July 15, 2024

Federal Housing Finance Agency
Division of Bank Regulation
400 7th Street SW
Washington, DC 20219

Re: *Federal Home Loan Bank Core Mission Activities and Mission Achievement*

Dear Sir or Madam,

The Conference of State Bank Supervisors ("CSBS")[1] and the National Association of State Credit Union Supervisors ("NASCUS")[2] (collectively, "state regulators") provide the following comments on the Federal Housing Finance Agency's ("FHFA") request for input ("RFI") on the core mission activities and mission achievement of the Federal Home Loan Bank ("FHLBank") System.[3] The RFI seeks public feedback on questions regarding potential changes to the FHLBank System's mission statement, the establishment of thresholds and metrics to measure mission achievement, and the creation of a member incentive program. FHFA states that it intends to address these potential changes in a forthcoming rulemaking.

State regulators urge the FHFA to refrain from: 1) issuing a proposed rule that would significantly revise the FHLBank System's mission or measurement of that mission, and 2) establishing any member incentive program that provides preferential treatment to institutions based on certain activities. These revisions could place non-statutory conditions or limits on FHLBank liquidity to a wide range of member institutions, have adverse impacts on credit availability for consumers and businesses, and undermine the safety and soundness of member institutions.

Comments on the RFI are organized as follows:

Part I – General Comments

- The FHLBanks help banks and credit unions fund mortgage loans and local economic development, and they are a critical provider of liquidity, including during times of economic stress.
- Absent a Congressional mandate, FHFA should refrain from making policy changes that could undermine the FHLBank System's ability to provide broad, equitable access to liquidity for member institutions.

[1] CSBS is the nationwide organization of state banking and financial regulators from all 50 states, the District of Columbia, and the U.S. territories.
[2] NASCUS is the professional association of the nation's forty-six state credit union regulatory agencies that charter and supervise over 1,800 state-chartered credit unions. NASCUS membership includes state regulatory agencies, state-chartered and federally-chartered credit unions, and other important industry stakeholders. State-chartered credit unions hold over half of the $3 trillion assets in the credit union system and are proud to represent nearly half of the 142 million members. The remaining states lack state-chartered credit unions.
[3] Federal Housing Finance Agency, Request for Input, *Federal Home Loan Bank Core Mission Activities and Mission Achievement* (May 16, 2024).

Part II – Specific Comments on the RFI

- Changes to the FHLBank System's mission must be made by Congress.
- Mission achievement measures and metrics would negatively impact members and the communities they serve.
- A member incentive program would be contrary to the Federal Home Loan Bank Act and create an unlevel playing field among member institutions.

Part I – General Comments

I. The FHLBanks help banks and credit unions fund mortgage loans and local economic development, and they are a critical provider of liquidity, including during times of economic stress.

State regulators have a significant stake in the FHLBank System's mission and how potential changes to it could impact the critical functions it provides to banks and credit unions. More than 90% of state-chartered banks are FHLBank members, and state-chartered banks represent more than half of the FHLBank Systems' member institutions. Over a third of federally insured credit unions are FHLBank members, of which 49% are state-chartered.[4] At the end of Q1 2024, FHLBank advances to depository institutions totaled $590 billion.[5]

State regulators strongly support the goals of increasing affordable housing, homeownership, and community development. FHLBank System liquidity is a critical source of funding that banks and credit unions use to meet the mortgage credit needs of their communities. In 2023, banks and credit unions originated 39% of closed-end mortgage loans, by volume, according to Home Mortgage Disclosure Act ("HMDA") data.[6] Research estimates that FHLBank funding increases mortgage originations by $130 billion and lowers mortgage interest payments by $13 billion every year. Additionally, FHLBank funding significantly empowers smaller institutions to compete against larger financial institutions, enabling these entities to provide more mortgage loans in their local markets. This increased competition leads to an annual increase in mortgage originations of $50 billion.[7]

While state-chartered banks constitute around 34% of banking industry assets, they outperform in terms of financing local economic activity. For example, state-chartered banks provide 55% of all small loans to businesses and 65% of agriculture lending funded by commercial banks. Similarly, state-chartered credit unions, while only 39% of the number of credit unions, hold half of all assets in the credit union system. FHLBank liquidity is critical in helping these institutions fund all manner of loans in their local communities, including to individual homebuyers, housing developers, and other borrowers.

