American Bankers Association
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The Honorable Sandra Thompson
Director
Federal Housing Finance Agency
400 7th Street, SW
Washington, DC 20019

Re: FHLB at 100 Request for Comments

Dear Director Thompson,

The American Bankers Association (ABA)[1] appreciates this opportunity to provide comments on the Federal Housing Finance Agency's (FHFA) comprehensive review of the Federal Home Loan Banks (FHLBanks).

The FHLBs have, for 90 years, quietly and efficiently served as an important liquidity source for their member institutions. During the nearly a century that they have been in existence, many changes have occurred in the financial services industry, including those that have affected the FHLBanks, most notably the 1989 enactment of the Financial Institutions Reform, Recovery and Enforcement Act (FIRREA). That law made significant changes to the FHLBank System, including the extension of membership eligibility for commercial banks and credit unions, the creation of the Affordable Housing Program (AHP) and the imposition of the Resolution Funding Corporation (REFCORP) obligation on the FHLBanks. In 1999, the passage of the Federal Home Loan Bank System Modernization Act as part of the Gramm/Leach/Bliley Act made membership voluntary for all members and expanded access to FHLBanks' products and services. It also required reform of the capital structure of the FHLBanks and transferred many corporate governance responsibilities to the FHLBanks directly. In 2005 the FHLBs became registrants with the Securities Exchange Commission, and in 2008, the FHFA was created, becoming the new regulator of the FHLBs as well as Fannie Mae and Freddie Mac.

Thus, throughout their 90-year existence, the FHLBanks have not escaped Congressional and regulatory oversight and reform. Still, ongoing oversight and review is prudent, and we welcome the current comprehensive review. This review, however, must recognize that the FHLBanks' mission, ownership structure and membership criteria are set by statute and can only be changed by Congress. We urge FHFA to be mindful of the limits of its statutory mandate and to focus on ensuring that the Banks are meeting their statutorily defined mission in a safe and sound manner.

FHFA has posed six topics for respondents to consider. We offer initial comments based upon general experience and feedback from our members, particularly members of our Federal Home

[1] The American Bankers Association is the voice of the nation's $22.8 trillion banking industry, which is composed of small, regional and large banks that together employ more than 2 million people, safeguard nearly $19 trillion in deposits and extend $11 trillion in loans.

Loan Bank Committee. However, we believe that each of these topics deserves in depth discussion that we hope the additional listening sessions, roundtables and other aspects of the comprehensive review can foster. We urge FHFA to provide more information about the format of each of these forums, as well as information about the timing and goals of the comprehensive review as soon as practicable.

With the above history, recommendations and reminder of the mandate of the FHFA in mind, we offer feedback on each of the topics in turn. They are:

1. The FHLBanks' general mission and purpose in a changing marketplace;
2. FHLBank organization, operational efficiency, and effectiveness;
3. FHLBanks' role in promoting affordable, sustainable, equitable, and resilient housing and community investment;
4. Addressing the unique needs of rural and financially vulnerable communities;
5. Member products, services, and collateral requirements; and
6. Membership eligibility and requirements.

The Federal Home Loan Banks' general mission and purpose in a changing marketplace

As FHFA notes on its website "The FHLBanks have been a fundamental part of the nation's financial system for more than eight decades. The System provides its members …with a source of funding for mortgages and asset-liability management; liquidity for a member's short-term needs; and additional funds for housing finance and community development. The FHLBanks provide long- and short-term advances (loans) to their members. Advances are primarily collateralized by residential mortgage loans, and government and agency securities…While the FHLBanks' mandate reflects a public purpose, all 11 regional FHLBanks are privately capitalized and do not receive any taxpayer assistance. During the nation's 2008 financial crisis, the FHLBanks did not take government money, in fact, as other sources of funding dried up, they increased their lending."[2]

By any measure, the FHLBanks have been successful in meeting this mission. They have provided liquidity to their member institutions without taxpayer assistance or a loss on advances for nearly a century, through all economic conditions. The FHLBanks have served as an important source of liquidity for depository institutions, allowing banks to better serve their customers, in particular during periods of stress, including the 2007-2008 financial crisis and the COVID-related stress experienced during the first half of 2020. The FHLBanks have also allowed banks to better diversify their funding sources, increasing the safety and soundness of the banking system. Our FHLBank members note that they continue to need access to liquidity and prioritize FHLBank advances over other sources of liquidity.

