November 26, 2024

Submitted Electronically
Clinton Jones, General Counsel
Attention: Comments/RIN 2590–AB41
Federal Housing Finance Agency
400 Seventh Street SW
Washington, DC 20219

Re: Comments on the Notice of Proposed Rulemaking on Unsecured Credit Limits for Federal Home Loan Banks RIN 2590–AB41

Dear Mr. Jones,

The Federal Home Loan Banks (FHLBanks) listed below and the Federal Home Loan Banks Office of Finance (OF and, together with the FHLBanks, the FHLBank System) respectfully submit the following comments on the FHFA's proposed rule on Unsecured Credit Limits for Federal Home Loan Banks. The FHLBanks support aspects of the FHFA's proposal which, if finalized, would align restrictions on unsecured credit exposure to interest bearing deposit accounts to the current restrictions on exposure to overnight federal funds. The FHLBanks are concerned with other aspects of the proposed rule, which would increase operational risks and be costly and time-consuming to implement.

The FHLBanks support the FHFA's position to treat interest bearing deposit accounts (IBDAs) in an equitable manner to overnight federal funds and increase the FHLBanks' flexibility to manage liquidity positions. The FHLBanks believe that the risk profile of IBDAs are comparable to, if not better than, overnight federal funds given the readily available, on demand nature of IBDAs and priority of such deposits over unsecured senior obligations of the banking counterparty. Permitting the FHLBanks to increase their exposure to IBDAs will help the FHLBanks to manage the amount of liquidity that the FHFA requires the FHLBanks to carry on their balance sheet.

Capital measurement

The FHLBanks strongly disagree with the FHFA's inclusion of a new calculation to determine maximum unsecured credit exposure limits in 12 C.F.R. § 1277.7(a)(1)(i). The proposed rule states that capital used to determine maximum unsecured credit exposure be the "lesser of the daily total or the most recent month end." The FHLBanks currently typically rely on a prior month-end capital calculation to determine transactional limits and do not have a readily available daily capital calculation that is subjected to the same level of reconciliation and scrutiny as month-end capital calculations. Adding the requirement of a daily capital calculation would add operational challenges, increase costs for updating systems, require revised trading guidelines and processes, and introduce uncertainty with FHLBank trading counterparties. Any daily capital calculations an FHLBank may currently use are typically an estimate of capital that represent daily updated stock balances only, and do not include the full range of general ledger impacts needed to accurately and completely report retained earnings and accumulated other comprehensive income. The proposed rule would add accounting challenges for the FHLBanks, as retained earnings and accumulated other comprehensive income positions are not otherwise required to be calculated and validated daily under generally acceptable accounting practices.

The FHFA states that it "does not expect that the proposed clarification would require the Banks to make any changes to their current methods of calculating month-end capital or daily capital." However, instituting a requirement to use the lesser of the daily and the month-end capital calculations would expressly require FHLBanks to perform daily what is currently a multi-day monthly close process. Such a change to the FHLBanks' current capital calculation methodology, a significant departure from historical practices among the FHLBanks, would require a lengthy and costly re-engineering of its systems, staffing and processes. The FHLBanks note that the FHFA has not provided a reason or stated a benefit to adding the concept of applying the lesser of the two limits, and the FHLBanks do not believe that any potential benefit would outweigh the operation risk or burden such requirement would introduce.

Additionally, utilizing the lesser of the two capital measurements for unsecured credit limits introduces inconsistency and confusion in, and compliance burdens with, the application of FHFA regulations. For example, the concept of a daily capital calculation is inconsistent with FHFA's regulation regarding the FHLBank investments in mortgage-backed securities, which utilizes the prior month-end capital figure to calculate maximum mortgage investment exposure for the FHLBanks.

The FHLBanks request that the FHFA maintain the regulation's current approach for measuring total capital for the purpose of determining unsecured credit limits.

Intraday exposure and definition of authorized overnight investments

The FHLBanks partly disagree with the FHFA's new requirement to monitor intraday unsecured credit exposure. Many FHLBanks use an increasingly smaller number of financial service providers for secured and unsecured credit transactions, including a combination of correspondent bank services, settlement services, safekeeping, payroll, business depository services, capital markets transactions (including functions related to funding and hedging, repurchase agreement transactions, settlement services, cleared derivatives, cleared repo, and broker/dealer services), and other financial transactions. Depending on the service provided, most, if not all, of these third-party providers do not have the technology available to provide verifiable intraday unsecured credit exposure data to the FHLBanks. Calculating and monitoring intraday exposure across all financial service providers without appropriate exclusions to recognize the purpose of the underlying transactions, as contemplated by the proposed regulation, would require a major operational and technological effort from the FHLBanks that would result in significant strain on IT and business resources. Further, it remains unclear whether real-time monitoring of some of the services mentioned above is achievable with the information provided by other financial entity counterparties or service providers. Additionally, any benefit in reduction to the risk position of the FHLBanks is theoretical. To date, the FHLBanks have not suffered a loss due to an intraday exposure in excess of unsecured credit limits. The requirement of intraday credit monitoring is an operational and compliance burden on the FHLBanks that does not support any theoretical benefit in managing potential credit exposure. The FHLBanks request that the current rule stay in place, which requires the FHLBanks to be in compliance with unsecured credit limits at the close of each business day.

