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<u>VIA E-MAIL</u> – Rule-Comments@SEC.gov

November 5, 2015

Secretary
Securities and Exchange Commission
100 F Street, NE,
Washington, D.C. 20549-1090

RE: File Number SR-FINRA-2015-036
Notice of Filing of a Proposed Rule Change to Amend FINRA Rule 4210 (Margin Requirements) to Establish Margin Requirements for the TBA Market

Dear Sir/Madam:

We are a small **<u>multifamily</u>** mortgagee approved by the U.S. Department of Housing and Urban Development (HUD) and the Federal Housing Administration (FHA). We are also a Government National Mortgage Association (GNMA) approved seller/servicer of multifamily mortgage backed securities (MBS). Our annual production volume results in about 5-7 loans annually. Dollar volume varies depending on the types of project we finance. Our loans typically finance substantial rehabilitation as well as refinancings on multifamily properties. Many of the projects we finance use FHA insured/GNMA enhanced first mortgages in conjunction with other public sources such as low income housing and historic tax credits, HOME, CDBG, and other public sources. Loan size on any given transaction can vary from $3m - $25m. Many of these projects serve low and moderate income tenants and also provide rental assistance through project based Section 8 contracts. I am profoundly concerned about the adverse consequences of this proposed rule on the availability of FHA insured/GNMA MBS loans for these types of projects and the impact on smaller lenders. Small lenders fulfill a critical role in this market. They often provide financing to smaller, affordable housing projects in secondary and tertiary markets. I fear this proposed rule will result in lending activity that becomes concentrated among the largest lenders and will reduce the availability of this source of capital in secondary and tertiary markets.

Over the past year, we have been made aware through the Mortgage Bankers Association of efforts to require such agency backed loans to become subject to margining in an effort to reduce risk in the financial markets and mitigate the likelihood of the Federal government from having to step in and bail out any banking institution in the future. This issue first surfaced with the U.S. Treasury's Treasury Management Practices Group (TMPG) which recommended two-way margining for GNMA and FNMA MBS loans. As I understand the proposed Rule, margining requirements would be exempt on such Covered Agency Transactions if the gross open position is $2.5m or less. Further, margining would not be required for any gross open position whose value was determined to be $250,000 or less. For those Covered Agency Transactions subject to this Rule, margining would be required based on a daily valuation of the gross open position from the time a trade agreement is entered into until the full delivery of the security is made. For example, assume an agreement was reached between a lender and a Broker/Dealer to securitize a $10m FHA insured loan through GNMA with a 3.00% rate. The value of this security changes roughly 1% for every 0.10% change in interest rates. If interest rates increase to 3.40% prior to delivery of the MBS, the value of that security has declined by 4%. If interest rates decrease to 2.60%, the value of that security has increased by 4%. Under the proposed rule, the lender would be responsible for posting margin if the value of the security declined by more than $250,000. In the example above, at a 2.60% rate, the lender would need to fund $150,000 margin ($10m x 0.4 = $400,000 - $250,000 = $150,000). TMPG and FINRA's thinking is that the lender (or borrower) poses counterparty risk to the broker/dealer since it would be inclined to break the agreement for a 3.00% rate and lock in at the lower 2.60% rate with another Broker/Dealer.

The Rule states several facts and concerns that are at odds with the GNMA multifamily MBS market and delivery process.

The Rule states that the agency and GSE MBS market is one of the largest fixed income markets with approximately $5 trillion of outstanding securities and $750 billion - $1.5 trillion in gross unsettled and un-margined transactions. Such a large open position, creates potential risk from counterparty exposure and that the sheer size of the un-margined open position can pose significant counterparty risk to individual market participants (the broker/dealer community). Risks arising from un-margined counterparty exposure are similar to the futures market where posting of initial margin is required for new positions and for open positions, maintenance, and mark to market also known as variation margin. Unsecured credit exposures that exist in the TBA market can lead to financial losses by dealers. Permitting counterparties to participate in the TBA market without posting margin can facilitate increased leverage by customers, thereby potentially posing a risk to the ealer extending credit and to the marketplace as a whole.