In the recent listening sessions, some have suggested an approach that would continue to make FHLBank advances available for community banks, but restrict larger banks to the Federal

[22] (The Federal Home Loan Bank System, 2022)

Reserve or other liquidity sources. Such a restriction would gravely undermine the FHLBanks' mission to provide reliable liquidity to their member institutions to support housing finance and community investment. FHLBank members include some of the largest home mortgage originators and investors in affordable housing and other community development activities, including low and moderate income communities, and they rely on the FHLBanks. Additionally, such a restriction risks undermining the FHLBanks' market presence necessary to borrow large sums at favorable rates, which would likely have a negative impact on smaller members.

The existing structure of the System is well calibrated and balanced. Member institutions capitalize the System with their investment and in return receive the benefits of borrowing at generally attractive rates, earning potential dividends on their investment, and eligibility for Affordable Housing Program funds (and other community support programs) in lieu of or in addition to potential dividends.

While it is true that the financial system is evolving and numerous new entities compete with FHLBank members in the housing and community development finance arena, those entities do not have comparable capital requirements, regulation or oversight as existing FHLB members. Most also do not have the kinds of eligible collateral used to back borrowing from the System in its current form. Given the success of the FHLBanks, it is not surprising that these entities want to join or replicate the System. However, their admission would introduce significant risk to the cooperative System. Allowing entities with vastly different regulation, collateral and oversight into the FHLBank System would destabilize it and put existing members' capital at risk, with potential negative cascading effects throughout the financial system.

If there is a demonstrated need to provide these entities with a liquidity source, Congress should enact legislation that addresses that need with a separate new system, ideally with the same level of safeguards that have kept the FHLBank System financially viable and fiscally stable for 90 years. Congress should not, however, attempt to revise or reform the existing System to accommodate these other entities, as doing so would almost certainly destabilize the existing system and potentially destabilizing the stability of the broader financial system.

FHLBank Organization, Operational Efficiency, and Effectiveness

One of the hallmarks of the FHLBank System has been the regional FHLBanks that comprise the System, which make it more responsive to regional and local differences and needs. We note that the existing statutory and regulatory construct of the System permits mergers of FHLBanks that can reduce the total number of FHLBanks, as occurred with the merger of the FHLBank of Seattle into the FHLBank of Des Moines in 2015. While FLHBank mergers are complicated and require significant agreement among members of the impacted FHLBanks and oversight from the FHFA, mergers are possible. We view this as appropriate for a cooperative system.

Some criticize the FHLBank System's regional structure as inefficient and call for a single, unified structure, like that of Fannie Mae and Freddie Mac. Proponents of the current System

counter that a single, centralized FHLBank would lose the regional input and awareness of localized needs that has made the existing System responsive.
An alternative to centralization or mergers that the FHLBanks may wish to consider is a shared services model that facilitates delivery of services but leaves decision making with the regional FHLBanks. The System's Office of Finance, which serves all 11 FHLBanks in accessing the capital markets, could serve as a model or even a vehicle for this approach.
We believe that this is an issue that should be determined by the member/owners of the FHLBank System, and we encourage FHFA to use the comprehensive review to foster discussion about the balance between regional responsiveness and centralized efficiency that may help members determine if voluntary mergers of FHLBanks or centralization of services may be desirable. We do not believe, however, that mergers or centralization should be driven by the FHFA or mandated by Congress The FHLBanks are private, member owned and capitalized institutions, and absent a financial or regulatory crisis that requires intervention, changes to the structure and organization of the System should be left to the member/owners.

FHLBanks' role in promoting affordable, sustainable, equitable, and resilient housing and community investment.

There is no question that the United States is in the midst of an affordable housing crisis, and it is appropriate that all players in the housing finance market play a role in addressing that crisis, including the FHLBanks. However, no single entity can act alone to respond to the crisis. We agree that an appropriate role for the FHLBanks is likely to be some form of expansion of the Affordable Housing Program (AHP) mandate or other, voluntary community support efforts. Members of Congress, including Senator Cortez-Masto (D-NV) and Representative Ritchie Torres (D-NY) have introduced legislation that would expand the AHP mandate, and others, including in the recent listening sessions, have offered proposals to increase the role that the FHLBanks play.

Because the FHLBanks are chartered by Congress, it is appropriate for Congress to set requirements about the level of support they must provide to affordable housing and community development.

