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November 17, 2008

Ms. Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Ave., N.W.
Washington, D.C. 20551

RE: Docket No. R-1335
Notice of Proposed Rule Making - Minimum Capital Ratios; Capital Adequacy Guidelines; Capital Maintenance; Capital: Treatment of Certain Claims on, or Guaranteed by, the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac)

Dear Madam:

On behalf of Napa Community Bank, I am writing this comment in response to the publication of the federal banking agencies' proposed rule to allow banking organizations to assign a 10 percent risk weight to claims on, and portions of claims guaranteed by, Fannie Mae and Freddie Mac, while maintaining a 20 percent risk weighting for FHLBank debt obligations. Thank you for the opportunity to address this issue.

Our institution has significant concerns about the proposal. While a reduction in the capital requirement for holding obligations of Fannie Mae and Freddie Mac is welcome, we believe that the proposed rule's failure to also assign a 10 percent risk weighting to FHLBank debt obligations is unwarranted. This rule, if enacted in its current form, may have unintended adverse consequences for the FHLBanks, their member financial institutions, and the housing market in general, particularly during this time of economic stress.

Our primary concern is that the proposal as drafted will put the FHLBanks at a competitive disadvantage by increasing the cost to the FHLBanks of issuing their debt obligations, and that those increased costs will be passed on to member financial institutions in the form of higher advance rates. Different risk weighting treatment also means that investors will likely reduce purchases of FHLBank debt obligations in favor of Freddie and Fannie debt, putting pressure on the availability of advances at a time when members depend on the FHLBanks as an essential liquidity source. It is our understanding that investors are already demonstrating a preference for Fannie and Freddie obligations and that spreads between FHLBank senior debt and comparable bonds issued by Fannie Mae and Freddie Mac have widened as much as 20 to 36 basis points since these entities were placed into conservatorship. We believe the proposed regulation will only aggravate this situation.

Because this proposal will increase the cost of advances available from the FHLBanks, it is also likely to increase the cost of mortgages that are funded by such advances. My institution and others depend on access to low-cost liquidity from the FHLBanks to provide credit in our communities for all types of loans. In particular, we depend on liquidity from the FHLBanks to make loans that do not meet conforming loan underwriting standards. Because the private securitization market is presently not an option for such loans, raising the cost of FHLBank advances would have a detrimental effect on the mortgage market and housing market, in some of the most severely impacted regions of the country, furthering the downward economic spiral in these regions.

The proposal in its current form also suggests that the United States government does not support the FHLBanks and their mission to the same degree that it supports the mission of Fannie Mae and Freddie Mac. Such a perception is contrary to the actions taken to date by the government to support all the housing GSEs. First, Congress created the Federal Housing Finance Agency (FHFA) to ensure that all the housing GSEs are subject to the same degree of regulation and supervision for safety and soundness. Second, the U.S. Treasury is providing the same temporary backstop funding facility to all the housing GSEs through the GSE Credit Facility. Finally, the New York Fed is providing support for the FHLBanks, as well as Fannie Mae and Freddie Mac, by purchasing their discount notes in recent open market operations.

In announcing the conservatorship of Freddie and Fannie on September 7, Treasury Secretary Paulson said that the measures being taken, including establishment of the GSE Credit Facility to which the FHLBanks have access, were intended to put all the GSEs in a stronger position to fund their regular business activities in the capital markets. Giving Freddie and Fannie obligations more favorable capital treatment will undermine this announced goal by making it more difficult and more expensive for the FHLBanks to raise debt in the capital markets.

Finally, many members of the FHLBanks are also investors in FHLBank System debt. While the proposed lower risk weighting for Freddie and Fannie debt is welcome, it is unfair to members as investors in FHLBank System debt to require a higher risk weighting for comparable FHLBank debt instruments.

I strongly urge the OCC, the Board of Governors of the Federal Reserve System, the FDIC, and the OTS to treat the debt securities of all the housing GSEs as comparable with regard to risk-based capital rules. Equal treatment would reflect the parity that Congress intended and achieve the most favorable outcome for all stakeholders in the housing GSEs.

Sincerely,

Dennis Pedisich
President & CEO
Napa Community Bank