Allow me to explain why these concerns are not and should not be relevant to the newly issued GNMA MBS multifamily/healthcare market.

1) The market is substantially smaller than suggested by the figures above. In FY 2014, the volume of GNMA MBS that securitized multifamily loans was approximately $12B. The number of GNMA approved multifamily and healthcare issuers totals 53 firms. The average size HUD insured loan for an apartment acquisition/refinance loan was $9.7m and $14.8m for a new construction/substantial rehab loan.

2) Lenders/Issuers are rigorously vetted by HUD and GNMA on an ongoing basis. They are not some unregulated, fly-by-night outfit that speculates in the TBA market. Both HUD and GNMA review, approve, and monitor the performance of multifamily and healthcare lenders by requiring annual audited financial statements, randomly reviews transactions for compliance with the lender's quality control plans, and requires net worth and liquidity thresholds based on size of operations. The lender's warehouse lender and Broker/Dealers also require lenders to provide annual audited financials and may place limits on the types or size of loans they are willing to warehouse and securitize.

3) The GNMA MBS market for multifamily and healthcare loans is not the same as the single family MBS market. Single family lenders will enter an agreement with a Broker/Dealer to issue a GNMA pool based on their pipeline of prospective loans that are in various stages of processing. These single family pools are often for $250m or more. In contrast, the GNMA MBS market for multifamily and healthcare loans is based upon a single security for a specific project that has already been carefully underwritten by the lender, reviewed and approved by HUD for which a Firm Commitment has been issued, and preparation of draft loan closing documents.

4) There are ample safeguards in place for the multifamily and healthcare borrower and lender to fulfill their obligation to close on the loan and deliver the GNMA MBS. At the time of rate lock with the broker/dealer, the lender collects a good faith deposit in the amount of 0.50% of the loan amount. Rate lock agreements with the broker/dealer typically stipulate extension fees should the GNMA MBS not be

delivered within the timeframe agreed upon. Furthermore, the GNMA issuer can be held liable to the broker/dealer if there are liquidated damages in excess of the good faith deposit. At the time of rate lock, the Borrower has already expended significant funds to process the loan. These costs average $30,000 for an acquisition/refinance and $100,000 or more on construction and rehab loans. These sunk costs are for third party reports (environmental, engineering/plan review, appraisal, survey, application fees, etc . . . .). The only way a borrower will be reimbursed for these costs is if they proceed to loan closing. It is highly unlikely that a Borrower would go through the cumbersome and expensive process of obtaining a HUD insured loan, rate lock, pay the good faith deposit, and then not proceed to loan closing.

5) Potentially there are three different time periods between rate lock and full delivery of the GNMA security that could pose counterparty risk to the broker/dealer; 1) the time between rate lock and loan closing with HUD; 2) the time between loan closing and delivery of the security; and 3) in the case of a construction loan, failure to deliver GNMA Construction Loan Certificates or conversion of the CLC's to the full Permanent Loan Certificate. None of which is likely and certainly unlikely to create an elevated risk to the broker/dealer or banking sector.

Conceivably, the borrower or lender could be in such a financially weak condition that either is unable to close the loan after rate lock. As part of the underwriting process, the principals of the borrower entity will have undergone a complete and thorough financial review. HUD will not issue a Firm Commitment if either the Borrower or the property is financially troubled. If HUD does not issue a Firm Commitment, the lender would not seek to rate lock with a broker/dealer. If FINRA is concerned about a financially weakened lender rate locking and then being unable to close, the firm's financial audits would surely cause concerns by HUD and GNMA who would curtail or terminate a lender's operations if its' net worth and liquidity are below the established requirements.

