

## **CUNA Summary of FHLBank System at 100: Focusing on the Future**

The Federal Housing Finance Agency (FHFA) recently released the report *FHLBank System at 100: Focusing on the Future*. The report is designed to ensure that the Federal Home Loan Banks (FHLBanks) are positioned to continue serving their members and their communities going forward. The report followed rounds of public engagement, including listening sessions and roundtables, in which stakeholders provided feedback on the FHLBank System. CUNA and credit unions from around the country participated in the public engagement sessions, making sure that the comprehensive review of the FHLBank System included the credit union perspective.

The report describes several issues that were raised during the public engagement and includes FHFA's recommendations on addressing those issues. The recommendations include engaging in rulemaking, requesting that Congress amend the Federal Home Loan Bank Act (FHLBank Act), issuing supervisory guidance to the FHLBanks, and performing studies to obtain more data before initiating rulemaking.

The report delivers FHFA's vision that the FHLBanks provide stable and reliable liquidity to FHLBank members and support housing and community development in their districts. The report looks to the future of the FHLBanks through four lenses:

- (1) the mission of the FHLBanks;
- (2) the FHLBanks serving as a stable and reliable source of liquidity;
- (3) the FHLBanks supporting housing and community development; and
- (4) the efficient operation and governance of the FHLBanks.

In the analysis that follows, we have paired objectives identified in the report with FHFA's corresponding recommendations using the report's themes.

It should be noted that the recommendations in the report will require future action and that the report, by itself, does not implement any changes in the FHLBank System. With the release of the Fall 2023 regulatory agenda, we will get a better sense of how quickly FHFA intends to move on some of the recommendations in the report. We wanted to provide this detailed analysis to get credit unions thinking about how they use the FHLBank System and how some of these recommendations may impact their use of the System.

### Mission of the FHLBank System

FHFA Objective	Recommendation From Report
<p>Clarifying that the mission of the FHLBanks is to provide liquidity to members and support housing and community development.”</p>	<p>Rulemaking that clarifies the mission of the FHLBanks. Existing mission described in Core Mission Activities regulation is not as direct.</p>
<p>Providing a way to evaluate how the FHLBanks achieve mission goals, including support for housing and community development.</p>	<p>Rulemaking that will “provide metrics and thresholds for measuring mission achievement.”</p> <p>FHFA will look at how mission objectives can be considered in examination ratings.</p>
<p>Encouraging FHLBank members to increase their advancement of the housing and community support mission.</p>	<p>Rulemaking and guidance to the FHLBanks regarding incentivizing members “with a strong and demonstrable connection” to the mission with benefits like better advance rates or dividends on capital stock.</p>
<p>Injecting more transparency into the assessment of a district’s needs, planning, and reporting of achievements.</p>	<p>Rulemaking and guidance to the FHLBanks about making the Targeted Community Lending Plan requirements “more comprehensive and transparent.” Report suggests “includ[ing] advances, activities under AMA and affordable housing and community development programs, and other business activities.”</p> <p>Guidance to the FHLBanks regarding the evaluation of programs and how to improve reporting outcomes to the public.</p>

### Stable and Reliable Source of Liquidity

FHFA Objective	Recommendation from Report
Clarifying that the FHLBanks are not lenders of last resort.	<p>Guidance to the FHLBanks regarding working with members and their prudential regulators to ensure that large depository institutions can borrow from the Federal Reserve discount window when the institutions are in a weakened financial condition.</p> <p>Supervisory expectation for the FHLBanks to establish agreements with the appropriate Federal Reserve Banks regarding movement of collateral when an FHLBank member needs to borrow from the discount window.</p>
Ensuring that large debt issuances do not distort and influence the cost of advances, making it more expensive for FHLBank members to borrow.	FHFA plans “to limit large issuances that unduly raise debt clearing costs or debt issuance activity.” The intent is to prevent a single borrower from negatively impacting other FHLBank members.
Improving ability to fund short-term liquidity demands of FHLBank members.	Rulemaking to treat funds held in interest-bearing deposit accounts at large domestic banks like overnight fed funds sales. Existing regulation has a higher credit limit for overnight fed funds sales, even though they have similar maturities.

