INDEPENDENT COMMUNITY BANKERS of AMERICA

June 23, 2008

Robert E. Feldman
Executive Secretary
Attention: Comments
Federal Deposit Insurance Corporation
550 17th Street, N.W.
Washington, D.C. 20429

Re: Covered Bond Policy; Interim Final Policy Statement

Dear Mr. Feldman:

The Independent Community Bankers of America (ICBA)[1] appreciates the opportunity to offer comments in connection with the FDIC's interim final policy statement on the treatment of covered bonds in a conservatorship or receivership.

Summary of ICBA's Position

While ICBA generally supports the FDIC's interim policy statement on covered bonds, ICBA strongly disagrees with including secured liabilities and in particular Federal Home Loan Bank (FHLBank) advances as part of an institution's assessment base or as a factor for determining an institution's insurance assessment rate. FHLBank advances serve as a consistent, reliable source of liquidity for all FHLBank members and discouraging their use would be counterproductive to reducing risks for the FDIC. ICBA also believes that penalizing the use of advances by charging

[1]*The Independent Community Bankers of America represents nearly 5,000 community banks of all sizes and charter types throughout the United States and is dedicated exclusively to representing the interests of the community banking industry and the communities and customers we serve. ICBA aggregates the power of its members to provide a voice for community banking interests in Washington, resources to enhance community bank education and marketability, and profitability options to help community banks compete in an ever-changing marketplace.*

With nearly 5,000 members, representing more than 20,000 locations nationwide and employing over 282,000 Americans, ICBA members hold more than $982 billion in assets, $788 billion in deposits, and more than $681 billion in loans to consumers, small businesses and the agricultural community. For more information, visit ICBA's website at www.icba.org.

higher premiums under the recently adopted risk-based assessment system would conflict with the intent of Congress in establishing the FHLBanks.

Background

Covered bonds are general obligation bonds of the issuing bank secured by a pledge of loans that remain on the bank's balance sheet. In a typical covered bond transaction, a bank sells mortgage bonds, secured by mortgages, to a trust or similar special purpose entity. The pledged mortgages remain on the bank's balance sheet, securing the bank's obligation to make payments on the debt, and the trust or other special purpose vehicle sells covered bonds, secured by the mortgage bonds, to investors. In the event of a default by the bank, the mortgage bond trustee takes possession of the pledged mortgages and continues to make payments to the special purpose vehicle to service the covered bonds.

Covered bonds originated in Europe, where they are subject to extensive statutory and supervisory regulation designed to protect the interests of covered bond investors from the risks of insolvency of the issuing bank. By contrast, covered bonds are a relatively new innovation in the U.S. with only two issuers to date—Bank of America and Washington Mutual. However, covered bonds are expected to grow in popularity in the U.S. since they are a useful liquidity tool for banks that need to hold their mortgages on their balance sheet.

Under the Federal Deposit Insurance Act, when the FDIC is appointed conservator or receiver of a bank, contracting parties cannot automatically terminate agreements with the bank. In addition, contracting parties must obtain the FDIC's consent during the 45 day period after appointment of the FDIC as a conservator, or during the 90 day period after appointment of FDIC as receiver, before liquidating any collateral pledged for a secured transaction. Covered bond obligees would therefore be subject to a lengthy wait before being able to repossess and liquidate collateral if the bank went into receivership or conservatorship.

Interim Policy Statement

To address this problem for covered bond transactions and to provide guidance to potential covered bond issuers and investors, the FDIC is adopting on an interim basis a Policy Statement that, in the event of a bank conservatorship or a receivership, would provide automatic consent to covered bond obligees to exercise their contractual rights over covered bond collateral within 10 business days after a monetary default or 10 days after the effective date of repudiation. However, the Policy Statement and the automatic consent would only apply to covered bond issuances (1) made with the consent of the primary federal regulator, (2) comprising no more than 4% of a bank's total liabilities, and (3) secured by "eligible mortgages."

The Policy Statement would define "eligible mortgages" as those secured by perfected security interests under applicable state and federal law on performing mortgages on one-to-four family residential properties, underwritten at the fully indexed rate and relying on documented income. Eligible mortgages would have to be underwritten in accordance with existing supervisory guidance governing the underwriting of residential mortgages, including the Interagency Guidance on Non-Traditional Mortgage Products and the Interagency Statement on Subprime Mortgage Lending.

Policy Issues Concerning Assessment Rates

From an insurance perspective, the FDIC also is seeking comment on whether an institution's percentage of secured liabilities to total liabilities should be factored into an institution's insurance assessment rate or whether the total secured liabilities should be included in the assessment base. The FDIC also seeks comment on whether, as part of this Policy Statement, there should also be an overall cap for secured liabilities.

