully request that the FHFA further clarify in the final rule the scope of applicability of certain standards as related to the OF.

This is of particular significance under Standard 8 — Overall Risk Management Processes. While we do not believe it is the FHFA's intention to require the OF to manage many of the risks enumerated under that standard (and other standards not proposed to apply to the OF), such as market, credit/counterparty and liquidity risks, the standard nonetheless states that the board of directors is responsible for "approving *all major risk limits*, and ensuring incentive compensation measures for senior management capture *a full range of risks* to the regulated entity or the Office of Finance" and that "[e]ach regulated entity and the Office of Finance should have *a comprehensive set of risk limits*." The standard also appears to suggest that the OF should review its risk exposures "on both a business unit (or business segment) and enterprise-wide basis"; however, the OF has historically managed its risk exposures on an enterprise-wide basis, which the OF believes is appropriate in light of the scope of its activities and the nature of its risk exposures.

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[4] See, e.g., 74 Fed. Reg. at 38560 ("Based on its general regulatory authority over the Office of Finance, FHFA is proposing that this regulation apply to the Office of Finance") (rulemaking related to record retention); 75 Fed. Reg. at 47496 (rulemaking related to the establishment of the FHFA's Office of the Ombudsman); 74 Fed. Reg. at 30976 (rulemaking related to golden parachute and indemnification payments amendments).

[5] Among others, bringing the OF within the scope of 12 U.S.C. § 4513b as contemplated in the Proposal may lead to unintended consequences for both the OF and the FHFA's regulation and supervision of the OF.

We request that the FHFA expressly re-affirm, either in the final rule or standards or elsewhere in the adopting release, the matters that are not relevant to the OF for purposes of compliance, similar to what it did in the original rulemaking in 2011, and further clarify the scope of applicability of certain aspects of the standards to the OF as opposed to simply having the OF rely on the phrase "as applicable" or similar wording that may give rise to significant uncertainty for compliance purposes. We believe such clarification would be consistent with the FHFA's approach in not applying many of the ten standards to the OF.

In addition, the Proposal does not include a proposed compliance date as related to the OF. Since the standards impose new requirements that were not previously applicable to the OF, we request that the FHFA establish in the final rule an implementation timeframe (e.g., six months after the promulgation of the final rule) for purposes of the OF's compliance with the final rule and the final standards, rather than suggesting that such compliance is required immediately upon rule effectiveness. We believe that including an implementation timeframe for the OF is appropriate given the new requirements and responsibilities imposed on the board of directors and management of the OF and the potentially significant amount of time needed to perform a gap analysis under the final rule and the final standards and to help ensure that the relevant standards are assimilated into processes, procedures and systems at the OF in order to determine, measure and report on compliance.

Potential Overlaps or Conflicts with Existing Regulations or Supervisory Guidance; the Role of Supervisory Guidance

As evidenced in the comment letter submitted on behalf of the FHLBanks and the OF in response to the FHFA's recent Notice of Regulatory Review, we are strongly supportive of the FHFA's efforts to conduct a review of its existing regulations, with a view to streamlining the agency's regulatory program and making the program more effective or less burdensome in achieving its objectives. In that regard, we note that there are potential overlaps or conflicts between the standards in the appendix to the Rule and existing regulations or supervisory guidance. Although the statement in the Rule about resolving conflicts between a standard established as a guideline and any FHFA regulation is helpful, we believe allowing any duplication or conflict to exist in the first place would not be consistent with the objective of the FHFA's regulatory review and could result in unnecessary regulatory burdens on the regulated entities and the OF or uncertainties in regulatory compliance.

For example, Standard 2 — Independence and Adequacy of Internal Audit Systems overlaps with existing regulations governing internal audit[6] and Advisory Bulletin 2016-05 on Internal Audit Governance and Function, which already sets forth detailed requirements or supervisory guidance on the internal audit function. Certain provisions of Standard 10 — Maintenance of Adequate Records also duplicate, and potentially conflict with or go beyond, the provisions of 12 C.F.R. Part 1235 on record retention. In addition, the standards require the board of directors of each regulated entity and of the OF to be "responsible for adopting business strategies and policies that are appropriate"

[6] See, e.g., 12 C.F.R. §§ 1239.32(d) and (e) for the FHLBanks and 12 C.F.R. § 1273.9(b)(5) for the OF.

for the particular subject matter addressed by each applicable standard and to "review and approve all major strategies and policies at least annually", while under 12 C.F.R. § 1239.14 the board of directors is only required to re-adopt a strategic business plan "at least every three years".

To help streamline the FHFA's regulatory program and facilitate compliance, we recommend the standards be revised to delete provisions that duplicate or conflict with existing regulations or supervisory guidance or at least provide cross-references to the relevant regulations or supervisory guidance that would satisfy the applicable requirements under the standards.

Furthermore, under the standards, each regulated entity and the OF "should comply with all applicable laws, regulations, and supervisory guidance (e.g., advisory bulletins)" governing the relevant subject matters. We appreciate the FHFA's intention under the Proposal to provide public notice of, and seek public comment on, any standard it plans to establish as a guidance (or on any material modification to any such standard), but supervisory guidance, such as advisory bulletins, generally sets forth the FHFA's supervisory expectations and does not itself go through the same "notice and comment" regulatory process established under the Administrative Procedures Act. We request that the FHFA clarify the role of supervisory guidance, and the process for establishing relevant supervisory guidance, in this context (e.g., whether existing or new advisory bulletins would, in effect, be used to establish additional or new standards without notice and comment). As indicated in the comment letter submitted on behalf of the FHLBanks and the OF in response to the FHFA's recent Notice of Regulatory Review, we believe that the "notice and comment" regulatory process established under the Administrative Procedures Act helps to create and sustain a system of rulemaking that is ultimately beneficial for the FHLBank System and its dual mission providing liquidity to members and supporting housing and community development.

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We appreciate your consideration of these comments.

Sincerely,

Ryan Donovan
President and Chief Executive Officer
Council of Federal Home Loan Banks