FHFA Objective	Recommendation from Report
<p>Enhancing FHLBanks' abilities to evaluate members' creditworthiness.</p>	<p>Guidance to the FHLBanks regarding ongoing evaluations of creditworthiness, including working with members and their prudential regulators to spot issues before they negatively impact members' eligibility to receive an advance.</p> <p>FHFA has already advised that it expects FHLBanks to look at their policies, procedures, and practices related to assessing a member's financial condition.</p> <p>And FHFA indicated that the FHLBanks should have practices in place to facilitate communication between prudential regulators and themselves notifying the FHLBanks of a material decline in financial condition of a member or when "new advances to that member would be counterproductive."</p> <p>FHFA also indicated that it planned to "enhance its oversight of the FHLBanks' credit risk evaluation of their members."</p>
<p>Continuing to deny or limit advances to members without positive tangible capital.</p>	<p>FHFA is not changing its current requirements (i.e., FHLBanks cannot make new advances or renew outstanding ones for a term greater than 30 days to members without positive tangible capital unless prudential regulator requests in writing).</p> <p>FHFA intends "to review and strengthen its policies and guidance to limit access to advances for members with insufficient capital."</p>

FHFA Objective	Recommendation from Report
<p>Reviewing advance prepayment fee requirements for members in poor financial condition.</p>	<p>FHFA plans to study these fees in different conditions. Existing regulation requires assessing prepayment fee on advances with maturities greater than 6 months, even if the borrower fails.</p> <p>May lead to rulemaking shifting responsibility for prepayment fees to FHLBanks or FHLBank System if advance is made to a member in poor financial condition that fails and the advance was made without consulting with the member’s prudential regulator.</p>
<p>Ensuring that the FHLBanks have enough retained earnings to overcome all but the most severe losses.</p>	<p>Through supervision, FHFA intends to advise the FHLBanks to reevaluate and update their retained earnings policies and may take additional action, if necessary.</p>
<p>Improving the FHLBanks’ stress testing.</p>	<p>Rulemaking to adjust stress testing scenarios published by the Federal Reserve to better reflect the risks present in the FHLBank System, which may face different risks from those institutions subject to stress testing under Dodd-Frank.</p>
<p>Making climate resiliency a priority.</p>	<p>Guidance to the FHLBanks to improve their assessment and mitigation of climate-related risks and natural disasters upon their business, members, and communities. Multi-step effort that first requires obtaining and understanding relevant data before analyzing the data through appropriate modeling “to determine how to incorporate climate risk into their risk management frameworks and their targeted housing and community development programs.</p>

## Housing and Community Development

FHFA Objective	Recommendation from Report
<p>Enhancing the engagement of nondepository CDFIs and Cooperativas with the FHLBank System.</p>	<p>FHFA intends to issue a regulatory interpretation explaining how Cooperativas may qualify for FHLBank membership.</p> <p>FHFA may require the FHLBanks to look at how they engage with CDFIs to see whether certain adjustments can be made to product offerings to facilitate lending to these community-based organizations, including:</p> <ul style="list-style-type: none"><li>• Reviewing whether it is necessary to require larger haircuts on CDFI collateral;</li><li>• Implementing credit support options that act to enhance a CDFI's access to advances.</li></ul> <p>FHFA will encourage the FHLBanks to help nondepository CDFI members and depository members interact and address the needs of their underserved communities with the potential for these CDFIs to receive more access to financing through these enhanced relationships.</p>

