

July 2, 2010

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

Alfred M. Pollard, General Counsel  
Attention: Comments/RIN 2590-AA32  
Federal Housing Finance Agency  
Fourth Floor  
1700 G Street, NW  
Washington, DC 20552

**Re: Comments on Notice of Proposed Rulemaking for Federal Home Loan Bank  
Investments (RIN 2590-AA32)**

Dear Mr. Pollard:

The Federal Home Loan Bank of Seattle appreciates the opportunity to comment on the above-referenced notice of proposed rulemaking (the “Proposed Rule”) issued by the Federal Housing Finance Agency (“FHFA”). The Proposed Rule would reorganize and readopt existing investment regulations for the Federal Home Loan Banks (“FHLBanks”) that were previously adopted by the Federal Housing Finance Board (“FHFB”), and incorporate into the new regulations limits on the FHLBanks’ investments in mortgage-backed securities (“MBS”) and certain asset-backed securities currently set forth in the FHFB’s Financial Management Policy (“FMP”). The FHFA also is seeking comments on four questions related to whether it should adopt additional restrictions, or lower the overall limit, on the FHLBanks’ investment in MBS generally, and private-label MBS (“PLMBS”) in particular.

As a policy matter, we believe that there is a compelling need to restart the private secondary market for residential mortgage loans, and that the FHLBanks’ investment authority may play a limited, but important, role in achieving that goal. Our current system of residential housing finance cannot continue on a sustainable basis if it continues to consist almost exclusively of government-guaranteed loans. While in retrospect there were many flaws in the PLMBS market in the years preceding the current financial crisis, those flaws are being corrected now through legislative and regulatory initiatives. The future private secondary mortgage market should emerge stronger and more resilient as a result and support more prudently originated loans as a consequence. The FHLBanks should be allowed to assist in facilitating this transition through their limited investment authority.

Specifically, we offer the following comments in response to the four questions posed by the Proposed Rule:

**I. What other measures, beyond the 300 percent of capital rule already contained in the FMP, might offer a prudent limit on the FHLBanks' MBS holdings that also would mitigate potential future losses on those holdings?**

We support incorporation into the final rule of the current standard in the FMP that limits an FHLBank's investments in MBS to 300 percent of its total capital. This limitation ensures that the FHLBanks have a prudent outlet for investing their capital and excess liquidity, but remain focused on their primary mission of providing financial products and services to their members. These investments can represent an important source of income that enables the FHLBanks to meet their REFCORP and affordable housing obligations, cover operating expenses, build retained earnings, provide their members with a reasonable rate of return on their capital stock investments, and support advance activity.

We do request that the 300 percent of total capital calculation be clarified and specified in terms of changes to US GAAP. Specifically, the numerator should include amortized historical cost for held-to-maturity and available-for-sale securities, and fair value for trading securities. The denominator should include total capital as defined by FHFA regulation §1229.1<sup>1</sup>.

**II. Should there be a separate limit, or additional restrictions, on the purchase of PLMBS by the FHLBanks? If so, what would these limits or restrictions be?**

In view of the extensive legislative, regulatory and market changes that are underway with respect to any future PLMBS, we believe that establishing specific limits or restrictions with respect to such purchases by the FHLBanks at this time is premature. We are supportive of the market enhancements currently under consideration by the Congress, SEC and certain federal banking regulators, including:

- Providing clear regulatory definitions and underwriting standards for mortgage loans generally, and PLMBS backed by such loans;
- Requiring additional due diligence by sponsors, servicers, trustees and other participants in PLMBS transactions;
- Allowing significantly more time for investors to conduct a careful analysis before purchasing PLMBS;
- Increasing transparency with respect to PLMBS by requiring that loan level data be provided to potential investors in a format and manner that is easily accessible by them; and
- Requiring meaningful, detailed ongoing disclosure (including loan level data) concerning outstanding PLMBS.

After these new legislative and regulatory requirements have been finalized, the FHLBanks, like other investors, will have a clearer understanding of the structure of this new market. At that point, the FHLBanks will be able to establish prudent risk parameters, limitations and procedures with respect to any

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<sup>1</sup> *Total capital* means the sum of the Bank's permanent capital, the amount paid-in for its Class A stock, the amount of any general allowances for losses, and the amount of any other instruments indentified in a Bank's capital plan that the Director has determined to be available to absorb losses incurred by such Bank. For a Bank that has issued neither Class A nor Class B stock, the Bank's total capital shall be the measure of capital used to determine compliance with its minimum capital requirement.

future PLMBS purchases through investment policies approved by their boards of directors. These risk parameters and policy limits, like other aspects of an FHLBank's credit and investment policies, would be subject to review by the FHFA as part of the supervisory process, and perhaps the subject of future guidance with respect to such purchases.

**III. Whether to restrict PLMBS purchases by the FHLBanks based on the characteristics of the underlying collateral?**

Since 2007, the FHFA and the FHFBS have issued guidance to the FHLBanks establishing supervisory expectations with respect to the FHLBanks' purchase of PLMBS, specifically concerning the characteristics of the underlying mortgage loans supporting PLMBS. In particular, such investments should comply with all aspects of the federal banking agencies' *Interagency Guidance on Nontraditional Mortgage Product Risks*<sup>2</sup> and *Statement on Subprime Mortgage Lending*<sup>3</sup>. Going forward, we would expect that the mortgage loans supporting any future PLMBS purchased by the FHLBanks would comply with the highest standards of prudent and sustainable lending, including any new requirements applicable through federal legislative and regulatory initiatives as described above. However, as noted above, these new standards currently are being formulated, and we believe that it would be premature for the FHFA to impose any specific limitations on the FHLBanks in this regard until these standards have been finalized. In the interim, the previous guidance issued by the FHFA and its predecessor agency has been an effective mechanism for establishing parameters for such purchases by the FHLBanks.

**IV. Whether to reintroduce a limitation on the FHLBanks' purchase of MBS to require that all such purchases must be rated in the highest investment grade category?**

We would support reintroduction of the requirement that all PLMBS purchased by an FHLBank must have the highest investment grade rating at the time of purchase as a prudent limitation on the FHLBanks' investment authority. As a practical matter, the FHLBanks historically have operated in compliance with this standard. Ratings can change, however, and an FHLBank should not be required automatically to divest a PLMBS if it is downgraded later.

Thank you for your consideration of these comments.

Sincerely,



Richard M. Riccobono  
President and Chief Executive Officer

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<sup>2</sup> Issued on October 4, 2006 (71 FR 58609)

<sup>3</sup> Issued on July 10, 2007 (72 FR 27569)