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March 6, 2000

Ms. Elaine L. Baker
Secretary to the Board
Federal Housing Finance Board
1777 F Street N.W.
Washington, DC 20006

Re: Reorganization of the Office of Finance; Authority to Issue Consolidated Obligations on which the Federal Home Loan Banks are Jointly and Severally Liable.¹

Dear Ms. Baker:

The Bond Market Association (the "Association") is pleased to comment on the above-referenced rule proposal. Our membership includes all major dealers and underwriters of debt securities issued by government-sponsored enterprises ("GSEs") and federal agencies.² As such, we take a keen interest in matters affecting the market for consolidated obligations of the Federal Home Loan Bank ("FHLBank" or "Bank") System.

As stated in an accompanying summary, the proposed rule is designed to help the FHLBanks carry out joint activities in an efficient manner that aids them in achieving their mission. For more than 67 years, that mission has been to promote residential mortgage lending and related community investment by providing low-cost capital to member financial institutions, who in turn lend at highly competitive rates to borrowers in the low- to moderate-income housing market. The FHLBank System has performed remarkably well, providing more than \$700 million in interest rate subsidies for rental housing and \$18 billion in mortgage financing in the past decade alone.

The cornerstone of the FHLBanks' financial strategy is the issuance of consolidated obligations ("COs"). Currently, the Federal Housing Finance Board (the "Board"), through the System's Office of Finance ("OF"), issues COs on behalf of the Banks. Since 1934, the Board or its predecessor agencies have issued securities at the lowest possible cost, allowing the Banks to pass that low-cost capital along to the housing market. Today, the CO program includes a wide range of securities, such as discount notes, bonds with fixed rates and fixed maturities, callable bonds, puttable bonds, variable rate bonds, and global bonds. As of September 30, 1999, there were more than \$477 billion in COs outstanding.

Investors throughout the world hold FHLBank COs with confidence in the credit quality and liquidity of the securities. National rating agencies have conferred their highest investment-grade ratings on COs due to the strength of the FHLBank System's financial management, the soundness of the System's businesses, the credit structure of the obligations, the System's GSE status, and for numerous other important reasons. Indeed,

the proposed rule observes that "no Bank has ever been delinquent or defaulted on a principal or interest payment on any CO issued by the Finance Board or its predecessor agencies.³" Dealers maintain highly active secondary markets for COs, ensuring that ready buyers and sellers are available to meet investors' needs. With a flawless credit history, sound management, and the dedication of the dealer community to support it, the FHLBank System offers investors a secure and well-tested place to deploy capital.

A pillar of the COs' credit standing is the mutuality of their financial backing. As pointed out in the proposed rule, "the joint-and-several liability of the banks on the COs is an integral part of investor confidence in Bank System debt."⁴ Under federal statute and Board rules, "each and every Bank, individually and collectively, has an obligation to make full and timely payment of all principal and interest on consolidated bonds when due."⁵ With more than six decades of experience assessing the credit, observing the financial management, underwriting the debt, and distributing the securities of the FHLBanks, the members of the Association are pleased that the proposed rule "would not have a substantive effect on the debt issuance process or on the joint and several obligation of the Banks on the COs."⁶

Board materials explaining the proposed rule observe that "the changes would be largely technical."⁷ While the proposed rule "would make the Banks, rather than the Finance Board, the issuers of COs . . .," the System's Office of Finance would remain the fiscal agent for all issuance and the Banks would continue to be jointly and severally liable for payments on all securities. As is now the case, no FHLBank would be permitted under the proposed rule to issue individual debt securities. The only debt obligations authorized for issuance by the FHLBanks would be consolidated obligations, defined as "any bond, debenture, or note issued jointly by the Banks . . . or any bond or note issued by the Finance Board on behalf of all Banks . . . on which the Banks are by statute or regulation jointly and severally liable."⁸

As intermediaries in the global financial markets, members of the Association are in regular contact with investors of every variety throughout the world. Based on this contact, Association members believe that maintaining continuity in the perceptions of market participants regarding the economic and credit characteristics of FHLBank debt is of paramount importance. We therefore applaud the Board for crafting a proposed rule that is designed to achieve such continuity by preserving the collective issuance and joint and several liability of all FHLBank debt. However, we urge the Board in publishing the final rule to ensure that nothing contained in the overview, summary, or other accompanying explanatory materials creates any confusion regarding the status of COs as the joint and several obligations of all 12 Banks.

Again, the Association applauds the Federal Housing Finance Board for issuing a rule proposal designed to aid the Federal Home Loan Bank System in continuing to achieve its mission in a rapidly evolving global economy. Our members look forward to working with the Board, the System, and the Office of Finance to perpetuate the high standards that market participants have come to expect from the Federal Home Loan Banks. If we

may be of any assistance, please do not hesitate to contact me at 510.628.8440, or Andy Waskow, Assistant General Counsel on the Association staff, at 212.440.9448.

Sincerely,

/s/Edward J. Doherty
Chairman
Federal Agency Committee
The Bond Market Association

cc: Mr. Bruce A. Morrison, Chairman, Federal Housing Finance Board
Mr. John Darr, Managing Director, Office of Finance, Federal Home Loan Bank System
Federal Agency Committee, The Bond Market Association
Primary Dealers Executive Committee, The Bond Market Association
Senior Policy Staff, The Bond Market Association

FOOTNOTES

1 65 Fed. Reg. 324 (2000) (the "Proposed Rule").

2 This comment letter was prepared in close consultation with the Association's Federal Agency Committee. The Association's membership also includes all major dealers and underwriters of other government securities, corporate bonds, municipal bonds, mortgage-and asset backed securities, money market instruments and funding instruments. Complete information about the Association can be found on our website at www.bondmarkets.com.

3 Id. at 325, n. 6.

4 Id.

5 64 Fed. Reg. 55,125 (1999) (to be codified at 12 C.F.R. Chap. IX, Sec. 910.7).

6 Proposed Rule at 324 (emphasis added).

7 See "Questions and Answers: Office of Finance Restructuring," at www.fhfb.gov/prgmoffices/opa/press/RestructQ&A's.htm (the "Q&A").

8 Proposed Rule at 333 (emphasis added).