

October 15, 2010

Alfred M. Pollard, General Counsel
Federal Housing Finance Agency, Fourth Floor
1700 G Street, NW
Washington, D.C. 20552

Re: Comments on Private Transfer Fee Covenants Proposed Guidance; No. 2010-N-11

Dear Mr. Pollard:

The Federal Home Loan Bank of Indianapolis (“Bank”) appreciates the opportunity to comment on the Federal Housing Finance Agency (“Finance Agency”) notice of proposed guidance on Private Transfer Fee Covenants (“Proposed Guidance”). The Bank supports the Finance Agency’s intent and goals as identified in the Proposed Guidance but the Supplementary Information to the Proposed Guidance differs from the text of the Proposed Guidance in one subtle, but important, respect. The Bank respectfully asks the Finance Agency to amend the text of the Proposed Guidance to mirror the Finance Agency’s intent as expressed in the Supplementary Information.

The Finance Agency’s Proposed Guidance notes that the “draft Guidance is based on the view that investments in mortgages on properties with private transfer fee covenants *and securities designed to generate income from the fees* are not acceptable for the regulated entities.” [emphasis added] 75 F.R. 49932 (August 16, 2010). In describing the Proposed Guidance, the Finance Agency states the Proposed Guidance directs the regulated entities not to purchase or invest in “*securities backed by private transfer fee revenue.*” [emphasis added] *Id.* at 49933. However, the text of the Proposed Guidance itself not only prohibits the purchase of, and investment in, securities backed by private transfer fee revenue, but expands the prohibition to *all securities* backed by a mortgage encumbered by a private transfer fee covenant.

The text of the Proposed Guidance states that Fannie Mae and Freddie Mac “should not purchase or invest in any mortgages encumbered by private transfer fee covenants *or securities backed by such mortgages.*” [emphasis added] *Id.* at 49934. The provision is

expanded to Federal Home Loan Banks (“FHLBanks”) by stating “The Banks should not purchase or invest in such mortgages or securities or hold them as collateral for advances.” *Id.* The text of the Proposed Guidance prohibits the purchase or investment in securities backed by “such mortgages,” presumably referring to the immediately preceding phrase which prohibits the purchase or investment in “any mortgages encumbered by private transfer fee covenants.” Thus, the text of the Proposed Guidance greatly expands the coverage of the Proposed Guidance as expressed by the Finance Agency in the Supplementary Information and is unnecessary to achieve the Finance Agency’s goals.

The text of the Proposed Guidance would require the FHLBanks to examine the mortgages backing every security, prior to purchasing or investing in that security or accepting such security as collateral, to determine whether any of the mortgages backing that security are encumbered by a private transfer fee covenant. In the event the FHLBank discovered a private transfer fee covenant on *one* mortgage backing the security, the Proposed Guidance would prohibit the FHLBank from purchasing or investing in that security or accepting that security as collateral. The Finance Agency recognizes that private transfer fee covenants “often are not disclosed by sellers and are difficult to discover through customary title searches.” *Id.* at 49933. The difficulty in discovering private transfer fee covenants is exacerbated in the purchase of or investment in securities or acceptance of such securities as collateral, which may require the review of hundreds or thousands of mortgages to ensure they are not encumbered by private transfer fee covenants.

The Bank supports the Finance Agency’s prohibition on purchasing or investing in securities *designed to generate income* from private transfer fees as expressed in the Supplementary Information, and the prohibition of the acceptance of such securities as collateral. However, the Bank has significant concerns with the difficulty of determining whether a security is backed by a mortgage that may be subject to a private transfer fee covenant and does not believe that such a prohibition is necessary to achieve the Finance Agency’s objectives. The Bank does not have access to the underlying mortgage loan files and therefore cannot determine whether the security is subject to a covenant. This may create the unintended consequence of preventing the Bank from accepting any security backed by residential mortgages as collateral.

Condominium and PUD home loans are actively purchased through the Mortgage Purchase Program (“MPP”) of the Bank and often are subject to private transfer fee covenants (PTFC). The PTFC normally benefits the homeowners as they are used to fund the maintenance and repairs of the common areas of the homeowner association and the costs of handling a transfer of ownership. Typically, these fees are very nominal and not a significant cost to the homeowner. However, actually being able to detect the presence of a in the mortgage documents in advance will be difficult and near impossible to determine as there does not appear to be a uniform market convention on how these fees are disclosed and documented. This would have a negative effect on supporting the housing recovery over very small fees. We agree that excessive fees paid to developers or investors’ providing no benefit to homeowners should be

prohibited. Other than formally prohibiting the sale of such loans and documenting this in the MPP Program Servicer Guide, the prohibition on purchasing affected loans, expanding existing representations and warranties provided by participating financial institutions, and instructing the quality control service provider to look for the presence of PTFC during their QC process, the FHLBI has limited ability to detect such loans, whether purchased through MPP or pledged as collateral.

With respect to accepting loans with PTFCs as collateral, the Bank believes that the risk of loss from such collateral can be managed by applying a “hair cut” or estimated market value attributable to such loans. This would avoid penalizing members that made loans in good faith to borrowers who themselves can be considered victims of private transfer fee covenants. The Bank believes that adjusting the lending value of such loans is the best way to discourage the proliferation of private transfer fee covenants without doing further harm to homeowners who may otherwise find themselves owning un-financeable real estate. Even if the Finance Agency determines that such loans made after the date that final guidance is issued may not be accepted as collateral, the Bank believes that members that acquired loans with PTFCs prior to final guidance should be allowed to pledge them as collateral subject to an appropriate diminution in lending value.

On behalf of the Federal Home Loan Bank of Indianapolis, we thank the Finance Agency for its consideration of these comments.

Sincerely,

Gregory L. Teare
SVP, Chief Banking Officer