

August 7, 2024

Sandra Thompson
Director
Federal Housing Finance Agency
Constitution Center
400 7th Street, SW
Washington, D.C. 20219

RE: Request for Input: Federal Home Loan Bank Core Mission Activities and Mission Achievement

Dear Director Thompson:

The undersigned officials thank you for undertaking your centennial review of the Federal Home Loan Bank System¹ and issuing this Request for Input (RFI) on its Core Mission Activities and Mission Achievement. We agree with the assessment at the beginning of the RFI that FHLBanks should “increase their support for housing and community development” and that clarifying their mission is “an essential step” in that process.

Our constituents need a more direct benefit from the \$1.3 trillion, taxpayer-subsidized Federal Home Loan Bank System (“FHLB” or “System”). The System’s primary lending activity has drifted from supporting housing finance in the public interest to instead increasingly subsidizing excessive private profit. We support FHFA’s intention to rewrite the mission of the FHLBanks and believe that mission must explicitly ensure that the System’s central business practice – the extension of advances to members – directly supports affordable housing and community development. Below, we suggest recommendations for revising the System’s mission and making it more effective in advancing its objectives.

The Federal Home Loan Banks were established in the Great Depression “as a new source of funding for mortgage lenders.”² At inception, collateral to borrow from FHLBanks was limited to home mortgages secured by real estate valued under \$20,000.³ Much has changed since then.

¹ U.S. Federal Housing Finance Agency, “FHLBank System at 100: Focusing on the Future”, <https://www.fhfa.gov/PolicyProgramsResearch/Programs/Pages/FHLBank-Focusing-on-the-Future.aspx>

² U.S. Federal Housing Finance Agency, “FHLBank System at 100: Focusing on the Future”, p. 11 <https://www.fhfa.gov/AboutUs/Reports/ReportDocuments/FHLBank-System-at-100-Report.pdf>

³ “Under the original Bank Act, home mortgages having no more than 15 years to maturity and an underlying real estate value of \$20,000 or less were eligible.” U.S. Federal Housing Finance Agency, “FHLBank System at 100: Focusing on the Future”, p. 43 <https://www.fhfa.gov/AboutUs/Reports/ReportDocuments/FHLBank-System-at-100-Report.pdf>

Today, more than 80% of the top 100 FHLB members borrowed more from the System than they loaned out in mortgages, according to an analysis by Bloomberg.⁴ One FHLBank promotes its lending to insurance members this way: “Membership in the Federal Home Loan Bank of Chicago provides access to a reliable funding source for spread investing strategies, with low rates that reflect our status as a government-sponsored enterprise (GSE).”⁵ A portfolio manager summed up the Home Loan Banks’ current role by saying her clients borrowed from the System because “the arbitrage was really attractive.”⁶

Our constituents, who subsidize the Federal Home Loan Banks with their taxes, need the System to produce tangible results for their housing needs, not arbitrage for financial institutions. The problem is demonstrated by insurance firms who access FHLBanks. As noted by the U.S. Treasury Department’s Office of Financial Research in 2022: “Life insurers often use these advances as part of a spread arbitrage program where the advances are reinvested in higher-yielding assets.”⁷ According to Cornelius Hurley, a former Independent Director at the FHLB of Boston, “All (insurers) do is they happen to have some government securities and mortgage-backed securities in their investment portfolios. But they don’t provide any public benefit in return for that.”⁸

As you know, the arbitrage opportunity arises from the Federal Home Loan Banks’ government-sponsored status and its ability to lend to members at low rates. According to your report, *FHLBank System at 100: Focusing on the Future*, those low rates are made possible by the System’s ability to issue debt “at rates only slightly higher than those on comparable Treasury instruments. This ability arises from the joint and several nature of consolidated obligations, as well as the perception that the federal government would provide support in the event of a default by the FHLBanks.”⁹

Through the government’s “implied guarantee” and an exemption from paying most taxes, the Congressional Budget Office (CBO) estimates that the net subsidy to the FHLBs from the federal government will amount to around \$6.9 billion in 2024.¹⁰ That’s about 20 times the \$350 million