As the FHFA states in the proposed regulation "overnight Fed Funds and reverse repos are returned to a Bank from the counterparty the next trading or banking day and often require a trade commitment early in the day". First, the FHLBanks note that reverse repos are secured transactions and do not introduce unsecured credit risk to the FHLBank. However, with respect to IBDAs and Fed Funds, the FHLBanks already monitor, and commit to continuing to monitor intraday unsecured credit exposure by ensuring that unsecured funds from the previous day's transactions are returned prior to the release by the FHLBanks of funds related to the current day's transaction.

Accordingly, as explained above, the intraday monitoring is already an activity performed by the FHLBanks with respect to IBDAs and Fed Fund transactions to remain within established unsecured

credit limits. However, the FHLBanks respectfully request that the FHFA remove "unsecured deposits in non-interest bearing deposit accounts such as settlement, payroll, or other transaction accounts" from its proposed definition of "authorized overnight investments" [emphasis added]. Balances in these types of accounts are not "extensions of unsecured credit" for the purpose of earning a return on liquidity investments, unlike, for example IBDAs and Fed Funds sold. The FHLBanks believe that the banking institutions that provide access to such accounts fulfill a processing agent role, and while the FHLBanks have a credit exposure to such entities for the limited time operating funds are held in such accounts, these transactional accounts do not involve the extension of credit or lending of funds to a counterparty within the context of the regulation, which is to limit unsecured investment transactions. Furthermore, the nature of these transaction accounts is that money moves more frequently to satisfy operational demands and the FHLBanks are unable to monitor intraday against any established limit which would not necessarily align with the operational transactions performed by an FHLBank. Accordingly, the FHLBanks urge the FHFA to exclude transaction or other non-interest bearing accounts that are used primarily for the FHLBanks' operations, and not for the FHLBanks' investment activities, from the unsecured credit limit requirements of 12 C.F.R. § 1277.7(a). The requirement of intraday credit monitoring for non-interest-bearing deposit accounts is an operational and compliance burden on the FHLBanks that does not support any theoretical benefit in managing potential credit exposure.

Furthermore, the FHLBanks respectfully request that the FHFA clarify that the proposed definition of "authorized overnight investments" does not include any accounts with entities that serve as custodians for safekeeping of cash or securities or processing agents for otherwise secured transactions, such as sponsored or cleared repos. The inclusion of such accounts could significantly limit the FHLBanks' abilities to execute transactions using an agent/custodian. For example, in a sponsored or cleared repo transaction cleared through FICC, cash balances may be briefly held by a processing agent or custodian during the off leg of the transaction for the purpose of completing the transfer of funds. Imposing unsecured limit requirements on intra-day operational deposits associated with these transactions or custodial transactions would significantly inhibit the FHLBanks' ability to trade in various products including: overnight tri-party repos for which the cash and securities exchanges are held by a third-party custodian; cleared Treasury repos through FICC or other similar entities, for which clearing requirements are expected to be implemented by 2026; and repo trades under the Federal Reserve Repo Program (FRRP) under which, at times, the FHLBanks have transacted secured FRRP trades in sizes that are 10 times the unsecured credit limit that would be placed on a custodian under the proposed rule. Ultimately, funds briefly held in the accounts of a custodian or a processing agent do not constitute borrowed funds subject to unsecured credit limits, as such custodian or processing agent is merely acting as an intermediary to complete an overnight or otherwise secured transaction. The FHLBanks also note that entities serving in a custodial capacity have stronger regulatory oversight and requirements to safeguard cash or securities held in such capacity, than a typical capital markets counterparty or broker/dealer.

The intraday monitoring requirement coupled with the increased scope of accounts that fall under the regulation could impact transactions that are not overnight investments. For example, an FHLBank that serves as a safekeeping agent would be required to manage positions at custodians to ensure that in instances of principal and/or interest payments or maturities, such cash inflows would not cause an unsecured exposure breach.

Also, as bonds mature at an FHLBank's custodian, an unsecured exposure is created. To manage the intraday exposure of its custodian, an FHLBank would have to actively manage the maturity profile of its investment portfolio and be made aware of the exact timing of the updating of the accounts to ensure the custodian's unsecured limit would not be exceeded. Depending on the size of maturing investments, this may not be possible.

