

January 15, 2002

The Honorable Armando Falcon, Jr.  
Director  
Office of Federal Housing Enterprise Oversight  
1700 G Street, NW, 4<sup>th</sup> Floor  
Washington, DC 20552

Re: Risk-Based Capital Rules for Fannie Mae and Freddie Mac

Dear Mr. Falcon:

As I stated in my letter to you dated October 2, 2001, the California Housing Finance Agency (CHFA) is one of many public agencies throughout the United States that issues municipal bonds to finance low-interest-rate mortgage loans to first-time homebuyers and to developers of affordable rental housing. CHFA issues more such bonds and makes a greater dollar amount of loans each year than any other such agency, state or local, in the nation. As an example, CHFA has purchased \$1 billion of home loans each of the last two fiscal years. In spite of our efforts, California ranks 49<sup>th</sup> among the fifty states in the percentage of households who own rather than rent.

We at CHFA continue to be concerned that the OFHEO's newly-proposed risk-based capital regulations for Government Sponsored Enterprises (GSEs), even as amended, will impede the capacity of Fannie Mae and Freddie Mac to support our affordable housing programs and those of our sister state and local housing agencies.

As we understand, the revised rules would assess the GSEs an 8.75% capital "haircut" for investments in double-A-rated housing bonds and a 3.5% "haircut" for triple-A-rated bonds. While we recognize that these proposed capital requirements are reduced from those originally proposed, we believe these percentages are still excessive and fail to take into account the strong creditworthiness of mortgage revenue bond programs that achieve these high ratings. For example, the proposed rules do not apparently reflect the high percentage of government loans (FHA and VA) backing most double-A-rated bonds nor Ginnie Mae or Fannie Mae MBS guaranties or bond insurance backing many triple-A-rated housing bonds. In addition, the rules seem to ignore the overall creditworthiness and business-like management of state housing agencies, many of which have substantial equity that is either already pledged to the investors or, if not directly pledged at this time, could and would be used to prevent defaults.

Fannie Mae and Freddie Mac are two of the most important investors in state and local housing bonds, providing stability and liquidity to the relatively thin market for long-term housing bonds. Over the last 6 years the two GSEs have purchased \$880 million of CHFA housing bonds. Because most state and local housing agency bonds have double-A ratings, there is a well-founded concern that even the newly-proposed 8.75% capital "haircut" will make it infeasible for the GSEs to continue to make these investments. Without Fannie Mae and Freddie Mac in the market, it is likely the interest rates for new housing bonds will have to be as much as 0.25% higher in order to attract private investors for whom affordable housing is not a mission activity. This cost would have to be passed on to first-time homebuyers and owners of affordable rental housing.

Fannie Mae and Freddie Mac are also major participants in providing credit enhancement to state and local agency bonds that are issued to provide low-interest-rate financing for affordable rental housing. Last year Fannie Mae agreed to provide CHFA with a \$250 million commitment to provide credit enhancement (in the form of a liquidity guaranty) to CHFA for this same purpose. As a result, in 2001 we issued \$193 million of double-A-rated variable rate bonds under this agreement to provide low-interest-rate funding for 45 affordable housing projects that contain over 2500 units.

As we stated previously, in the coming years CHFA will need approximately \$500 million per year of such agreements for its financing programs and hopes that Fannie Mae and Freddie Mac can help meet this demand. We are concerned, however, that the new regulations may make this program so financially unattractive to the GSEs that they may not be able to partner with us except at a cost we would find prohibitive. If such were the case, CHFA would be forced to rely on the dwindling number of highly rated commercial banks that may be willing to offer this service.

In summary, we continue to be concerned that the OFHEO's new rules will result in Fannie Mae and Freddie Mac curtailing their investments in housing bonds and reducing their commitment to other important partnerships with state and local housing agencies. As we said previously, financing affordable housing, especially here in California, is very difficult. We implore you not to make the problem worse by making crucial public/private partnerships with the GSEs less attractive to them.

Thank you very much for considering these comments. Please call me at (916) 324-4638 if you have any questions.

Sincerely,

Theresa A. Parker  
Executive Director