America's Credit Unions

July 15, 2024

The Honorable Sandra L. Thompson
Director
Federal Housing Finance Agency
Constitution Center
400 7th Street SW
Washington, DC 20219

RE: FHLB Core Mission Activities and Mission Achievement

Dear Director Thompson:

America's Credit Unions and the state credit union leagues (the "Leagues")[1] are writing in response to the Federal Housing Finance Agency's (FHFA's) Request for Input for Federal Home Loan Bank Core Mission Activities and Mission Achievement (RFI).[2] Credit unions often rely on the Federal Home Loan Banks (FHLBs) for liquidity purposes and greatly value their partnerships with the FHLBs. America's Credit Unions and the Leagues appreciate the opportunity to comment on the FHFA's updates to the mission statement, methods for measuring and evolving mission achievement, and financial incentives for members with a strong and demonstrable connection to the mission of the FHLB System.

America's Credit Unions and the Leagues write to express concerns that the proposed changes to the mission statement and the proposed incentive programs will be detrimental to the interest of credit unions. Credit unions depend on the flexibility of the FHLBs to adapt to changing economic conditions and community needs. The proposed changes to the mission statement could limit credit unions' access to liquidity, impose restraints on their ability to offer innovative financial products, and increase compliance costs and administrative burdens. Furthermore, without additional clarification, the proposed incentive program would likely primarily benefit volume lenders and push small community lenders out of the market.

[1] Association of Vermont Credit Unions; Alaska Credit Union League; California Credit Union League; Carolinas Credit Union League; Cooperative Credit Union Association; Cornerstone Credit Union League; Credit Union Association of New Mexico; Credit Union League of Connecticut; CrossState Credit Union Association; Dakota Credit Union Association; GoWest Credit Union Association; Hawaii Credit Union League; Illinois Credit Union League; Indiana Credit Union League; Iowa Credit Union League; Kentucky Credit Union League; League of Southeastern Credit Unions; Louisiana Credit Union League; Maine Credit Union League; Maryland & DC Credit Union Association; Michigan Credit Union League; Minnesota Credit Union Network; Mississippi Credit Union Association; Montana Credit Union League; Nebraska Credit Union League; Nevada Credit Union League; New York Credit Union Association; Ohio Credit Union League; Tennessee Credit Union League; Utah Credit Union Association; Virginia Credit Union League; West Virginia Credit Union League; Wisconsin Credit Union League.
[2] "Request for Input: Federal Home Loan Bank Core Mission Activities and Mission Achievement" (May 16, 2024), https://www.fhfa.gov/sites/default/files/2024-05/FHLBank-Mission-RFI-2024.pdf.

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General Comments

The FHLBs were chartered in 1932, by the Federal Home Loan Bank Act (Bank Act), with a mission "to provide reliable liquidity to member institutions to support housing finance and community investment"[3] (Mission). The RFI expresses concern that, "…its membership base, the types of collateral that can be pledged to secure advances and the FHLBs' product offerings have expanded. As these changes have occurred, the FHLB System's connection to housing and community development has become less direct."[4] We understand and support this concern but believe that ultimately the question of whether the FHLBs' mission requires a refresh is one for Congress. Recent judicial decisions have discouraged regulatory agencies from expanding their authority to questions traditionally in the purview of the legislature. Accordingly, we caution the FHFA against expanding its statutorily prescribed authority to oversee the FHLBs.

To strengthen the FHLB System's connection to housing and community development, the FHFA should focus on the FHLBs' engagement with the credit union industry. Like FHLBs, credit unions are member-owned, not-for-profit financial cooperatives. Credit unions are at the heart of the FHLBs' statutory mission. At the end of the first quarter of 2024, 1,631 credit unions were FLHB members, making up over 25 percent of the FHLB membership.[5] Over its 100-year history, the FHLB system has provided critical liquidity for credit unions, including many smaller community lenders that often do not have access to other sources of low-cost funding, especially in stressed market environments. America's Credit Unions and the Leagues support an amendment to the Bank Act that includes credit unions in the definition of "community financial institutions" (CFIs). We want to extend our sincere thanks for the FHFA's support in the "FHLB System at 100: Focusing on the Future" report[6] (FHLB System at 100 Report) to authorize all credit unions below the statutory cap to pledge CFI collateral to secure FHLB advances. However, we urge the FHFA to explicitly support an amendment redefining CFI to include credit unions so that membership and participation in the FHLB system is simplified and parity is established with community banks.

