FHLB System at 100: Summary of Final Report

Starting in August 2022, FHFA launched a comprehensive review of the FHLB System in order to ensure that the FHLBanks are well positioned to fulfill their mission going forward. FHFA defines that mission as one that will ensure the safety and soundness of the FHLBanks as they efficiently provide stable and reliable funding to creditworthy members and support the housing and community development needs of the communities their members serve.

More than a year later, FHFA released its final report that outlines the actions it intends to pursue based on their findings and from stakeholder feedback. The report categorizes its findings under four broad themes:

1. Mission of the FHLBank System
2. Stable and reliable source of liquidity
3. Housing and community development
4. FHLBank System operational efficiency, structure and governance.

Within each theme, FHFA describes future plans to address various issues that the agency argues will better allow the FHLBanks fulfill their mission. Below is a list of these recommendations and actions that ICBA believes will especially impact community banks and will be our main focus as we advocate on your behalf.

1. **FHFA will begin evaluating the FHLBanks based on a measure of their mission achievement**, specifically their core mission activities (CMA) related to housing and community development activities.

   FHFA plans to issue a proposed rule that would clarify the mission of the FHLBanks and provide metrics and thresholds for measuring mission achievement. This proposed rule will also attempt to establish an incentive structure for FHLBank members to support the FHLBank Mission. Additional rulemakings will attempt to set up benefits to members that can demonstrate a strong connection to this mission – likely in the form of discounted advance rates or differential dividends on capital stock.
   ICBA Position: While ICBA supports the FHLB mission, we are concerned that community banks could be negatively impacted by differential pricing of advances or dividends. Some community banks may not be able to generate sufficient mission related collateral needed to get preferred pricing.

   FHFA will attempt to enhance the scope of the Targeted Community Lending Plans while amending the regulation governing Community Support Requirements (CSR) and providing additional guidance to the FHLBanks.
   ICBA Position: ICBA is concerned that these reports could negatively impact a particular community bank even though that bank has a strong CRA record and is a major contributor to the well-being of the communities they serve.

2. **FHFA plans to take steps to ensure members continue to support the FHLBank mission.** This includes a future rulemaking to require that certain members have at least 10 percent of their assets in residential mortgage loans or equivalent mission assets on an ongoing basis to remain eligible for FHLBank financing. FHFA does not define which members this will impact.

ICBA Position: ICBA has long opposed an ongoing 10% test regarding the level of mortgage assets community banks retain in portfolio.

3. **FHFA encourages the FHLBanks to voluntarily increase their Affordable Housing Program (AHP) contributions to at least 20 percent and will recommend Congress consider amending the Bank Act to at least double the minimum required annual contribution.** It is important to note that FHFA does not have the authority to raise this requirement without Congressional approval.
ICBA Position: Most FHLBs have routinely exceeded the minimum AHP contribution of 10% of net earnings. However, FHFA's authority to pressure the FHLBs to increase that contribution to 20% is questionable. Further ICBA is concerned that mandating 20% AHP contribution could negatively impact the costs of advances or other services which community banks depend on.

4. **FHFA defers to Congress to address whether or not to expand membership to the FHLBanks.** FHFA highlights the importance of requiring currently ineligible entities (such as non-bank mortgage companies or mortgage REITs) be subject to appropriate regulation and requirements applicable to current members.
ICBA Position: ICBA does not support the expansion of FHLB membership to non-bank lenders and REITs.

5. **FHFA may use its authority to consolidate the FHLBanks if deemed necessary.** Under the Bank Act, the FHLBank System must consist of between eight and twelve districts. FHFA will review the issue in the near term and establish a protocol for regular periodic reviews to determine whether districts should be re-aligned.
ICBA Position: Except in the case of the possible failure of a FHLB, FHFA's authority to consolidate the system in limited by the statute. Any discussions regarding consolidation of FHLB districts must rise up from the members of those bank districts and not from FHFA.

6. **FHFA is initiating multiple actions to strengthen member risk management.** This is, in part, driven by the market disruption and bank failures earlier this year. FHFA is directing the FHLBanks to revisit their policies and procedures for evaluating the financial conditions of their members. FHFA also emphasizes the importance of working with members' primary regulators to harmonize protocols.
ICBA Position: ICBA supports efforts to ensure the FHLB system remains safe and strong. However, we are concerned that FHFA is trying to insert itself as another prudential banking regulator which will add additional cost and regulatory burden to community banks.

7. FHFA plans to issue guidance for the FHLBanks to begin incorporating climate resiliency efforts into their core businesses, as well as in their AHP and voluntary and pilot programs.
ICBA Position: The FHLBs have always managed credit and collateral risk very well. Climate and weather-related risks within the FHLB districts are naturally a part of that process. FHLBs should not be forced to undertake expensive and questionable risk management initiatives that could result in higher costs for members.

8. **FHFA addresses and reinforces its decision to deny advances to members without positive tangible capital.** FHFA will provide additional guidance that the FHLBanks should work with the member's primary federal regulator in these situations.
ICBA Position: ICBA has called on FHFA to align its tangible capital rule with the prudential banking agencies.

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There are numerous other potential actions and recommendations listed in the report. They include, but are not limited to:

1. Requiring additional stress testing for the FHLBanks.
2. Actions to increase support for multifamily lending.
3. The creation of structured pilot and voluntary programs to address unmet needs of the communities.
4. Revisions to AHP regulation to allow more entities to access AHP funds.
5. Increased financing for Community Investment Program (CIP) and Community Investment Cash Advance (CICA) Programs
6. Steps to limit large issuances that unduly raise debt clearing costs or debt issuance activity.
7. Actions to enable FHLBanks to better manage intra-day liquidity and respond to member requests.
8. The allowance of more mission-oriented institutions (such as CDFIs) to pledge Community Financial Institution (CFI) collateral.
9. The alignment of executive compensation with FHLBanks' public purpose.