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<https://www.bloomberg.com/news/features/2023-06-04/us-effort-to-help-homebuyers-get-affordable-loans-mainly-benefits-banks-instead>

⁵ <https://www.fhlbc.com/solutions/details/spread-investing-strategies-for-insurance-companies-q2-2019> Q2 2019

⁶ <https://www.reuters.com/markets/us/life-insurers-binge-us-financing-aimed-helping-housing-2023-12-05/>

⁷ U.S. Department of Treasury, Office of Financial Research, “Rising Interest Rates Help Insurers, but Market Volatility Poses Risk to Some” p. 2

<https://www.financialresearch.gov/the-ofr-blog/2022/07/21/Rising-Interest-Rates-Help-Insurers-but-Market-Volatility-Poses-Risk-to-Some/>

⁸ <https://www.reuters.com/markets/us/life-insurers-binge-us-financing-aimed-helping-housing-2023-12-05/>

⁹ U.S. Federal Housing Finance Agency, “FHLBank System at 100: Focusing on the Future”, p. 48

<https://www.fhfa.gov/AboutUs/Reports/ReportDocuments/FHLBank-System-at-100-Report.pdf>

¹⁰ Congressional Budget Office, “The Role of Federal Home Loan Banks in the Financial System,” March 7, 2024, p. 2

the CBO estimates FHLBs will contribute to the Affordable Housing Program (AHP) this year.¹¹ The government subsidy ultimately accrues to the System's members, like banks and insurance companies, who get to borrow at lower costs and receive dividends from FHLBanks' profits. In 2023, Federal Home Loan Bank members received \$3.4 billion in dividends.¹²

Therefore, tying borrowing from the Federal Home Loan Banks more directly to housing finance, as you recommend, has the potential to redirect the \$1.3 trillion System toward our national housing crisis.

Our housing crisis can be illustrated in several ways. Nationally, housing costs remain the single biggest driver of inflation, accounting for more than two-thirds of the monthly inflation increase in January 2024.¹³ Rent prices remain high,¹⁴ after an historic 15% spike between 2020 and 2022.¹⁵ The rent spike is a major reason a record number of Americans pay more than 30% of their income on housing.¹⁶

The precipitous rise in standard mortgage rates, which peaked close to 8% last year and are still double what they were in late 2021, further exacerbates the crisis.¹⁷ High mortgage rates and high home prices have chilled the home purchase market and created a vicious circle: it is harder for families to achieve their dream of homeownership, which also pushes up demand and prices in the rental market.

These dual housing crises come during a period of record borrowing from the Federal Home Loan Banks by members,¹⁸ expanding the balance sheet and profits of the FLHB System and illuminating the disconnect between FHLB lending and effective liquidity for housing.

https://www.cbo.gov/publication/59712?utm_source=feedblitz&utm_medium=FeedBlitzEmail&utm_content=812526&utm_campaign=Express_2024-03-07_14:30:00&utm_medium=FeedBlitzEmail&utm_content=812526&utm_campaign=Express_2024-03-07_14:30:00

¹¹ Congressional Budget Office, "The Role of Federal Home Loan Banks in the Financial System," March 7, 2024, p. 2 https://www.cbo.gov/publication/59712?utm_source=feedblitz&utm_medium=FeedBlitzEmail&utm_content=812526&utm_campaign=Express_2024-03-07_14:30:00&utm_medium=FeedBlitzEmail&utm_content=812526&utm_campaign=Express_2024-03-07_14:30:00

¹² FHLBanks Office of Finance Announces Fourth Quarter and Annual 2023 Combined Operating Highlights for the Federal Home Loan Banks, 2/23/24

https://www.fhfb-of.com/ofweb_userWeb/resources/2023Q4FHLBCombinedOperatingHighlights.pdf

¹³ <https://www.bls.gov/news.release/cpi.nr0.htm>

¹⁴ https://www.jchs.harvard.edu/sites/default/files/reports/files/Harvard_JCHS_Americas_Rental_Housing_2024.pdf