Counterparty risk to the broker/dealer after the loan is closed and funded, but prior to securitization, is negated by the lender's warehouse funder who has the right to step in through a Power of Attorney and complete the GNMA issuance. This is the only way the warehouse funder will be reimbursed for the funds they disbursed. In the case of a construction loan that has achieved Initial Endorsement and initial delivery of the MBS, the HUD insured Note and all collateral mortgage documents have been assigned to GNMA. GNMA's master servicer, Walker & Dunlop, can step in and assign the project to another lender to complete the securitization process if the lender is unable to do so. If the financial condition of the principals of the borrower were to deteriorate such that they could no longer complete the construction process, the lender and HUD would attempt a workout by bringing in new principals or if that would be infeasible, the loan would go into default and HUD/GNMA would ensure that the broker/ealer received all principal disbursed as well as the timely payment of interest during the insurance claims process. Clearly, these are concerns and situations HUD and GNMA have thought through and they have established processes and procedures to complete the securitization process. See attached GNMA bond letter template issued at closings. Letter confirms that once the initial GNMA CLC is issued, any subsequently disbursed funds that are not securitized, will be treated as such. Thus, the MBS investor is protected.

6) Securitization of a multifamily or healthcare loan is not like the futures market where there is variation of the value of the position. Lender and broker/dealer enter into an agreement to deliver a single GNMA MBS pool at the agreed upon coupon. If the agreed upon coupon at the time of rate lock is 3.00%, then that is what the broker/dealer will receive upon delivery whether the then current market rate is 2.60% or 3.40%.

7) The proposed rule relies on data from two sources in an effort to evaluate the impact of the proposed rule. The data sets include TBA data in the TRACE database from March 1, 2012 through July

31, 2013 as well as transaction data from TRACE data provided by a major clearing broker. FINRA noted that there are several limitations to the analysis due to data availiability. We respectfully suggest these limitations do not allow FINRA to determine the impact that newly issued multifamily/healthcare GNMA MBS have on the level of systemic risk that is the heart of this proposed rule. If FINRA staff spoke with staff at GNMA or FNMA, they would understand that neither agency has observed any sizable failures by issuers and would learn more details about the level of oversight they conduct on lenders.

8) The proposed rule mentions that allowing lenders to participate in the TBA market may facilitate increased leverage and thus elevate systemic risk. As a small multifamily lender and GNMA issuer, I cannot conceive of how we could increase our leverage simply by entering into rate locks with a broker/dealer. It would seem that this concern is more directed at the major financial institutions that use the TBA market to hedge other financial positions.

We respectfully request the Commission provide more time to review this proposed rule and its impacts on the multifamily and healthcare industry and on affordable housing as well as secondary and tertiary markets. From our perspective, current business and risk mitigation practices in place have proven newly issued multifamily and healthcare GNMA MBS do not create an elevated risk to broker/dealers or the banking sector. Quite the opposite, during the recent financial crisis, these sources of capital stepped up and efficiently provided capital to the multifamily and healthcare industry at a time of great economic stress. Burdening them with a solution looking for a problem that doesn't exist will have negative consequences. Smaller lenders will likely not have access to capital or lines of credit to fulfill their margining obligations under this proposed rule. Many may need to turn to their borrowers to provide such capital. If borrowers are ultimately looked to for meeting margin requirements, lenders will not be able to use this source of financing for affordable housing transactions as many of the developers are smaller firms or non-profits without access to capital for margining. Neither the exemption of $2.5m or initial $250,000 margin is large enough to avoid negatively impacting such projects or borrowers. Thus lenders who participate in the GNMA MBS program will be larger financial institutions that have ample capital to move around on a daily basis to meet this obligation. Nor will larger institutions have much incentive to finance smaller projects in secondary and tertiary markets.

Thank you for your consideration of these concerns.

Sincerely,

FOREST CITY CAPITAL CORPORATION

Tony Love

Tony Love
Vice President

Ginnie Mae
Our Guaranty Matters
451 Seventh Street S.W., B-133
Washington, D.C. 20410
(202) 708-1535

[redacted]

[redacted]

Re: Ginnie Mae Pool Number: [redacted]
FHA Case Number: [redacted]
Project Name: [redacted]

Dear [redacted]:

This is in response to your electronic request of [redacted], requesting confirmation and clarification of Ginnie Mae's obligations regarding the authorization of the issuance of Ginnie Mae Construction Loan Certificates (CLC) collateralized by bond financing.