An important factor that must be considered in conjunction with these issues is that the FHLBanks are cooperatively owned and have voluntary membership. Changes to the AHP or imposition of other mandates could have unintended consequences. If a mandate is seen as too onerous and negatively impacts the value proposition of membership in the System, members may choose to leave, reducing the profitability of the System and the funding sources for AHP or other mandates. Therefore it is important that members are involved in the discussions about any increased or additional mandates for affordable housing and community development.

Again, the comprehensive review can play an important role in furthering those conversations and in bringing all interested parties to the table to discuss viable options.

Addressing the unique needs of rural and financially vulnerable communities

This topic is closely related to the FHLBanks' organizational structure. As noted above, the regional nature of the FHLBank System is critical to their ability to identify and support the needs of individual communities, including rural and financially vulnerable communities. Indeed, these are the communities that would be most at risk if the FHLBanks were merged or centralized. We have little further feedback to offer at this time but recommend that these issues be prioritized during the regional roundtables. We also recommend that the roundtables be held in locations and structured to encourage participation by representatives of rural and financially vulnerable communities. As stated previously, we believe that it should largely fall to the members/owners of the System to determine the structure and number of the FHLBanks, but we acknowledge and affirm that the FHFA has a role to ensure that members of these communities get a seat at the table and that their concerns are heard and addressed.

Member products, services, and collateral requirements

Again, this topic is closely tied to that of the FHLBanks' regional structure because each FHLBank determines its products, services and collateral requirements. However, because of the cooperative nature of the System, all 11 FHLBanks and their members have an interest in ensuring that products and services, and especially collateral requirements, are appropriate and do not present undue risks to the individual FHLBanks or the System overall. Beyond that, however, it is a hallmark of the responsiveness of the System to local needs that each FHLBank is able to offer products, services and collateral requirements tailored to their individual members.

For example, some of the FHLBanks chose to expand eligible collateral to include certain agricultural loans when the Federal Home Loan Bank Modernization Act was passed as part of the Gramm/Leach/Bliley Act of 1999. Other FHLBanks, with fewer agricultural focused members, chose not to. Now, with more than twenty years of experience by at least some of the FHLBanks, and a changing landscape, both literally and figuratively, for American agriculture, it may be prudent for the FHLBanks to reexamine their acceptable collateral. In any event, this should be done in consultation with the members/owners of the System to ensure that the FHLBanks are responding to member needs, while also ensuring that the collateral accepted and products and services offered are safe and do not bring undue risk to the System.

Membership eligibility and requirements

As noted above, Congress, by statute, sets the membership eligibility requirements for the FHLBank System. While the comprehensive review – and the listening sessions held thus far – have brought forth a number of proposals to modernize or repurpose the System to allow currently ineligible members to join, that cannot happen without Congressional legislation. Further, it should not happen without careful consideration of how potential membership

changes could impact the safety, soundness and long term viability of the System, as well as the capital investment of the current owners/members of the System.
ABA recognizes that the financial services landscape of our country continues to evolve and that non-bank entities play a growing role in housing and other finance. Indeed, many have cited the growing dominance of non-bank mortgage providers as evidence that the FHLBank System needs to be revised. However, even with the growth of nonbank marketshare in mortgage finance, current members of the FHLBank System still – and will continue – to play an important role in housing finance and community development. Indeed, their engagement is more important than ever when the nation faces an affordable housing crisis.

While these other entities may desire additional liquidity sources, and it may be desirable from a public policy standpoint to provide them with one, it is far from certain that the FHLBanks should be used for that purpose. Doing so comes with considerable challenges, not the least of which is how to accommodate less regulated and supervised entities, which also typically lack the kind of collateral necessary to safely and soundly support the existing cooperative structure of the FHLBanks.

While the comprehensive review may provide a forum for these entities to raise their concerns and make their case for access to a liquidity source like the FHLBanks, it should not become an avenue for the development of proposals by FHFA to change the structure of the System. That action would exceed the authority and mandate of FHFA as the regulator of the FHLBanks. That mandate, to ensure that the FHLBanks are meeting their mission in a safe and sound manner, must remain paramount.

Conclusion

We appreciate this opportunity to provide the FHFA with initial thoughts on the topics presented and to suggest topics that warrant further discussion as well as on the appropriate limits of that review. We look forward to further engagement with the comprehensive review process in order to promote a vibrant, responsive and safe FHLBank System.

Sincerely,

Joseph Pigg,
Senior Vice President, Mortgage Finance
American Bankers Association