Gershman Mortgage

November 18, 2015

By Electronic Submission

Robert W. Errett
Deputy Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

RE: *Multifamily Industry Coalition Comments on SR-FINRA-2015-036*, Proposed Rule to Amend FINRA Rule 4210 Margin Requirements for To Be Announced Transactions (Notice published October 20, 2015)

Dear Mr. Errett:

Our Company is an independently owned, mortgage banking firm engaged in financing multifamily housing and healthcare projects through the FHA-insured loan programs. Our financing is funded by the sale of Ginnie Mae Mortgage Backed Securities. We are active in the issuance and sale of both Construction Loan Pools as well as Project Loan pools.

We strongly urge the Commission and FINRA to remove coverage of Ginnie Mae Mortgage Backed Security forward-settling transactions from the proposed rule SR-FINRA-2015-036. The proposed rule lacks any data or analysis on the impacts to the very distinct FHA/GNMA multifamily finance markets. We don't think the rule should cover these securities and are very concerned that the proposed rule could have significant and unintended consequences on the financing of affordable multifamily rental apartments. Most of the properties financed using the FHA-insured loan programs provide housing or healthcare to families earning median income or less. Some of the important considerations are identified below.

THE PERCEPTION OF SYSTEMIC RISK IS NOT REALITY

Systemic risk concerns appear to be a central reason for imposing margining on the multifamily forward-settling market as is noted in the Treasury Market Practice Group (TMPG) white paper release. They noted that "to the extent uncleared transactions in the TBA market remain unmargined, these transactions 'can pose significant counterparty risk to individual market participants' and that 'the market's sheer size . . . raises systemic concern.'" TMPG's release stated that "A sizeable portion of the non-

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centrally cleared agency MBS market currently remains unmargined, posing both counterparty and systemic risks to overall market functioning if one or more market participants were to default."

While the concerns raised in the white paper may be applicable to certain securities markets, the new issue GNMA Mortgage Backed Security for multifamily housing and healthcare market contains safeguards and speed brakes that make the potential for a systemic event highly remote.

The FHA-insured/GNMA multifamily and healthcare programs are a critically important source of financing for rental housing in the U.S.; however, the volumes are not large enough to pose systemic risk concerns. In 2014, all forward-settling multifamily agency executions originated approximately $45 billion. Approximately $9.5 billion of that was financed using the FHA-insured loan/GNMA programs. This volume is dwarfed by the over $1 trillion in single-family mortgage originations.

Moreover, it is important to recognize that only of a *fraction* of the annual origination volume is outstanding during a forward commitment period at a given point in time. For example, while the total originations under this program for 2014 was $9.5 billion, the weekly average amount of outstanding forward commitments in the Ginnie Mae MBS program would only be a fraction of that number.

The asset-specific lending character of this market largely confines the risk to the identified asset and isolates it from "contagion risk." Since multifamily properties are heterogeneous, each GNMA multifamily security is property-specific with the terms of the mortgage loan and security known at the time of forward trade.

Unlike in the single-family mortgage market, FHA-Insured/GNMA multifamily Lenders do not enter into forward TBA contracts and seek to fill a pipeline and inventory with mortgages prior to settlement (when pools must be delivered). Single-family originators assume the risk that they will be able to deliver the agreed upon quantity of loans with similar generic terms by a certain date. This differs greatly from the multifamily agency securitization market, where the underlying loan is already committed to by both the borrower and the lender, with meaningful penalties to the borrower for failing to close the loan.

Forward-settling multifamily loans are originated by a small network of Lenders approved by FHA/Ginnie Mae. These Lenders are subject to strict oversight and capital requirements from both FHA and GNMA. The FHA-insured multifamily and healthcare execution risk is backed by a Good Faith Deposit, which we send to the broker dealer or investor and is spelled out in a contractual rate lock agreement with the borrower. The borrower cannot simply and easily switch lenders or capital sources based on market fluctuations. Breakage fees are substantial, and costly third-party reviews have been performed that cannot be readily transferred to another lending source. In addition, the months required to switch capital sources would prevent borrowers from capitalizing on short-term interest rate movements, as the lengthy underwriting process for the borrower would have to begin again upon switching lenders. Consequently, the concerns about systemic risk are clearly not applicable to the FHA-insured/GNMA MBS multifamily agency market.

In the event of a delivery failure, financial relief for losses comes from remedies provided in the transaction documents — there is not a market mechanism to replace the security with another similar security, given that the trade is for a specific security backed by an identified multifamily loan. In other words, the trades and securities are *not fungible*, as the multifamily transaction stipulates a specific asset — a loan on an identified, unique multifamily property.

Over several months, a multifamily property is reviewed and underwritten through expensive and extensive third party reports assessing physical condition, rental income analysis, property management plans, and more. Property owners and lenders in the highly specialized multifamily agency market are well-aligned and highly motivated to close a trade given the investment of time and money (typically $25,000 or more for the borrower's hard costs for one multifamily transaction). Since each multifamily property is unique, involves property-specific underwriting and credit determinations and is issued in a security with a unique interest rate, it is difficult to see how the requirement to mark-to-market on a daily basis would work at all.

Historically Miniscule Delivery Failures of GNMA Multifamily/Healthcare Securities

There have been very few settlement failures in the history of the forward-settling multifamily GNMA market. We queried the broker-dealers with whom we do business and they indicate there have been a very small number of delivery fails during the past decades. Among the small number of delivery fails that have occurred, a common cause was a property-level event (rather than a counterparty risk-driven cause), such as property damage caused by a natural disaster. .