There are two possible situations under which Ginnie Mae's willingness to issue a CLC may be in question:

1) If an approved Ginnie Mae issuer defaults under the Ginnie Mae Guaranty Agreement after a construction loan advance is made and insured, but prior to the issuance of the corresponding CLC ("Issuer Default") and/or;
2) When a borrower defaults on a construction loan subsequent to a loan advance insured by FHA, but prior to the issuance of the corresponding CLC covering that advance ("Borrower Default").

Both situations are further conditioned by defaults, which occur prior to and after the issuance of an initial CLC.

Borrower Default Prior To or After Issuance of Initial CLC.

If a borrower defaults on a construction loan after a construction loan advance has been made and insured, either prior to or after the issuance of the initial CLC, Ginnie Mae will authorize the issuance of the corresponding CLC. A default by a borrower or mortgagor is a matter, which primarily concerns FHA and the issuer and does not immediately involve Ginnie Mae. However, the issuer is obligated to pay the security holder(s) the interest payments due on the CLC to be issued, as well as on the outstanding CLCs, through the month that the pool is terminated due to the loan default.

Issuer Default Prior to Issuance of Initial CLC.

If an issuer defaults under the Ginnie Mae Guaranty Agreement after an initial construction loan advance has been made and insured, but prior to the issuance of the corresponding CLC and the initial CLC for the project, Ginnie Mae will not authorize the issuance of the initial CLC. Section 3-1 of the Ginnie Mae Guide 5500.3 states that Ginnie Mae may terminate an issuer's authority to administer pools, to utilize commitment authority already outstanding, and to receive additional commitment authority or pool numbers in the event of default. The above position would also apply to instances where an issuer becomes ineligible to participate in any of HUD-FHA's programs. Sections 2-3 and 3-2 of the Ginnie Mae Guide 5500.3 states that an issuer must be an approved FHA mortgagee in order to issue Ginnie Mae Mortgage-Backed Securities.

Issuer Default after Issuance of Initial CLC.

If an issuer defaults under the Ginnie Mae Guaranty Agreement after a construction loan advance has been made and insured, but prior to the issuance of the corresponding CLC and the initial CLC had been issued prior to the default, Ginnie Mae generally will issue the CLC, except when issuer fraud or misrepresentation exists. In such cases, Ginnie Mae will assign the defaulted issuer’s pools to either a subservicer or a substitute issuer. The remaining CLCs for the project would continue to be issued as construction progresses, as long as the borrower does not default, and the Project Loan (or Project Note) security would be issued for the project following final endorsement of the mortgage.

Simultaneous Default by Both Issuer and Borrower.

In cases of simultaneous defaults by both the borrower and the issuer after a construction loan advance has been made and insured, but prior to the issuance of the corresponding CLC, and the initial CLC had been issued prior to the default, Ginnie Mae generally will issue the CLC except when issuer fraud or misrepresentation exists.

For simultaneous defaults of issuer and borrower occurring prior to the issuance of an initial CLC, Ginnie Mae will not authorize the issuance of a CLC, even if the initial advance had been made and insured.

Finally, Ginnie Mae's guaranty attaches to any prepayment penalty or premium on a mortgage note. Pursuant to Section 31-13(D) of the Guide, the issuer must specify in the Prospectus the prepayment provisions of the note, including any provision detailing prepayment penalties or premiums. If a prepayment penalty or premium is collected, it must be passed through to security holders together with the regularly scheduled payment of principal and interest.

The policies discussed above apply irrespective of the FHA program authority under which the pooled loan is insured.

I hope that this letter adequately responds to your request. If you have any questions or concerns, please contact me at [redacted].

Sincerely,

Philip H. Buckley
Director, Multifamily Division
Office of Issuer and Portfolio Management