



**National Association
of Federal Credit Unions**
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NAFCU | Your Direct Connection to Education, Advocacy & Advancement

January 12, 2015

Alfred M. Pollard, Esq., General Counsel
Federal Housing Finance Agency
400 7th Street, SW
9th Floor
Washington, D.C. 20024

RE: Notice of Proposed Rulemaking and Request for Comment on Members of FHLBanks
(RIN 2590-AA39)

Dear Mr. Pollard:

On behalf of the National Association of Federal Credit Unions (NAFCU), the only trade association that exclusively represents federal credit unions, I write to you regarding the Federal Housing Finance Agency's (FHFA) proposed changes to eligibility requirements for Federal Home Loan Bank (FHLB) membership. *See* 79 FR 54849 (September 12, 2014). For the reasons discussed in more detail below, NAFCU strongly opposes the proposed rule and urges its withdrawal.

General Comments

As you are aware, credit unions are not-for-profit, member-owned financial institutions. This structure, as well as over one-hundred years of espousing a member-first philosophy, fosters a culture that prioritizes the well-being of consumers. NAFCU and our members believe that the well-being of consumers begins with an acute attention to making home ownership an achievable goal. As a result, we have always supported *The Federal Home Loan Bank Act's* intention of promoting mortgage lending and ensuring the extension of credit for housing, community and economic development.

Over the past several years, credit union membership in FHLBs has also been increasing as the FHLBs provide an array of valuable services to credit unions, including serving as a vital source of liquidity. In 2007, 11.4% of credit unions were members of an FHLB, representing 61.7% of

total credit union assets. Today, however, 19% of all credit unions are members of an FHLB, and these credit unions represent 75.8% of the total credit union assets and this number continues to grow. This growth of credit union membership in FHLBs only underscores the need to ensure that the eligibility requirements for membership in FHLBs are set appropriately. Unfortunately, this proposal would disenfranchise over 1 million credit union member-owners from receiving the benefits of FHLB resources as their institution's membership would be terminated under the newly proposed requirements.

While NAFCU appreciates FHFA's intention of fostering FHLB's housing finance missions, we believe the current regulatory requirements effectively ensure that FHLB members demonstrate ongoing commitments to mortgage lending in their communities. For example, when an FHLB member borrows an advance, it must provide eligible collateral to secure the advance. Nearly all eligible types of collateral, which are determined by Congress, are related to housing. In addition, current members must certify their active support of housing for first-time homebuyers to the FHFA every two years through the Community Support Statement. Further, FHFA has failed to provide any data or empirical evidence to support its claims that the FHLB system is at risk because some members may not meet the proposed asset percentage requirements on an ongoing basis. Given the sufficient existing requirements, and the lack of statistical support for the proposed changes, NAFCU does not believe FHFA needs to move forward with the newly proposed "ongoing" membership requirements for depository institutions in this rulemaking.

One-Size-Fits-All-Approach

Each credit union has a unique membership with unique characteristics. Accordingly, FHFA's changes to FHLB membership requirements should not be one-size-fits-all; instead, they should provide credit unions and other community institutions with the flexibility necessary to continue to meet their members' needs.

A one-size-fits-all regulation does not take into consideration either the asset size or the experience level of individual credit unions. For example, a credit union may have years of experience with originating mortgage loans that it sells on the secondary market. While such a credit union would satisfy the current regulatory requirement to "originate and purchase" mortgage loans, it would fail to meet the rigid one percent and ten percent standards of the proposal. Should the proposal be finalized, such credit unions would, in many cases, be forced to restrict their activity on the secondary market, thereby cutting off one of their most effective tools for hedging interest rate risks.

Unfortunately, however, FHFA has proposed a rule that would nullify a credit union's experience and the benefits it garners for their members. The rigid one percent and ten percent standards would force credit unions to manage their portfolios to achieve artificial thresholds, rather than meeting the housing finance needs of their members and communities. NAFCU and our members believe the one-size-fits-all approach that FHFA took in this proposal will be counterproductive, unworkable and may lead to unwanted results. As a result, we respectfully urge that FHFA withdraw the proposal.

Alternatively, if FHFA determines to move forward with the proposal, NAFCU urges the agency to provide an asset-based exemption for credit unions akin to what other community depository institutions enjoy. Credit unions and other “exempt” community financial institutions deliver similar housing finance services to their communities and both use FHLB advances to extend credit for their communities’ housing and economic development needs. Despite their similar housing-related functions, credit unions and community banks are treated disparately differently under FHFA’s current membership regulations. Disadvantaging the ability of credit unions to meet the housing needs of their communities, as compared to other community financial institutions, would seem to run contrary to the intention of this proposal. Therefore, NAFCU and our members encourage the agency to establish an asset-based exemption for credit unions parallel the one currently available to community banks.

1% Standard

Generally speaking, an institution must meet six requirements in order to qualify for FHLB membership. One of these requirements mandates that an institution “makes long-term home mortgage loans.” *See* 12 CFR 1263.6(a)(3). Currently, FHFA’s FHLB membership regulation does not require a FHLB to assess compliance with this “makes long-term home mortgage loans” requirement for any institution once it has become a FHLB member.