Currently, the Bank Act's definition of a CFI only includes members whose deposits are insured under the Federal Deposit Insurance Act;[7] this definition excludes credit unions because they are insured by the National Credit Union Administration (NCUA) under the Federal Credit Union Act or another insurer approved by their primary regulator, not the Federal Deposit Insurance Act. Structurally, credit unions are bound to a mandate to serve their communities because they are not-for-profit, member-owned financial cooperatives and are only allowed to serve their defined fields of membership. Due to this unique structure and the significant legal

[3] *See* FHLBanks' Mission, available at https://fhlbanks.com/mission.
[4] "Request for Input: Federal Home Loan Bank Core Mission Activities and Mission Achievement," (May 16, 2024), https://www.fhfa.gov/sites/default/files/2024-05/FHLBank-Mission-RFI-2024.pdf.
[5] "Combined Financial Report for the Quarterly Period Ended March 31, 2024," Federal Home Loan Banks (*last accessed* July 7, 2024), https://www.fhlb-of.com/ofweb_userWeb/resources/2024Q1CFR.pdf.
[6] "FHLB System at 100: Focusing on the Future," FHFA, at 44, https://www.fhfa.gov/AboutUs/Reports/ReportDocuments/FHLBank-System-at-100-Report.pdf.
[7] 12 U.S.C. § 1422.

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limitations placed on credit unions to ensure this mission is adhered to, all credit unions are inherently CFIs.

According to the most recent data from the NCUA, dated March 2024, there are 4,315 credit unions with assets under $1.323 billion.[8] Of these, 1,882 credit unions have less than 10 percent of their total assets in mortgage loans and cannot currently qualify for membership without the use of the exception for CFIs.[9] Including credit unions in the definition of CFI would allow more credit unions to make use of the exception to the membership requirement to have 10 percent of total assets in residential mortgages. This access to becoming an FHLB member opens doors to critical liquidity sources and partnerships that can help strengthen smaller credit unions and the communities they serve.

As it pursues its review of the FHLB System, we encourage the FHFA to measure all FHLB activities as mission activity. All actions towards liquidity, affordable housing, and community investment should be counted including programs whose impact may be indirect and whose results may not be easily quantifiable.

Lastly, we have significant concerns that the proposed member incentives will violate the impartiality standards established in the Bank Act and create tiers of membership instead of a level playing field. We see this uneven incentive structure as an invitation for volume lenders to claim special discounts, which will allow them to increase their volume further and draw consumers from community and relationship-based financial institutions. The program as proposed is inherently unfair and will result in unequal treatment for smaller institutions with fewer resources to put toward special programs. Further, it violates 12 U.S.C. 1427(j) which requires FHLB Board Directors to "administer the affairs of the bank fairly and impartially."

Mission Statement

America's Credit Unions and the Leagues believe that Congress has adequately stated the FHLBs' mission in the Bank Act, and in subsequent legislation such as the Housing and Economic Recovery Act of 2008 (HERA). We support the FHFA's intent to bring focus back to housing finance and community development but suggest the proper way to do so is through targeted policy enhancements, rather than establishing a mission statement.

12 U.S.C. 1430(a)(2)[10] states that, "A long term advance may only be made for the purposes of, (A) providing funds to any member for residential housing finance; and (B) providing funds to any community financial institution for small businesses, small farms, small agri-businesses, and community development activities." This language requires that the main mission of

[8] NCUA Call Report Quarterly Data (March 2024), https://www.ncua.gov/analysis/credit-union-corporate-call-report-data/quarterly-data.
[9] *Id.*
[10] 12 U.S.C. § 1430(a)(2).

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providing liquidity is inherently tied to the support of housing finance and community development. 12 U.S.C. 1431 lays out the power and duties of the banks, and the roles in which the FHFA Director (Director) would play in each, which indicates that Congress intended to have control over these factors. For example, 12 U.S.C. 1431(a) states, "Each Federal Home Loan Bank shall have power, subject to rules and regulations prescribed by the Director, to borrow and give security therefor and to pay interest thereon, to issue debentures, bonds, or other obligations upon such terms and conditions as the Director may approve, and to do all things necessary for carrying out the provisions of this chapter and all things incident thereto."[11] The specificity of this section, and those following, infer that if Congress had intended to grant the Director the authority to define or redefine the mission statement, that authority would be explicitly delineated. Congress declined to do so.