[4] At the end of Q1 2024, there were 6,501 members of the FHLBank System, including 3,332 state-chartered banks and 805 state-chartered credit unions. *Federal Home Loan Bank Membership* (March 31, 2024).
[5] Federal Home Loan Banks, *Combined Financial Report for the Quarterly Period Ended March 31, 2024* (May 14, 2024).
[6] *See* Richey May, *2023 Interactive HMDA Market Share Dashboard* (Accessed July 12, 2024).
[7] Dayin Zhang, Assistant Professor of Real Estate and Urban Land Economics, University of Wisconsin-Madison, *Government-Sponsored Wholesale Funding and Industrial Organization of Bank Lending* (August 11, 2020).

The availability of FHLBank liquidity throughout the economic cycle contributes to a more resilient and stable financial system. The FHLBank System serves as a key source of stable funding, including during times of economic and financial stress, as proven during the 2008 financial crisis, the COVID pandemic, and last year's banking industry turmoil. During the spring 2023 turmoil, depository institutions availed themselves of FHLBank liquidity, the Federal Reserve discount window, and the Federal Reserve Bank Term Funding Program, and together these sources helped stabilize liquidity and diminish stress across the financial system.

It is critical that any policy changes that might affect FHLBank liquidity be considered holistically alongside other regulatory and supervisory requirements and available liquidity sources, including the availability and effectiveness of the Federal Reserve discount window. Liquidity policy changes made without coordination, or with inadequate consideration for the timing of such changes, could undermine financial stability and the ability for banks and credit unions to lend in their local markets, particularly as financial institutions continue to face a higher rate environment and economic headwinds.

II. Absent a Congressional mandate, FHFA should refrain from making policy changes that could undermine the FHLBank System's ability to provide broad, equitable access to liquidity for member institutions.

FHFA has stated that it intends to pursue a future rulemaking that could change the FHLBank System's mission, measurement of mission achievement, and incentives for certain FHLBank members. The changes contemplated by FHFA are meant to direct or condition FHLBank advances to specific uses, which risks undermining the FHLBanks' ability to provide equitable and impartial access to liquidity to its diverse membership. State regulators are confident any change that limits access to FHLBank funding will adversely impact credit availability, the safety and soundness of individual depository institutions, and the broader banking and credit union systems, while further constraining the housing market.

These potential changes represent FHFA's policy objectives, but they are not reflective of the mission that Congress outlined for the FHLBank System. Until Congress amends the Federal Home Loan Bank Act[8] (the "Act") to update the FHLBanks' mission, FHFA should refrain from pursuing major policy changes that are not supported by statute.

Part II – Specific Comments on the RFI

I. Changes to the FHLBank System's mission must be made by Congress.

The purpose of the RFI is to inform a future rulemaking that would revise the Core Mission Activities ("CMA") regulation. FHFA states that the FHLBank System has two core objectives: (1) to provide stable and reliable liquidity; and (2) to support housing and community development. FHFA contemplates a revised CMA regulation that would expressly link these two objectives: FHLBanks would provide liquidity *for* supporting housing finance and community development, as opposed to providing liquidity *and* supporting housing finance and community development. FHFA argues that over time, the FHLBank

[8] 12 U.S.C. § 1421 *et seq.*

System's connection to this second objective has become less direct, requiring a revised mission statement regulation to address this purported shift.[9]

Congress, however, has viewed these two objectives as distinct,[10] even if there may be a natural "relation and overlap[]" between them.[11] Revising the CMA regulation to tie or condition the uses of FHLBank advances to housing finance or community development[12] presents a major change, and cannot be done without Congressional mandate. Indeed, the CMA regulation itself was promulgated[13] to implement significant changes passed in the Federal Home Loan Bank System Modernization Act of 1999.[14] The FHLBanks' mission has already been clearly articulated through the authorities and activities granted by Congress, and FHFA cannot revise the CMA regulation unless and until Congress amends the FHLBanks' mission.

