



FEDERAL HOME LOAN BANK OF INDIANAPOLIS

Building Partnerships. Serving Communities.

March 23, 2012

*via Federal eRulemaking Portal and
electronic mail to:
RegComments@fhfa.gov*

Alfred M. Pollard, General Counsel
Attention: Comments/RIN 2590-AA53
Federal Housing Finance Agency
Eighth Floor
400 Seventh Street SW
Washington, DC 20024

**Re: Comments on ANPR regarding Mortgage Assets Affected by PACE Programs
RIN 2590-AA53**

Dear Mr. Pollard:

The Federal Home Loan Bank of Indianapolis (the "Bank") appreciates this opportunity to comment on the Federal Housing Finance Agency ("FHFA") advance notice of proposed rulemaking on mortgage assets affected by PACE programs ("ANPR"), which would apply to Fannie Mae, Freddie Mac, and the Federal Home Loan Banks ("FHLBanks" and, together with Fannie Mae and Freddie Mac, the "Regulated Entities"). The Housing and Economic Recovery Act of 2008 ("HERA") established FHFA as the single regulator of the Regulated Entities to ensure HERA, "the authorizing statutes, and any other applicable law are carried out."

The Bank supports and urges the Finance Agency to issue guidance to the Regulated Entities concerning mortgages that are or could be affected by PACE programs, including implementing certain conditions and restrictions related to the Regulated Entities' dealings in mortgages on properties participating in PACE programs.

I. Background

Federal Home Loan Banks as Secured Lenders

Pursuant to the authority of Section 10 of the Federal Home Loan Bank Act (the "Bank Act") (12 U.S.C. § 1430), the FHLBanks make secured advances, along with other credit products, to their member financial institutions to assist those institutions with funding their residential mortgage lending activities. All credit products extended to a member institution must be fully collateralized by the member's pledge of eligible assets. Each borrowing member and its affiliates that hold collateral are required to grant the Bank a security interest in such collateral. The member must represent and

warrant to the Bank that any first mortgage it pledges to the Bank as collateral is not junior to any other loan on the property. Generally, all security interests held by the Bank are afforded a priority by the Competitive Equality Banking Act of 1987 (commonly known as the "CEBA lien") over the claims of any party, including any receiver, conservator, trustee, or similar party having rights as a lien creditor, except for claims held by bona fide purchasers for value or by parties that are secured by prior perfected security interests, provided that such claims would otherwise be entitled to priority under applicable law.

In addition, the Bank also purchases residential mortgages from our members through our Mortgage Purchase Program ("MPP"), subject to certain rigorous credit standards. Only first mortgages are purchased through this program. Finally, the Bank also maintains a portfolio of investments, including mortgage-backed securities ("MBS") to provide liquidity, utilize balance sheet capacity and enhance our earnings. As of December 31, 2011, the Bank held \$18.5 billion in advances, \$5.9 billion in MPP loans, and \$7.3 billion in MBS.

II. Effect of PACE Programs on the Bank and the FHLBank System

Although the Bank currently does not have PACE program legislation for first mortgage home loans (for single-family residences) in place within its district (Indiana and Michigan), the Bank is concerned about the legal structure often found in these programs. As a secured creditor, the PACE program allows PACE loans to have priority over other, preexisting mortgages. While PACE energy loans and other property rehabilitation loans may have merit to assist the property, as a public policy matter, the structure of the programs are contrary to traditional first mortgage lending. The automatic priority lien status typically granted to PACE lending undermines the Bank's pre-established lien priority and disrupts well-established first mortgage home lending. The risk of this alteration of lien priority after the fact could have an adverse impact on the valuation of the Bank's collateral in jurisdictions with PACE programs, forcing the Bank to apply loan market value adjustments, require higher loan collateral discounts, or implement greater overcollateralization requirements, along with possibly a more conservative maximum LTV/CLTV requirement for pledged loans in those jurisdictions. Because there is no way to determine what properties are encumbered by PACE loans, these adjustments could negatively impact loan collateral within a PACE program's jurisdiction. In turn, these higher borrowing costs at the FHLBank member level could ultimately result in an overall increase in the cost of home mortgage finance.

III. FHFA Authority to Address Safety Soundness Concerns related to the FHLBanks and Regulated Entities

Our experience as a collateralized home mortgage lender to our member financial institutions confirms and supports the FHFA's view that PACE programs present significant safety and soundness concerns, particularly as it relates to jurisdictions that have established first priority positions for such loans. As regulator of the FHLBanks, the FHFA has the authority to address such concerns. Per Section 8 of the Bank Act (12 U.S.C. § 1428), if the FHFA determines "*that under the laws of any*

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such State or the regulations or procedure thereunder there would be inadequate protection to a Federal Home Loan Bank in making or collecting advances...the Director may withhold or limit the operation of any Federal Home Loan Bank in such State until satisfactory conditions of law, regulation, or procedure shall be established.” In addition, the Director is authorized “*to exercise such incidental powers as may be necessary or appropriate to fulfill the duties and responsibilities of the Director in the supervision and regulation*” of the Regulated Entities.

Therefore, the FHFA is authorized to address the Regulated Entities’ possible exposure to PACE programs that under certain structures could be construed to erode the legal and equitable bases of traditional first home mortgage lending. This authority extends to implementing certain conditions and restrictions related to properties that participate in PACE programs. Such conditions and restrictions may be appropriate, consistent with the Act and applicable regulations, to support the FHLBanks’ position under otherwise well-established federal and state Uniform Commercial Code secured lending practices. To the extent such conditions and restrictions are considered and developed, we urge the FHFA and the PACE program state and local policymakers to avoid unintended consequences to the FHLBanks’ member institutions, such as decreased borrowing capacity resulting from the associated changes to the members’ collateral valuation, especially since many institutions rely on the FHLBanks to meet their liquidity needs.

We thank you for this opportunity and for your consideration of our comments on this ANPR. If you have any questions or need clarification with respect to these comments, please contact the undersigned.

Sincerely,

FEDERAL HOME LOAN BANK OF INDIANAPOLIS



Daniel A. Lane
General Counsel