ICBA's Position

ICBA generally supports the FDIC's interim policy statement on covered bonds and the proposed treatment of covered bonds when a bank is under FDIC receivership and conservatorship. The proposed new policy, if adopted, will provide important guidance to potential covered bond issuers and investors and will encourage the use of covered bonds in the United States. We believe, however, that as covered bonds mature as a product and more banks realize their utility as a liquidity tool and as a good substitute for mortgage securitizations, the FDIC should reconsider and possibly raise the proposed 4% cap. We also support limiting the policy statement to covered bonds secured by eligible mortgages underwritten in accordance with existing supervisory guidance governing the underwriting of residential mortgages.

However, ICBA strongly disagrees with including any secured liabilities and in particular FHLBank advances as part of an institution's assessment base or as a factor for determining an institution's insurance assessment rate. This issue was raised previously by the FDIC in connection with its proposal in 2006 for a new risk-based assessment system as authorized by the Federal Deposit Insurance Reform Act of 2005**. ICBA said then that it strongly opposes including FHLBank advances as part of "volatile liabilities" since that would inappropriately discourage banks from borrowing from the FHLBanks and would be counterproductive to reducing risks for the FDIC.**[2]

FHLBank advances serve as a consistent, reliable source of liquidity for all FHLBank members. The availability of FHLBank advances as a means of wholesale funding is especially important to the community banks that comprise a large majority of the FHLBank System's members. These institutions do not have reliable access to other sources of cost-effective wholesale funding and rely on the availability of FHLBank advances as a critical tool for managing their balance sheets and implementing their business plans. In fact, in 2007 FHLBank advances increased 36.6 percent to $875 billion, and increased further to $913 billion by the end of the first quarter 2008 - indicating that the FHLBanks are playing a vital role in alleviating the current shortage of

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[2] See ICBA's letter to the FDIC dated September 22, 2006 commenting on the proposed new risk-based assessment system.

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liquidity in the mortgage markets. Discouraging the use of the FHLBank funding would be counterproductive to the current efforts by the Administration, Congress, and the Federal Reserve to restore liquidity and bolster confidence in the mortgage sector.

As we pointed out previously in our letter to the FDIC concerning the proposed new risk-based assessment system, ICBA believes that any policy that discourages borrowing from the FHLBanks would not only be counterproductive to reducing risks for the FDIC but could actually increase risks. FHLBank advances are commonly used for liquidity purposes, and help FHLBank members manage interest-rate risk and fund loan growth, especially in markets in which the supply of deposit funds is inadequate to meet loan demand and prudent financial management needs. If the use of FHLBank advances is discouraged, FHLBank members would be forced to seek alternative, often more costly and volatile sources of funding, thereby reducing profitability and increasing liquidity risk.

ICBA also believes that penalizing the use of advances by charging higher premiums under the new risk-based assessment system would conflict with the intent of Congress in establishing the FHLBanks, in opening membership in FHLBanks to commercial banks under FIRREA, and in adopting the Gramm-Leach-Bliley Act which expanded small banks' access to advances. Congress wanted commercial banks to have unfettered access to the low-cost funding of the FHLBanks. Charging higher assessments for banks that have FHLBank advances would be inconsistent with that goal.

FHLBank advances are a critical source of credit for housing and community development purposes, sustain prudent financial management practices, and enable small community member banks throughout the nation to remain competitive. FHLBank membership has long been viewed as protection for deposit insurance funds because FHLBank members have access to a reliable source of liquidity. **In considering a final Policy Statement on covered bonds, or in taking any other administrative action, ICBA strongly urges the FDIC not to penalize institutions based on their use of Federal Home Loan Bank advances, or to limit the amount of such liabilities that they can use for their funding needs.**

Conclusion

While ICBA generally supports the FDIC's interim policy statement on covered bonds, and the treatment of covered bonds when a bank is under FDIC receivership and conservatorship, ICBA strongly disagrees with including secured liabilities and in particular FHLBank advances as part of an institution's assessment base or as a factor for determining an institution's insurance assessment rate. FHLBank advances are a consistent, reliable source of liquidity for all FHLBank members and discouraging their use would be counterproductive to reducing risks for the FDIC. ICBA also believes that penalizing the use of advances by charging higher premiums under the new risk-based assessment system would conflict with the intent of Congress in establishing the FHLBanks, in opening membership in FHLBanks to commercial banks under FIRREA, and in adopting the Gramm-Leach-Bliley Act which expanded small banks' access to advances.

ICBA appreciates the opportunity to offer comments in connection with the FDIC's interim Policy Statement on Covered Bonds. If you have any questions about our letter, please do not hesitate to contact me at 202-659-8111 or Chris.Cole@icba.org.

Sincerely,

/s/ Christopher Cole

Senior Regulatory Counsel