FHFA Objective	Recommendation from Report
<p>Establishing mission-oriented collateral programs (MOCs).</p>	<p>FHFA expects that the FHLBanks will implement MOCs, which “incentivize[] the use of collateral with a strong connection to the mission of the FHLBank System.” FHFA will review all FHLBank MOC proposals.</p> <p>FHFA may consider rulemaking and guidance as appropriate.</p> <p>FHFA plans to provide the public with more transparency about the collateral pledged by FHLBank members through reporting “the amount and types of MOC pledged in the Report on Collateral Pledged to FHLBanks.”</p> <p>Once MOC programs are implemented, FHLBanks will be expected to encourage the “use of MOC, find risk mitigants for less-liquid, non-standard, or unique MOC, and improve transparency of collateral practices.”</p>
<p>Permitting credit unions and CDFIs to be CFIs and pledge CFI collateral.</p>	<p>FHFA recommends that Congress revise the definition of CFI under the FHLBank Act to include institutions other than those whose deposits are FDIC insured to ensure that credit unions and CDFIs that satisfy the CFI requirements can accrue the benefits of being a CFI under the FHLBank Act.</p>

FHFA Objective	Recommendation from Report
<p>Increasing the relationship between mission activities and advances.</p>	<p>FHFA intends to study whether to change the term for a long-term advance—currently greater than 5 years. Any change to what constitutes a long-term advance could affect when a member could get a long-term advance because the total amount of long-term advances is limited by a member’s residential housing finance assets.</p> <p>FHFA may consider rulemaking to amend the definition of long-term advance depending on the results of the study.</p>
<p>Increasing the use of Community Investment Program (CIP) and Community Investment Cash Advance (CICA) programs.</p>	<p>FHFA and the FHLBanks intend to work together to explore how to expand the use of CIP and CICA.</p> <p>Rulemaking to stimulate CIP/CICA usage by updating the geographically defined targeted beneficiaries in the regulation and addressing targeted income levels.</p>
<p>Increasing the required minimum level of funding for the Affordable Housing Program (AHP).</p>	<p>FHFA recommends that Congress should at least double the minimum AHP contribution required by the FHLBank Act.</p> <p>Until the FHLBank Act is amended, FHFA encourages the FHLBanks to voluntarily contribute more than what is required by the FHLBank Act.</p> <p>FHFA plans to perform research to fully examine the benefits, both direct and indirect, to consumers and communities provided by the FHLBank System. This research may lead to rulemaking “to correct imbalances in the relative value of the public and private benefits provided by the FHLBank System.”</p>



FHFA Objective	Recommendation from Report
Expanding access to AHP.	Rulemaking to streamline requirements and improve access. Potential changes may cover compliance and monitoring requirements, more flexibility for high-cost areas, and revolving loan funds.
Enhancing support for voluntary and pilot programs implemented by the FHLBanks.	<p>Guidance to the FHLBanks setting standards to consider when to initiate a pilot program (e.g., size, scope, duration, etc.).</p> <p>Supervision and oversight will “foster prudent and meaningful use of pilot and voluntary programs to address unmet needs in the communities they serve in a safe and sound manner.”</p>
Providing more support for multifamily housing.	<p>FHFA noted that the FHLBanks could do more to support multifamily housing through core business and pilot programs.</p> <p>FHFA encouraged the FHLBanks to “find innovative ways to increase the production, rehabilitation, and preservation of multifamily housing, particularly smaller multifamily properties.”</p>

FHFA Objective	Recommendation from Report
<p>Strengthening community support requirements.</p>	<p>FHFA will consider tailoring community support requirements “based on member type and mission orientation.”</p> <p>FHFA will review requirements before engaging in rulemaking that could require more information from members about how they support first-time homebuyers and “establishing additional standards that demonstrate support for multifamily housing or community development.”</p>
<p>Enhancing Acquired Member Assets (AMA) program and adding affordable housing goal.</p>	<p>FHFA encourages the FHLBanks to collaborate with their members to develop safe and sound AMA products that are tailored to their communities and local credit needs or address gaps in the secondary market (e.g., purchase/renovation loans in distressed neighborhoods where rehabbed valuation may not be supported by current appraisals, small multifamily properties, and “reuse of commercial properties to support housing finance and community development.”).</p> <p>Rulemaking to add minority census tract goal to affordable housing goals like the enterprises’ minority census tract subgoal.</p>

