NATIONAL ASSOCIATION OF HOME BUILDERS

DAVID L. LEDFORD

SENIOR VICE PRESIDENT
HOUSING FINANCE AND LAND DEVELOPMENT

October 15, 2009

Office of the Comptroller of the Currency
250 E. Street, SW, Mail Stop 2-3
Washington, DC 20219
Docket No. OCC-2009-0012

Jennifer J. Johnson
Board of Governors of the
Federal Reserve System
20th Street and Constitution Ave., NW
Washington, DC 20551
Docket No. R-1368

Mr. Robert E. Feldman
Executive Secretary
Attention: Comments/Legal ESS
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429
RIN 3064-AD48

Regulation Comments
Chief Counsel's Office
Office of Thrift Supervision
1700 G Street, NW
Washington, DC 20552
Attention: OTS-2009-0015

Re: Risk-Based Capital Guidelines; Capital Adequacy Guidelines; Capital Maintenance: Regulatory Capital; Impact of Modifications to Generally Accepted Accounting Principles; Consolidation of Asset-Backed Commercial Paper Programs; and Other Related Matters

Dear Sir/Madam:

On behalf of more than 200,000 members of the National Association of Home Builders (NAHB), I am pleased to respond to the request for comments on the Agencies' (comprised of the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Board of Governors of the Federal Reserve System and the Office of Thrift Supervision) notice of proposed rulemaking (NPR) related to risk-based capital guidelines and the impact of modifications to generally accepted accounting principles (GAAP).

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NAHB is a national trade association representing individuals and companies involved in the production of housing and related activities. Each year, NAHB's builder members construct about 80 percent of all new housing in America. NAHB's builder members are typically mid-sized and small businesses with limited capital of their own and depend almost entirely upon commercial banks and thrifts for housing production credit. Our surveys show that 90 percent of all loans for residential land acquisition, development and construction (AD&C) come from commercial banks and thrifts, many of whom will be impacted by the NPR. Therefore, regulatory changes that affect the capital requirements of banks could have major ramifications for our members, especially during periods when the housing finance system is not functioning efficiently.

Proposal

The Agencies are requesting comment on a proposal to better align capital requirements with the actual risk of certain exposures and on the effect on regulatory capital that will result from the implementation of the Financial Accounting Standards Board's (FASB) Statement of Financial Accounting Standards No. 166, *Accounting for Transfers of Financial Assets, an Amendment of FASB Statement No. 140* (FAS 166), and Statement of Financial Accounting Standards No. 167, *Amendments to FASB Interpretation No. 46(R)* (FAS 167), on consolidation of variable interest entities (VIEs). In the comments that follow, these statements are referenced as the 2009 GAAP modifications.

The proposal would modify the general risk-based and advanced risk-based capital adequacy frameworks to eliminate the exclusion of certain consolidated asset-backed commercial paper programs from risk-weighted assets. The proposal would also provide a reservation of authority in the general risk-based and advanced risk-based capital adequacy frameworks to permit the Agencies to require banking organizations to treat entities that are not consolidated under accounting standards as if they were consolidated for risk-based capital purposes. The Agencies request comment on the regulatory capital impact of FASB's amended statements, including the effect of FAS 166 and FAS 167 on a banking institutions financial position, lending, and other activities. Finally, the Agencies request public comment on a phase-in period, and the impact of FAS 166 and FAS 167 on loan loss provisioning, mortgage loan modifications, and securitization reform programs.

The Agencies have requested comment on whether the enhanced capital requirements resulting from the 2009 GAAP modifications should be given immediate effect or whether they should be phased-in over time and, if the latter, what type of phase-in should be considered. Under a four-quarter phase-in approach, banking institutions would be required to hold capital (for purposes of calculating both the leverage and risk-based capital ratios) incrementally against 25 percent of exposures subject to consolidation due to the 2009 GAAP modifications for each of the first three quarters of 2010, and against 100 percent of the exposures thereafter.

Background

The 2009 GAAP modifications generally would increase the amount of exposure recognized on financial institutions' balance sheets. Among other things, it would alter the consolidation analysis for VIEs, thereby subjecting many VIEs that are not consolidated under current GAAP standards to consolidation requirements. These changes will require some banking institutions to consolidate the assets, liabilities and equity of certain VIEs onto their balance sheet for financial and regulatory reporting purposes. FASB completed the 2009 GAAP modifications on June 12 and FAS 166 and FAS 167 will become effective as of the beginning of a financial institution's first annual financial statement reporting period that begins after November 15, 2009.

The Agencies' capital standards generally use GAAP treatment of an exposure as a starting point for assessing regulatory capital requirements. However, if the assets are securitized through sale to a VIE that the banking institution does not consolidate under GAAP, generally the bank is required to hold risk-based capital only against its contractual exposure to the VIE. Under the Agencies' leverage capital requirements, tier 1 capital is generally assessed against a measure of a banking organization's total assets. Therefore, previously unconsolidated assets that now must be recognized on a banking institution's balance sheet due to the 2009 GAAP modifications will increase the denominator of the institution's leverage ratio. In most cases both the risk-based and leverage capital ratios of affected institutions' will decrease following implementation of the 2009 GAAP modifications.

The Agencies have stated that with regard to certain off-balance sheet structures where banking institutions were not required to consolidate prior to the 2009 GAAP modifications, the recent turmoil in the financial markets has demonstrated that the credit risk exposure of the sponsoring institutions to such structures (and their related assets) has in fact been greater than the Agencies perceived. In light of recent experience, the Agencies believe that the broader accounting consolidation requirements implemented by the 2009 GAAP modifications will result in a regulatory capital treatment that more appropriately reflects the risks to which banks are exposed. In their consideration of the 2009 GAAP modifications and the interaction of the modifications with the regulatory capital requirements, the Agencies have determined that the qualitative analysis required under FAS 167, as well as the enhanced requirements for recognizing transfers of financial assets under FAS 166, converge in many respects with the Agencies' assessment of a financial institution's risk exposure to a structured finance transaction.