II. Mission achievement measures and metrics would negatively impact members and the communities they serve.

FHFA indicates that a forthcoming rulemaking could establish new metrics and thresholds for measuring achievement of a revised mission statement. Many of these potential measures could have dramatic impacts on member institutions, not just the FHLBanks. Indeed, the RFI specifically states that FHFA aims to "strengthen the ties between FHLBank *member* activity and the FHLBank System's public purpose by helping to ensure that the focus of the FHLBanks' business supports housing finance and community development."[15] FHFA should refrain from establishing new mission measurements that could disadvantage certain member institutions or provide preferential treatment of certain CMA activities.

In particular, new mission measurements that only count or provide beneficial weightings for advances to members with a strong housing and community development nexus could create significant adverse consequences for broad swaths of member institutions. Those negative consequences would ripple through the communities served by these institutions. For example, community banks and small credit unions in rural or underserved markets may face limited demand for residential mortgage loans. Moreover, it could be exceedingly difficult for member institutions, particularly community banks and small credit unions, to monitor, document, and demonstrate how their specific lending activities or businesses meet FHFA-established benchmarks or thresholds. FHLBanks may be disinclined, or even face

[9] *Supra* note 3, at 6-7.
[10] The Housing and Economic Recovery Act of 2008 explicitly requires FHFA to consider the FHLBanks' "mission of providing liquidity to members" independently of the FHLBanks' "affordable housing and community development mission." *See* 12 U.S.C. §§ 4513(f)(1)(B)-(C).
[11] *Supra* note 3, at 7.
[12] Long-term advances are the only instance in which Congress has directed that FHLB liquidity be used for particular purposes. *See* 12 U.S.C. § 1430(a)(2).
[13] Federal Housing Finance Board, Final Rule, *Powers and Responsibilities of Federal Home Loan Bank Boards of Directors and Senior Management*, 65 Fed. Reg. 25267 (May 1, 2000).
[14] The Federal Home Loan Bank System Modernization Act comprised Title VI of the Gramm-Leach-Bliley Act, Pub. L. 106–102 (1999).
[15] *Supra* note 3, at 7 (emphasis added).

FHFA-imposed limits,[16] on providing advances to such institutions. This could negatively impact some depository institutions simply because they do not have significant FHFA-favored loan demand in their markets. Ultimately, these communities would suffer from less credit availability due to FHFA-imposed limits or conditions on FHLBank advances.

III. A member incentive program would be contrary to the Federal Home Loan Bank Act and create an unlevel playing field among member institutions.

The RFI discusses a potential member incentive program that would provide enhanced benefits to members with a "strong and demonstrable" commitment to housing finance and community development.[17] Section 7(j) of the Act explicitly states that the FHLBanks are to treat members "fairly and impartially and without discrimination."[18] An incentive program that provides preferential discounts on advances or differential dividends to members based on FHFA-favored activities would contradict a plain reading of the Act, and it should not be created.

Further, state regulators are concerned that an incentive program would disadvantage a wide range of member institutions. As noted earlier, many depository institutions may have limited demand for FHFA-favored lending activities, but these institutions still rely on FHLBank liquidity to fund credit that fuels economic development in their communities.

Conclusion

State regulators urge FHFA to refrain from issuing a proposed rule to revise the FHLBank System's mission or measurement of that mission, as well as establishing any member incentive program that provides preferential treatment to institutions based on certain activities. These policy objectives are contrary to Congressional directive and intent, and they could limit or condition FHLBank liquidity to the detriment of member institutions and the communities they serve.

Sincerely,

Brandon Milhorn
President and CEO
CSBS

Brian Knight
President and CEO
NASCUS

[16] *Id.* at 11 (Measurement Question 3.b.: "Should all FHLBank advances count as core mission activities, or should there be *limits or exclusions* for advances (or other activity) involving members that have only a limited connection to housing and community development?") (emphasis added).
[17] *Id.* at 7.
[18] 12 U.S.C. § 1427(j). (Each FHLBank's "board of directors shall administer the affairs of the bank *fairly and impartially and without discrimination in favor of or against any member*, and shall, subject to the provisions hereof, extend to each institution authorized to secure advances such advances as may be made safely and reasonably with due regard for the claims and demands of other institutions, and with due regard to the maintenance of adequate credit standing for the Federal Home Loan Bank and its obligations.") (emphasis added).