Administrative law doctrines also suggest the FHFA is exceeding its statutory authority in this instance and should reconsider its effort to establish a mission for the FHLBs. In *West Virginia v. EPA*,[12] the Supreme Court found that the Environmental Protection Agency's imposition of industry-wide changes violated the "major questions doctrine" which states that if Congress intended to give such power to the administrative agency, it must clearly delegate such power. Congress defined the FLHBs' mission in 12 U.S.C. 1430(a)(2) and 1431 and has given no indication that it intended to or now intends to grant authority to the FHFA to further refine or redefine this mission. Even more recently, in *Loper Bright v. Raimondo*,[13] the Supreme Court overturned the long-held *Chevron* doctrine, which required courts to defer to regulators when a statute contains ambiguous language. Even if a court found the statutory language was ambiguous, the FHFA's interpretation of the Bank Act would not automatically receive deference. Litigating the question of whether the FHFA has such authority would be an unnecessary use of time and resources when the FHFA's objectives could be met through policy changes that carry a lower risk of legal challenge.

In October 2022, America's Credit Unions' legacy associations wrote[14] to the FHFA in response to the FHLB System at 100 Report, requesting that no harm be done to the FHLB System as a result of the review. Maintaining a strong FHLB System is important for America's Credit Unions, the Leagues, and our members as the liquidity that the FHLBs provide is critical to credit unions. For example, credit unions utilize the FHLBs' Affordable Housing Programs (AHP) to assist in community development and providing access to credit for minority and low- and moderate-income borrowers. We believe that instituting a dual mission to underscore the

[11] 12 U.S.C. 1431(a).
[12] *West Virginia v. Environmental Protection Agency*, 597 U.S. 697 (2022).
[13] *Loper Bright Enterprises v. Raimondo, Secretary of Commerce*, 603 U.S. ___ (2024).
[14] Credit Union National Association's Letter to FHFA re: Comprehensive Review of the Federal Home Loan Bank System (Oct. 31, 2022), https://media.americascreditunions.org/ext/resources/NewsNow/2022/10-2022/Comment-Letter---FHFA-Comprehensive-Review-of-the-FHLBank-System.pdf; National Association of Federally-Insured Credit Unions' Letter to FHFA re: FHLBank System at 100: Focusing on the Future (Oct. 21, 2022), https://www.nafcu.org/system/files/files/10.21.2022%20Letter%20to%20FHFA%20re%20FHLB%20System%20at%20100.pdf.

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importance of the FHLB System's commitment to housing finance and community development would harm the FHLB System by dividing its interests and creating additional reporting requirements.

Any policy changes, such as altering the valuation of collateral used for FHLB advances or a reduction in liquidity or funding options for the AHP, would have a substantial impact on credit unions' ability to serve their members. Major policy adjustments should be considered from a holistic perspective and should only be adopted after notice and comment rulemaking to ensure a transparent process and opportunity for stakeholder feedback. However, there are more incremental policy steps that can be taken to better realign the FHLBs' activities with the mission that has already been established.

America's Credit Unions and the Leagues support a number of the innovative suggestions made in the FHLB System at 100 Report, including additional support for mission-oriented organizations, streamlining the requirements for the AHP, and enhancing support for voluntary and pilot programs.

More specifically, only a few non-depository Community Development Financial Institutions (CDFIs) and no Puerto Rican Cooperativas have become members of the FHLBs. Those who have joined have difficulty accessing FHLB products and services such as advances. We support the proposed solutions of a regulatory interpretation to clarify how Cooperativas can qualify for membership; developing prudent means of lending to these organizations, including revisiting advance product and collateral offerings; and alternative credit support programs. We would be happy to assist the FHFA in conducting outreach to eligible Cooperativas to encourage FHLB membership and facilitate education and resource sharing.

Another innovation we support is modernization of the requirements for the AHP. The FHFA regulates how FHLBs operate their AHP. Suggested updates to those regulations have included updating the AHP regulatory provisions for revolving loan funds, assessing options for area median income (AMI) flexibility in high-cost areas, and revising certain project compliance and monitoring requirements to increase programmatic efficiency. As member-owned institutions, credit unions operate at a low margin and compliance costs are a significant burden. Any regulatory relief that can be offered would redirect those resources to lending and community investment activities.

Credit unions, like the FHLBs, are community-oriented and have an interest in any voluntary pilot programs focused on vulnerable and underserved communities. We support expansion of these programs and their funding. In fact, previously, one of America's Credit Unions' legacy association supported a pilot program to expand the government-sponsored enterprises' (GSEs) purchases of credit union CDFI residential first mortgages. The FHFA should also consider ways it can enhance the membership of credit union CDFIs in the FHLB System.