## FHLBank System Operational Efficiency, Structure, and Governance

FHFA Objective	Recommendation from Report
<p>Making the FHLBank System more operationally efficient.</p>	<p>FHFA noted that the FHLBanks should collaborate to create System-wide efficiencies by creating centers of excellence that can foster operational efficiency across multiple districts (e.g., eNotes acceptance, climate resiliency, affordable multifamily housing, Native American and tribal community support, etc.).</p> <p>FHFA will study whether the districts should be realigned or consolidated to improve efficiency. FHFA will implement periodic reviews regarding realignment. Depending on outcomes of reviews, FHFA may need to recommend that Congress amend the FHLBank Act if the optimal number of districts dips below the minimum number of districts permitted by the Act (8 districts).</p>
<p>Ensuring that members continue to support the FHLBank mission as they obtain new financing.</p>	<p>Rulemaking that will “require that certain members have at least 10 percent of their assets in residential mortgage loans or equivalent mission assets (including assets that qualify as CFI collateral where appropriate) on an ongoing basis to remain eligible for FHLBank financing.”</p> <p>FHFA intends to monitor membership requirements “and may consider harmonizing the manner in which membership eligibility requirements are applied to the different membership types and ensure that advance terms and pricing are not manipulated by members with access to multiple FHLBanks.”</p>

FHFA Objective	Recommendation from Report
<p>Assessing member eligibility requirements.</p>	<p>FHFA intends to study member eligibility requirements. Could lead to rulemaking to ensure that members support the FHLBank mission (e.g., requiring all applicants “demonstrate a measurable and ongoing commitment to housing finance,” standardizing financial documentation for application, and requiring higher compliance standards for certain membership requirements).</p> <p>If Congress were to expand membership eligibility to certain entities that are not currently eligible for membership such as nonbank mortgage companies and real estate investment trusts (REITs), “FHFA recommends that such entities be subject to membership requirements that currently apply to most members including: (1) inspection and regulation, (2) community support or service requirements, and (3) the requirement that 10 percent of their assets be in residential mortgage loans or an equivalent mission asset or activity requirement.”</p>
<p>Ensuring parity between members who have membership in more than one district and those who are members in a single district.</p>	<p>FHFA will monitor the effects that multidistrict members have on the FHLB System.</p> <p>FHFA encourages the FHLBanks to share information about the borrowing activity of multidistrict members.</p> <p>Guidance to the FHLBanks regarding multidistrict membership will be provided, as necessary.</p>

FHFA Objective	Recommendation from Report
<p>Determining the optimal size for boards of FHLBanks.</p>	<p>FHFA will study optimal board size for governance of FHLBanks and may recommend that Congress amend the FHLBank Act, if necessary, including the potential removal of the grandfather provision that requires representation for states at 1960 levels “regardless of whether members in the state have sufficient required stock holdings to warrant that number of seats today.”</p>
<p>Strengthening the composition of FHLBank boards.</p>	<p>FHFA plans to:</p> <ul style="list-style-type: none"> <li>• Expand what constitutes qualifying experience for regular independent directors “to reflect business developments in housing finance and new and emerging risks and complex problems;”</li> <li>• Urge the FHLBanks to identify gaps in skills, backgrounds, experience, and knowledge and nominate individuals to fill those gaps;</li> <li>• Clarify that public interest director nominees’ qualification requirements “must include advocating for, or otherwise acting primarily for the direct benefit of, consumer or community interests;”</li> <li>• Make it easier to nominate people with technical subject matter expertise, including people who do not live in the district (Note: FHFA would need to recommend that Congress revise the FHLBank Act to permit this along with other flexibilities that might be needed).</li> </ul>

<b>FHFA Objective</b>	<b>Recommendation from Report</b>
<p>Align executive compensation with the public purpose of the FHLBanks rather than with commercial banks.</p>	<p>FHFA recommends that Congress amend the FHLBank Act so that it has the “authority to prescribe levels or ranges for the compensation of executive officers of the FHLBanks.”</p> <p>Rulemaking to set forth that mission performance is “a core responsibility of the board.” The intent is to tie mission performance and mission activity to executive incentive compensation.</p>