¹⁵ <https://www.washingtonpost.com/business/interactive/2023/rent-prices-coming-down-near-me/>

¹⁶ https://www.jchs.harvard.edu/sites/default/files/reports/files/Harvard_JCHS_Americas_Rental_Housing_2024.pdf

¹⁷

<https://www.bloomberg.com/news/articles/2024-02-14/us-30-year-mortgage-rate-climbs-to-a-two-month-high-of-6-87>

¹⁸ U.S. Federal Housing Finance Agency, "FHLBank System at 100: Focusing on the Future", p. 2 <https://www.fhfa.gov/AboutUs/Reports/ReportDocuments/FHLBank-System-at-100-Report.pdf>

One example of the disconnect between the System and its housing mission is illustrated by Athene Annuity and Life Company (“Athene”), a wholly owned subsidiary of private equity giant Apollo Global Management. As of the first quarter of 2024, Athene was the second largest borrower of the FHLB of Des Moines, with \$7.6 billion in outstanding advances.¹⁹ These borrowings “were issued in an investment spread strategy, consistent with other investment spread operations,” according to Apollo.²⁰

Moreover, Athene (the FHLB of Des Moines member) is a wholly owned subsidiary of a Bermuda-based reinsurer called Athene Annuity Re Ltd.²¹ In 2023, a majority of Athene’s aggregate capital was held by its Bermuda reinsurance entities.²² There are tax and regulatory advantages for insurers based in Bermuda,²³ raising concerns for us about the offshoring of the benefits of the FHLB System.

Currently, collateral requirements for FHLB advances do not support the System’s housing mission. Collateral is permitted to include any real estate related assets, residential or commercial, including residential mortgage-backed securities (RMBS), commercial MBS, whole loans, and government securities. Owning RMBS to pledge as FHLB collateral is not additive in the housing finance market nor evidence of mission support, because RMBS is a \$10 trillion,²⁴ highly liquid market, already dominated by other government sponsored enterprises. Today, around 65% of mortgage debt in the United States is securitized into MBS, most of it agency MBS that is guaranteed by Fannie Mae, Freddie Mac, or Ginnie Mae.²⁵ We do not believe that leveraging MBS as eligible collateral contributes to mortgage affordability, housing supply, or community development and resilience.

¹⁹ Apollo Global Management, Form 10-K for period ending 12/31/2023, filed 3/1/2024, p. 108
<https://www.sec.gov/ixviewer/ix.html?doc=/Archives/edgar/data/1858681/000185868124000031/apo-20231231.htm>

²⁰ Apollo Global Management, SEC Form 10-Q, 9/30/2023, p. 181
<https://www.sec.gov/ix?doc=/Archives/edgar/data/1858681/000185868123000042/apo-20230930.htm> and Athene Holding Ltd 2022 10-K p. 109: “We have issued funding agreements to the FHLB. These funding agreements were issued in an investment spread strategy, consistent with other investment spread operations.”
https://www.sec.gov/Archives/edgar/data/1527469/000152746923000014/ahl-20221231.htm#i516596e310ab4972ac56ca0735e8d119_70

²¹ Athene Annuity & Life Assurance Company of New York, Schedule Y of Annual Statement for the Year 2022 submitted to New York Department of Insurance, p. 53.136. Athene Annuity and Life Company of Iowa is owned 100% by Athene Annuity & Life Assurance Company of Delaware, which is owned 100% by Athene Annuity Re Ltd., a Bermuda company.

²² Apollo Global Management 10-K Report to the Securities and Exchange Commission for the period ending 12/31/2023, p. 22
<https://www.sec.gov/ix?doc=/Archives/edgar/data/1858681/000185868124000031/apo-20231231.htm>

²³ Foley-Fisher, Heinrich, and Verani “Are Life Insurers the New Shadow Banks?” April 2023, pp. 14-16
<https://ssrn.com/abstract=3534847>

“Therefore, the premiums collected by the Bermuda captive from its affiliated US insurer are tax exempt and US insurers can claim the premiums paid to its Bermuda captive as an expense.”