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Member Incentive Program

The RFI states, "The purpose of establishing a member incentive program….[is to] allow the FHLBs to provide increased benefits to those members that demonstrate a meaningful commitment to housing and community development activity." The RFI claims that the incentives would be dependent on members' activity in support of the Mission but does not indicate how that activity would be measured or categorized. It further states that the incentives would include at least three categories, including a base category, and two categories that receive enhanced benefits.

Without further clarification and specificity regarding metrics and criteria for the member incentive program, America's Credit Unions and the Leagues oppose the proposed program and strongly encourage the FHFA to consider the potential adverse effects of such a policy. This structure will increase reporting requirements for all lenders, but will be most burdensome on small lenders. Volume lenders have the extensive resources to tailor their activities to obtain benefits on the highest tier level and draw consumers from small, community-based financial institutions to one-size-fits-all loans, which will then be sold to remote servicers. We have previously opposed volume-based discounts for guarantee fees from the GSEs and oppose volume-based discounts for FHLB programs.

12 U.S.C. 1427(j)[15] outlines the duties of the board of directors for each FHLB and states, "Such 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." This language precludes the implementation of an incentive program that would include discounted advance rates or other special treatment for certain members. Offering enhanced benefits for specific behavior is the definition of partial action and favoritism. If the FHFA directed the FHLBs to move forward with such incentive programs, the boards of directors would be placed in the difficult position of refusing or risking violation of 12 U.S.C. 1427(j).

Creating a tiered system which grants added benefits to certain members is inherently unfair and will result in unequal treatment for smaller institutions with fewer resources to put toward special programs. The RFI states that the activities that allow increased benefits should be "dependent on a member's activity in support of the System mission and not on the size of the institution." This gives an automatic advantage to lenders with greater volumes of activity. Neither aspect of the mission benefits from this course of action. While incentivizing volume lenders may rapidly increase housing activity and community development, it will not serve the communities that need assistance the most; credit unions are already serving many of those communities.

[15] 12 U.S.C. § 1427(j).

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Low-income and underbanked areas are more likely to be served by credit unions. In February 2024, the Federal Reserve Bank of Philadelphia released a report, "U.S. Bank Branch Closures and Banking Deserts."[16] Census tracts without a financial institution branch rose 6 percent since 2019, while bank branch closures doubled at the same time. Banks with $10 billion or more in assets created nearly two-thirds (62 percent) of new banking deserts through branch closures. Credit unions were able to "cure" these deserts in about 36 percent of all instances by opening a branch in a tract where one had not previously existed.[17] Credit unions also only closed branches that created a banking desert 8 percent of the time compared to 45 percent for very large banks (with $50 billion or more in assets), 17 percent for large banks (between $10 billion and $50 billion in assets), and 30 percent for community banks (under $10 billion in assets).[18]

Credit unions are more likely to serve consumers who are living hand-to-mouth (described as households with net liquid assets of less than two weeks' income). More specifically, 38.9 percent of households where a credit union is the primary financial institution can be described as living hand-to-mouth, compared to 35.5 percent of households where a bank is the primary financial institution.[19]

The FHFA should further clarify the metrics and criteria for this member incentive program proposal or discard it and instead encourage the FHLBs to find new ways to partner with community-based lenders like credit unions to better serve these communities in need of access to safe and affordable housing that can help build generational wealth for these families. A policy that provides preferential treatment to financial institutions based on volume of activity will result in unequal distribution of assistance, and less favorable benefits for those FHLB members who cannot afford to implement such programs.

Conclusion

America's Credit Unions and the Leagues appreciate the opportunity to comment on this topic. We encourage FHFA to reconsider establishing a dual mission statement and to consider targeted policy initiatives as alternatives. We further believe that the membership incentive tiers would violate the impartiality requirements placed on the boards of directors and encourage utilizing other methods of incentivization. Thank you for the opportunity to submit comments on this RFI.

Sincerely,

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[16] "U.S. Bank Branch Closures and Banking Deserts," Federal Reserve Bank of Philadelphia (Feb. 2024), https://www.philadelphiafed.org/-/media/frbp/assets/community-development/reports/banking-deserts-report-feb-2024.pdf.
[17] *Id.* at 14.
[18] *Id.*
[19] America's Credit Unions calculations using data from Federal Reserve 2022 Survey of Consumer Finances, *available at* https://www.federalreserve.gov/econres/scfindex.htm.

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