The minimal number of failed trades is a very strong indication that the numerous protections for counterparty risk in the market have been effective, even during periods of severe market disruption. Clearly, Lenders as counterparties operate as going concerns and fulfill their obligation as loan sellers and/or issuers. We understand the same to be true for broker-dealers as counterparties in the multifamily agency market, particularly the GNMA MBS markets.

Unintended Consequences

The forward-settling GNMA project loan market enables the borrower to rate lock and the lender to mitigate interest-rate risk, thereby allowing the lender to finance additional multifamily projects and provide liquidity to the market. A margining requirement would effectively impose additional liquidity requirements placing liquidity pressures on FHA lenders, in particular smaller independent firms like ours. This gives an unfair competitive advantage to large bank owned Lenders that participate in this program.

Given the safeguards and protections that already exist in the market (*e.g.*, the Good Faith Deposit, agency oversight and regulation, and counterparty risk management measures), we believe the negative consequences outweigh any incremental benefit.

Requiring lenders to post margin for GNMA MBS multifamily securities would pose significant burdens on market participants, disrupt mechanisms that are currently in place, and result in unintended consequences. The liquidity and operational burden would be particularly detrimental to smaller lenders. Small, non-bank-owned lenders, who tend to finance more affordable rental properties with the FHA-insured loan programs, will face difficulty in implementing margining mechanisms; the personnel, infrastructure and resources needed for these firms could be cost prohibitive.

The Ginnie Mae program is unique in that the new construction or substantial rehabilitation of a multifamily or residential healthcare property is financed through one long term loan with two securities – one for the construction loan phase (CLCs – a series of CLCs are issued and settled as draws occur during the construction period) and the other for the project's permanent loan (PLC – issued in exchange for the outstanding CLCs when the loan is converted to a permanent loan). Counterparty exposure is reduced incrementally over the construction term. Borrowers draw funds according to their construction schedule throughout the term and the individual construction draws are delivered to the investor (dealer) on a pro-rata basis, thus reducing the counterparty exposure.

Mark-to-market valuation for GNMA Mortgage Backed Securities is nearly impossible to do in an accurate or consistent manner. These Securities, like the underlying collateral, are heterogeneous and different dealers will often provide differing bids on a bond. This would compound the difficulty of determining how much margin would need to be posted.

Price discovery will be challenging at best and likely cause disputes among lenders and dealers, exacerbating the time and resources expended to comply with the requirement. There are no widely used indexes, exchanges, or virtual marketplaces to trade GNMA MBS at this time. Each bond is sold via direct placement or auction to set a rate for a specific property with specific characteristics, *e.g.*, asset/product type, loan term, prepayment protection, amortization, interest only period, and lien position. An adjustment to one of the variables above may increase/decrease the rate by 15-20 basis points. Additionally, the same loan may have a bid range of up to 20-120 basis points from different dealers. Differences in perceived value will result in disputes, which will require time and effort to resolve. The mark-to-market issue could be even more problematic for construction loans that back Ginnie Mae Construction Loan Certificates (CLCs).

The affordable rental housing market, in particular, could be disproportionately harmed. Capital sources, whether equity or debt, are often limited for "targeted affordable properties," such as those supported by the federal low-income housing tax credit, historic tax credits, or city or local government grants. The liquidity that would be necessary to provide margining may not be available from any of the market participants that are constructing, rehabilitating or refinancing an affordable rental property. Notwithstanding the limited availability of capital for these property types, the same safeguards and protections noted above exist, including the Good Faith Deposit and stringent oversight and monitoring by the agencies.

Likewise, many borrowers (who will ultimately bear the cost of margining) are not in a position to post significant margin beyond the Good Faith Deposit. A significant number of borrowers who own, operate and renovate affordable rental housing are smaller institutions or nonprofit organizations. Unable to post margin (beyond the Good Faith Deposit), such borrowers would be unable to lock-in a long term fixed rate during the underwriting and closing process, which would significantly increase their execution risk. The effect could be that modest multifamily rental properties, seniors housing properties, or affordable apartment buildings may not get constructed, renovated or rehabilitated.

FINRA does not appear to have considered the Proposal's economic impact on the multifamily rental housing market. The Proposed Rule scopes in multifamily agency securities in a footnote by referencing the views of the Treasury Market Practices Group, a best practices group. We are deeply concerned with the cursory manner with which the Proposal sweeps in multifamily rental housing sector with little or no justification.

FINRA's policy on economic impact assessments contains three key principles: FINRA will a) consult with key stakeholders in the development of rules; b) provide clarity about the objectives and potential impact of rule proposals and alternatives considered; and c) obtain supporting evidence where possible. The Proposed Rule appears to completely ignore the multifamily rental housing market with regard to the latter two principles. As a resulted, we believe that the FHA-insured/GNMA MBS multifamily finance market should be exempted from the rule. Given the significant impact that this rule could have on the multifamily finance market, any requirement must have an extended, multi-year implementation period.

We urge the Commission and FINRA to exclude multifamily and healthcare, GNMA Mortgage Backed Security forward-settling transactions from the proposed rule. Examination of the distinct aspects of the multifamily housing market and the related economic impact is necessary before this rule moves forward.

Thank you for your consideration. If you have any questions, please contact me.

Sincerely,
GERSMAN MORTGAGE

Bruce Sandweiss
Executive Vice President