



VIA EMAIL TO REGCOMMENTS@FHFA.GOV

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

Re: Guidance on Private Transfer Fee Covenants (No. 2010-N-11)

Dear Mr. Pollard:

The Federal Home Loan Bank of Des Moines (“Bank”) appreciates this opportunity to comment on the Federal Housing Finance Agency (“FHFA”) proposed “Guidance on Private Transfer Fee Covenants” (“Guidance”). The FHFA has indicated that the entities it regulates should not deal in mortgages on properties encumbered by Private Transfer Fee Covenants (“PTFCs”) because, in its view, such covenants appear adverse to liquidity, affordability and stability in the housing finance market and to financially safe and sound investments. The Guidance would extend to mortgages and securities held by the Federal Home Loan Banks (“FHLBanks”) as investments or as collateral for advances. This letter sets forth the comments of the Bank with respect to the Guidance. We thank you for the opportunity to be heard on this matter.

I. Purpose of Covenants

The Bank shares the FHFA’s concern over the negative impact that PTFCs currently being adopted by certain housing developers will have on the marketability and valuation of affected homes and on the financial health of homeowners. We also share the belief that such fees are simply in place to provide a continuous stream of income for developers and/or other investors through securitized investment vehicles. Therefore, we agree that FHLBanks should not lend against mortgage collateral or purchase mortgage loans that are subject to this relatively new application of transfer fee covenants by housing developers.

However, the Bank respectfully requests that the FHFA consider distinguishing between PTFCs such as those described in the foregoing paragraph which accrue value to unrelated parties, from those PTFCs which render a benefit to the affected property’s homeowners association, such as PTFCs that are made part of condominium and PUD projects. These PTFCs that serve to benefit homeowners and their community should not be considered as detrimental to the housing market.



II. Acquired Member Assets Impact

While condominium and PUD home loans are actively purchased through the MPF program, the use of PTFCs does not appear significant in this market. The fees in this case benefit the homeowners as they are used to fund the maintenance and repairs of the common areas of the homeowner association. However, actually being able to detect the presence of PTFCs in the mortgage documents will be difficult as there is no uniform market convention on how these fees are disclosed and documented. Other than formally prohibiting the sale of such loans and documenting this in the MPF 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 PTFCs during their QC process, the FHLBanks are limited in their ability to detect such loans. The FHLBanks could benefit from an industry standardization initiative in the disclosure of PTFCs within the closing documents.

III. Investments Impact

The Guidance notes that it “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.” 75 F.R. 49932 (August 16, 2010) [Emphasis added]. In describing the Guidance, the FHFA states that it directs the regulated entities not to purchase or invest in “*securities backed by private transfer fee revenue.*” *Id.* at 49933 [Emphasis added]. However, the text of the 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 PTFC.

The text of the 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.*” *Id.* at 49934 [Emphasis added]. The provision is expanded to Banks by stating “[t]he Banks should not purchase or invest in such mortgages or securities or hold them as collateral for advances.” *Id.* The text of the 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 Guidance appears to unnecessarily expand its coverage as expressed by the FHFA in the Supplementary Information and is unnecessary to achieve the FHFA’s goals.

The Bank supports prohibitions on purchasing or investing in securities *designed to generate income* from private transfer fees used to benefit developers or as expressed in the Supplementary Information, and further supports prohibitions on accepting 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 PTFC and does not believe that such a prohibition is necessary to achieve the FHFA’s objectives.

IV. Monitoring

We respectfully request that the FHFA does not require “testing” of securities (purchased as investments or pledged as collateral) that were issued prior to the effective date of the final guidance. As a general



rule, testing underlying mortgages of mortgage-backed securities present significant challenges, and if ultimately required should be limited to securities issued after the effective date of the final guidance.

The text of the Guidance would appear to require FHLBanks to examine the mortgages backing every security, prior to purchasing or accepting as collateral that security, to determine whether any of the underlying mortgages are encumbered by a PTFC. In the event the Bank discovered a PTFC on *one* mortgage backing the security, the Guidance would prohibit the Bank from purchasing that security or accepting it as collateral. If this is the intent of the Guidance, we believe that this degree of testing will be an impossible standard to accurately verify, and a difficult standard to uphold. In fact, the FHFA recognizes that PTFCs “often are not disclosed by sellers and are difficult to discover through customary title searches.” *Id.* at 49933. The difficulty in discovering PTFCs is exacerbated when applied to securities, which may require the review of hundreds or thousands of underlying mortgages to ensure none are encumbered by PTFCs. Monitoring for the presence of PTFCs will be no less challenging for mortgage loans pledged as collateral because, as the FHFA has acknowledged, PTFCs “are difficult to discover through customary title searches.”

We believe consideration should be given to have condominiums and PUDs excluded from the final guidance, with focus directed on those PTFCs imposed by housing developers. For the situations warranted, we do believe that realistic and reasonable efforts can ensure adherence to the spirit and primary objective of the Guidance. This might include informing members of the prohibition on pledging such loans as collateral, requiring enhanced member certifications that such loans are not pledged, and conducting reasonable assessments of loans reviewed during on-site visits. Expectations to pursue compliance verification much beyond these standard practices will not be practical or meaningful.

V. Conclusion

The FHLBanks’ mission is to provide a reliable source of liquidity to meet the housing finance and credit needs of their communities. Due to the potential for excessive verification and monitoring burdens, the Guidance as written may impair the Bank’s ability to efficiently meet this mission, and may prevent its members from obtaining credit from the Bank. As previously noted, not all PTFCs are created equal so a distinction must be made between those “good” PTFCs that provide value in which they benefit the affected property’s homeowners association and community as opposed to those “bad” PTFCs which accrue value only to unrelated parties. The FHFA should also carefully consider the extent to which FHLBanks will be required to verify that mortgages underlying securities comply with the final guidance to be issued. The monitoring requirements imposed on the Banks should result in the FHLBanks exercising reasonable efforts to ensure adherence to the spirit of the Guidance.

Should the FHFA decide to issue final guidance on this subject, the Bank respectfully requests that the final guidance:

- (i) Excludes condominiums and PUDs from the purview of the guidance;
- (ii) Only prohibits regulated entities from investing in securities backed solely by private transfer fee revenue;



- (iii) Establishes prudent and reasonable compliance requirements prospectively to mortgages originated and securities issued after the final guidance issue date; and
- (iv) Allows for prudent and reasonable monitoring processes for the review of mortgages in determining whether PTFCs exist.

On behalf of the Federal Home Loan Bank of Des Moines, we thank the FHFA for its consideration of these comments.

Sincerely,

A handwritten signature in black ink, appearing to read "Aaron B. Lee". The signature is fluid and cursive.

Aaron B. Lee
Vice President, General Counsel
and Corporate Secretary