The proposed rule would make significant changes to the “makes long-term home mortgage loans” requirement. It would establish an ongoing quantitative standard that each institution must meet in order to be deemed to make long-term home mortgage loans. To meet this standard, an institution would have to maintain at least one percent of its total assets in home mortgage loans. The proposal would apply this one percent standard both at the time of initial membership approval and on an ongoing basis. The proposal would also require FHLBs to calculate each member and applicant’s home mortgage loan percentage using three-year averages as of the end of the preceding three calendar years to determine the institution’s compliance with this one percent standard.

NAFCU is concerned that the proposed one percent standard is unnecessarily rigid because it fails to take into account fluctuations that can occur in portfolios due to national changes in the housing market or local economic conditions. As demonstrated by the recent financial crisis, such fluctuations can actually last several years – something this proposal does not seem to take into account. Credit unions should have the flexibility to prudentially adjust their portfolios in response to changing market conditions, and should not be penalized by a regulator for such prudence. Therefore, NAFCU and our members believe the proposed one percent standard is inappropriate, and we encourage FHFA to retain the current “makes long-term home mortgage loans” requirement.

Alternatively, if FHFA determines to move forward with proposed one percent standard, NAFCU recommends that the agency allow mortgage loans that are sold into the secondary market to count towards an institution’s one percent threshold. We believe FHLB members should be allowed to count the amount and percentage of all residential mortgage loans and long-term home mortgage loans made by the FHLB member during each of the three relevant years,

including loans originated that will be or were subsequently sold within the secondary market, towards their one percent threshold.

10% Standard

In addition to its general membership eligibility requirements, FHFA's FHLB membership regulation also requires insured depository institutions, other than community financial institutions (CFIs), to hold at least ten percent of their total assets in residential mortgage loans in order to be eligible for membership in a FHLB. As with the "makes long-term mortgage loans" requirement, the regulation does not require an institution, such as a credit union, that is subject to the ten percent requirement to continue to hold ten percent of its total assets in residential mortgage loans after it becomes a FHLB member.

The proposed rule, however, would extend the ten percent requirement on an ongoing basis, and mandate that an institution continually hold at least ten percent of its assets in residential mortgage loans, in order to maintain its membership in the FHLB. The proposal would also require FHLBs to calculate each member's home mortgage loan percentage using three-year averages as of the end of the preceding three calendar years to determine the institution's compliance with this ten percent requirement.

NAFCU strongly opposes the proposed extension of the ten percent standard. We believe that credit unions should have the flexibility to manage their mortgage portfolios with the best interest of their members in mind, rather than having to manage their portfolios to meet an arbitrary standard. Extending the ten percent standard on an ongoing basis would unnecessarily restrict a credit union's ability to provide the mortgage financing needed by their members and the communities that they serve. Further, applying the ten percent standard to credit unions on an ongoing basis would disadvantage them and their members when compared to other community financial institutions. This new standard would likely slow the growth of credit union membership in FHLBs, and disproportionately hinder the role that credit unions play in meeting the housing needs in their communities – something that would also seem counter to the intention of this proposal.

1% and 10% Standards Contrary to Congressional Intent

NAFCU strongly believes that the proposed asset tests run afoul of Congress' history of expanding FHLB membership and activities. Since the passage of *The Federal Home Loan Bank Act*, Congress has reconsidered and expanded the FHLB System many times. Most notably, the *Financial Institutions Reform, Recovery and Enforcement Act of 1989* expanded FHLB membership to credit unions and commercial banks. In all of its changes to the FHLB System, Congress did not see the need to require continuous testing of membership requirements nor did it see it appropriate to use ongoing asset percentages to demonstrate a commitment to housing finance. NAFCU does not believe that FHFA is in the scope of its statutory authority to do so now.

Automatic Membership Termination

The proposal would also impose a new requirement on FHLBs to determine on an annual basis whether FHLB members properly maintain one percent of their assets in long-term home mortgage loans and ten percent of their assets in residential mortgage loans, based on three-year averages. The proposal would require FHLBs to terminate any member that fails to comply with either asset test after a limited grace period.

NAFCU strongly opposes the proposed requirement on FHLBs to terminate any member that fails to comply with either the one percent or ten percent standards. If the rule is not withdrawn, we would suggest that any member who fails to meet these standards be given a five-year probationary period to re-establish the requisite levels before being terminated. Should they meet these standards at any point during the five years, NAFCU suggests that FHFA allow the FHLB to remove the institution from probation.

Conclusion

Given the onerous nature of this proposal on credit unions, the lack of a Congressional mandate for “ongoing” FHLB membership requirements and the current requirements that already exist for FHLB members to demonstrate a commitment to housing finance, NAFCU must oppose the proposed rule and urge its withdrawal.

NAFCU appreciates the opportunity to provide our comments. Should you have any questions or concerns, please feel free to contact me at anealon@nafcu.org or (703) 842-2266.

Sincerely,

A handwritten signature in cursive script that reads "Alicia Nealon". The signature is written in dark ink and is positioned above the typed name and title.

Alicia Nealon
Director of Regulatory Affairs