NAHB Position

Excessive use of leverage, mismanagement of liquidity risk and the absence of risk management controls accentuated the deep dysfunction that we see in the securitization markets today. NAHB agrees with the Agencies' assessment that the risk of financial institutions' off-balance sheet structures, which actually amplified leverage and reduced needed liquidity, were understated as evidenced by the scale of unanticipated losses caused by these instruments during the financial turmoil over the last three years. However, NAHB also believes that the implementation of the Agencies' proposal will have far reaching implications for financial institutions and will increase capital requirements and further restrict credit when the economy can least afford it. In addition, NAHB believes that this proposal, in conjunction with financial reform efforts underway in Congress and with the Group of Twenty Finance Ministers and Central Bank Governors (G20), will work to substantially reduce, or even eliminate, some of the important benefits of securitization.

In their most recent meetings in Pittsburgh, the following were among the many recommendations made by the G20:

> We commit to developing by the end of 2010, internationally agreed rules to improve both the quantity and quality of bank capital and to discourage excessive leverage..with the aim of implementation by the end of 2012. The implementation of higher level and better quality capital requirements, counter-cyclical capital buffers, higher capital requirements for risky products and off-balance sheet activities, together with strengthened liquidity risk requirements and forward-looking provisioning, will reduce incentives for banks to take excessive risks and create a financial system better prepared to withstand adverse shocks. We welcome the key measures recently agreed by the Basel Committee to strengthen the supervision and regulation of the banking sector. We support the introduction of a leverage ratio as a supplementary measure to the Basel II risk-based framework.

These reforms also include higher risk retention for securitizations (more "skin-in-the-game") and generally higher capital risk weighting and a more challenging leverage ratio that will restrict balance sheet growth without regard to the risk level of acquired assets. NAHB does not take issue with the proposed G20 reforms or the Agencies' proposal on risk-based capital. It is simply the wrong time to initiate such comprehensive reforms while we continue to experience dramatically tighter credit conditions and systematic deleveraging in the U.S. and around the world.

A well functioning securitization market will be one of the main engines of economic recovery and a healthier housing market. During the credit crisis, we have seen substantial dislocation in the securitization markets which have become dependent upon government support. The subject proposal, if implemented in accordance with the NPR, and the impact of the aforementioned proposed financial regulatory reforms, will result in continued government intervention in the financial markets into the foreseeable future. Private securitization markets will not regenerate under such conditions and lending and credit availability will be constrained by financial institutions' inability to effectively manage their balance sheets. The magnitude of off-balance sheet assets that will be subject to risk-weighting is substantial. The financial press has suggested that the GAAP modifications will reconsolidate up to $1 trillion of assets of the largest bank holding companies.

NAHB strongly believes that the implementation of the proposed rule should be delayed so the consequences of the 2009 GAAP modifications will not translate into higher capital requirements for several years. Since the credit crisis took hold of the economy, financial institutions have taken very significant measures to enhance loan underwriting standards, reduce operational and financial risk, increase loan loss provisions, and deleverage balance sheets in response to the severe capital and credit shock that the financial system has undergone. Despite a recent rally in financial stocks, equity markets are still weak and bank valuations continue to be well below the peaks seen in 2007. For these reasons, NAHB recommends that the Agencies delay implementation for at least 3 years. This will allow financial institutions the necessary time to continue to adjust to a very difficult market and to raise equity to meet regulatory capital requirements resulting from the GAAP modifications under more favorable terms. It will also allow banks time to adjust to financial regulatory reforms that will undoubtedly create additional regulatory capital burdens over the next few years. As the Federal Reserve has stated,

> The Board is not bound to use GAAP accounting concepts in its definition of tier 1 or tier 2 capital because regulatory capital requirements are regulatory constructs designed to ensure the safety and soundness of banking organizations, not accounting designations established to ensure the transparency of financial statements…Tier 1 capital, for example, has differed from GAAP equity in a number of ways.

Finally, the Agencies are silent as to how risk-based capital will be applied to reconsolidated assets. NAHB recommends that the Agencies establish risk-weights for these assets that are consistent with existing regulation.

Conclusion

Thank you again for the opportunity to comment on the Agencies' proposal related to risk-based capital guidelines and the impact of modifications to GAAP. NAHB agrees that the off-balance sheet risks addressed in the proposal contributed, and in some cases continue to contribute, to the financial turmoil experienced over the last several years. At the same time, banking institutions, regulators, securitizers, investors and borrowers have gained a far keener sense of how these risks impacted the financial markets and the health of the banking system. Banking institutions in particular have taken significant steps to address risks that undermined the banking system. Unfortunately, regulatory overreach and the multitude of new regulations and proposed financial regulatory reforms threaten a recovery and could potentially create a procyclical impact on credit that must be reversed. For these reasons, NAHB believes that the proposed rule which would align regulatory capital requirements with the 2009 GAAP modifications should be delayed. This will relieve banking institutions of a difficult burden that if implemented now, or if phased-in during the next year, would delay recovery and restrict credit availability.

Please direct questions regarding this matter to Michelle Hamecs, NAHB's Assistant Vice President for Housing Finance, at 202-266-8425, or via e-mail at mhamecs@nahb.com .

Sincerely,

David L. Ledford

David L. Ledford
Senior Vice President
Housing Finance and Land Development

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