²⁴ https://www.newyorkfed.org/research/staff_reports/sr1001.html

²⁵ Fuster, Andreas, Lucca, David, and Vickery, James, “Mortgage-Backed Securities.” (Federal Reserve Bank of New York, 2022), https://www.newyorkfed.org/medialibrary/media/research/staff_reports/sr1001.pdf.

Moreover, there is no publicly available data that tracks how much money is borrowed by which institutions nor the types of collateral used to back FHLB advances, despite the System’s government-sponsored status and the public’s “implied guarantee.” The lack of transparency further obscures the housing mission that should be at the heart of FHLB lending and enables FHLBs to undercut the Federal Reserve’s role as lender of last resort by not disclosing the identity of borrowers and the amount of their borrowings in a timely manner.²⁶

We understand the Council of FHLBs seeks to maintain the status quo, in which FHLBanks provide liquidity for liquidity’s sake and act as a lender of last- or second-to-last resort, as it has recently argued to the Federal Deposit Insurance Corporation.²⁷ In addition to centering FHLB’s housing mission, we agree with your report that “[t]he role of the FHLBanks in providing secured advances must be distinguished from the Federal Reserve’s financing facilities, which are set up to provide emergency financing for troubled financial institutions confronted with immediate liquidity challenges.”

We believe the status quo is not good enough.

If our constituents are subsidizing the Federal Home Loan Banks and their members’ borrowings, then those borrowings should directly benefit the housing needs of American families – the very mission and original purpose of the FHLB System. To that end, we propose the following recommendations in answer to your RFI:

Answers to RFI Mission Questions

Mission Question One: How should the mission statement for the FHLBanks reflect the connection between the liquidity provided by the FHLBanks and their support for housing and community development?

1. We recommend revising the FHLB’s mission statement to state: The mission of the FHLBanks is to provide liquidity *for* unmet credit needs in the markets for residential housing and community development, including affordable housing, through lending to members for this public purpose. All of the FHLBanks’ resources should further this mission, consistent with sound credit management, with appropriate exceptions for small member institutions for whom general liquidity is a critical need.

They should accomplish this mission through:

²⁶ Steven Kelly, Susan McLaughlin, and Andrew Metrick “FHLB Dividends: Low-Hanging Fruit for Reconfiguring FHLB Lending” Yale School of Management Program on Financial Stability. January 18, 2024. <https://som.yale.edu/story/2024/fhllb-dividends-low-hanging-fruit-reconfiguring-fhllb-lending>

²⁷ In a letter to the Federal Deposit Insurance Corporation (FDIC), the Council of FHLBs argued that “the longstanding role of emergency lender for the FHLBanks to address run contagion and provide a liquidity backstop for the deposit insurance funds should not be disrupted.”

<https://www.fdic.gov/resources/regulations/federal-register-publications/2023/2023-resolution-plans-required-idi-100-billion-more-total-assets-3064-af90-c-005.pdf>

- a. Using FHLBanks' balance sheets and excess capital that exceeds regulatory capital requirements to support and provide liquidity for housing and community development in underserved markets.
- b. Offering direct financial support to subsidize homeownership opportunities and affordable rental housing and community development projects that benefit low- and moderate-income households and households of color in underserved communities, over and above Affordable Housing Program contributions.

Measurement Question Three: In developing multiple measurements, what additional aspects of mission achievement should FHFA assess? What additional measurements should FHFA adopt to assess support for housing and community development, including support for lower income households or other groups with identified needs?

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? How might this be measured? Should the type of collateral securing an advance be considered in evaluating advances? (Alternatively, this type of approach could be used for calculating one or more additional measurements.)

2. As the primary activity of FHLBanks is making advances to members, we believe advances must be directly used for housing and community development needs. Therefore, we urge FHFA to require collateral for advances that reflect a revised mission for FHLB, that is assets serving unmet credit needs in housing and community development. We propose that collateral backing advances be bifurcated to ensure mission use of advance proceeds: (1) strict "mission collateral" equal to the amount of advances, excluding highly liquid RMBS and other non-residential loans, and (2) "risk collateral," such as commercial and residential MBS or other allowable real estate and government loans providing liquid security to satisfy FHLB's risk and liquidity needs. FHFA should define "mission collateral" to appropriately align advances with the FHLB's revised mission.
3. We also recommend amending the definition of "long-term advances," which must be used for housing finance by statute, in order to tie more proceeds of member borrowings to unmet credit needs in housing directly. Rules like these could aim more of the lending power of FHLBs to its housing mission:
 - a. We agree with your report proposing to define "long-term advances" as greater than 1 year maturity, down from 5 years, to increase the portion of FHLB lending serving its housing mission.

- b. Additionally, we propose strengthening the “proxy test” used to prove that long-term advances meet the statutory requirement by considering only mission-specific housing assets defined similarly to assets that count as “mission collateral” as discussed above.²⁸
 - c. We propose to exclude small banks, community financial institutions, and community development financial institutions (CDFIs) from these stricter borrowing terms to preserve their access to FHLB liquidity.
4. Central to measuring the mission use of FHLB advances is the need for public disclosure of member borrowing on a reasonable schedule. We propose adopting standards of disclosure similar to borrowing from the Federal Reserve Discount Window. We believe disclosure will encourage mission use of advances by members, provide accountability to FHLB’s public purpose, and support FHFA’s goal to “Ensure FHLBanks are not the Lender of Last Resort”²⁹ by bringing transparency to member borrowing on par with Federal Reserve.

Measurement Question Five: Are there other approaches FHFA should consider?

5. We urge you to consider rulemaking that would prevent foreign-owned entities from borrowing from Federal Home Loan Banks, including insurance companies with foreign-domiciled parent entities and foreign-owned banks. Even as the FHFA seeks to rebalance the benefits of the FHLB System from private profit to its public purpose, all benefits of the government subsidized system should remain in the United States.
6. We support your recommendation to increase the percentage of System profits that are contributed to the Affordable Housing Program from 10% to at least 20% by seeking Congressional action to amend the statute.
 - a. We further encourage you to offer rulemaking to cap dividends from FHLBanks to their members at a level equal to their Affordable Housing Program contributions to incentivize FHLBanks to implement a more balanced use of System profits.

The recommendations above would aim more of the lending activity and profits of the FHLB System toward urgent, unmet credit needs in housing, while ensuring that foreign-owned companies are not reaping the benefits of this taxpayer-subsidized System.

²⁸ U.S. Federal Housing Finance Agency, “FHLBank System at 100: Focusing on the Future”, p. 44-45
<https://www.fhfa.gov/AboutUs/Reports/ReportDocuments/FHLBank-System-at-100-Report.pdf>

²⁹ U.S. Federal Housing Finance Agency, “FHLBank System at 100: Focusing on the Future”, p. 31
<https://www.fhfa.gov/AboutUs/Reports/ReportDocuments/FHLBank-System-at-100-Report.pdf>

Thank you for undertaking this mission review. Borrowings from the Federal Home Loan Bank System can and should be used to address unmet residential housing and community development needs, in turn helping our constituents see concrete relief in their housing costs.

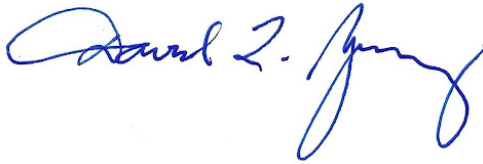
Signed,

A handwritten signature in black ink, appearing to be 'Zachary B. Conine', with a long horizontal stroke extending to the right.

Nevada State Treasurer Zachary B. Conine

A handwritten signature in black ink, appearing to be 'Colleen C. Davis', written in a cursive style.

Delaware State Treasurer Colleen C. Davis

A handwritten signature in blue ink, appearing to be 'David L. Young', written in a cursive style.

Colorado State Treasurer David L. Young

A handwritten signature in black ink, appearing to be 'Michael Frerichs', written in a cursive style.

Illinois State Treasurer Michael Frerichs

A handwritten signature in black ink, appearing to be 'Fiona Ma', written in a cursive style.

California State Treasurer Fiona Ma