Additionally, putting constraints on an operational account balance could lead to counterproductive practices such as the payment processing bank counterparty not accepting third party repayments to a Bank that would exceed the unsecured credit limit. This would unnecessarily increase credit risk to those third parties.

The FHLBanks respectfully request that the FHFA remove the requirement to monitor intraday unsecured credit exposure from the proposed rule and exclude non-interest bearing accounts held by the FHLBanks to support their operations or facilitate the transfer of funds for otherwise secured transactions from the proposed rule's definition of "authorized overnight investments".

Future method to expand the definition of authorized overnight investment

The FHFA requested comments on whether future changes to the definition of "authorized overnight investments" should be authorized by the FHFA through the regulatory approval process, or whether any such changes should be subject to notice and comment rulemaking. The FHLBanks believe rulemaking with a public comment period is the best practice in enacting such changes. This method provides the clearest and most transparent path forward to building a better FHLBank System.

Request to Clarify Reporting requirements

The FHFA asked in the proposed rule whether the use of the term ''promptly'' in 12 C.F.R. § 1277.7(e)(3) is too ambiguous and open to different interpretations given the seriousness of the context of extending unsecured credit in excess of a limit and, if so, whether this standard should be revised to reference a more specific timeframe such as ''two business days.'' The FHLBanks believe that the creation of a predefined number of days in the regulation, especially one as short as two days, may require the FHLBanks to report possible violations of the regulation prematurely before management can complete its investigation. The use of the word "promptly" recognizes that management of the FHLBanks should perform a reasonable investigation and report issues to the FHFA in a commercially reasonable timeframe. If the FHFA prefers to adopt an objective timeframe, the FHLBanks propose the use of five business days from the time the respective FHLBank's management confirms a *bona fide* breach has occurred, which is generally in line with other communicated FHFA expectations.

The FHFA also requested comment on whether the provision should explicitly address how to notify FHFA in situations where the Bank may not identify a violation until well after the event occurred. The FHLBanks propose that any timeframe be measured from the date the FHLBank obtains actual notice or knowledge of any such violation.

Elimination of the OF's Monitoring of the FHLBanks' Unsecured Credit Exposure under 12 C.F.R. § 1273.6(f)

As raised in the FHLBank System's joint letter in response to the FHFA's Spring 2023 Notice of Regulatory Review and as conveyed to the FHFA staff on other occasions, the FHLBanks and the OF respectfully request again that, as part of its streamlining and enhancement of its regulations governing the FHLBanks' unsecured credit limits, the FHFA eliminate the OF's monitoring of the FHLBanks' unsecured credit exposure under 12 C.F.R. § 1273.6(f). Such elimination would be consistent with the FHFA's objective of improving its regulations' effectiveness and reducing their burden, similar to what the FHFA has articulated when proposing to remove the redundant reporting requirements in 12 C.F.R. § 1277.7(e)(1) and (2) in this case ("to avoid confusion and the possibility that the regulatory text may conflict with the DRM reporting requirements as FHFA's supervisory reporting needs evolve").

12 C.F.R. § 1273.6(f), related to the monitoring of the FHLBanks' unsecured credit exposure, states that the OF shall "timely monitor, and compile relevant data on, each FHLBank's and the FHLBank System's unsecured credit exposure to individual counterparties." We note that, under 12 C.F.R. § 1277.7, the FHLBanks are already required to comply with regulatory limits on unsecured extension of credit and report information relating to their credit exposure to the FHFA. Since 2015, under the new reporting process developed by the FHFA, the FHLBanks have submitted unsecured credit exposure information required under these regulations directly to the FHFA instead of reporting it through the OF, as before. In light of these process changes (including the change in the OF's role in the related data collection and compilation process), the existence of a separate, enhanced regulatory mechanism (independent of the OF) under which the FHLBanks monitor and report on their unsecured credit exposure and the lack of day-to-day involvement by the OF in the FHLBanks' extension of unsecured credit to their counterparties, we believe that the requirement on the OF under 12 C.F.R. §1273.6(f) is duplicative, burdensome, and obsolete.

We note that, to the extent any unsecured credit exposure information relating to any FHLBank is significant enough for disclosure in the FHLBanks' combined financial reports (CFRs), that information will be collected, compiled, and reported on under generally accepted accounting principles or pursuant to other disclosure requirements, as in the cases of other relevant items, in the ordinary course of the preparation of the CFRs. 12 C.F.R. § 1273.6(f) would be unnecessary for that purpose, as CFR disclosures are already governed by existing FHFA regulations.

Sincerely,

The Federal Home Loan Banks

[Signature Page Follows]

Federal Home Loan Bank of Atlanta

James Canty
Senior Vice President, Treasurer

Federal Home Loan Bank of Boston

Frank Nitkiewicz
Executive Vice President, Chief Operating Officer &
Chief Financial Officer

Federal Home Loan Bank of Chicago

Virxhini Gjonzeneli
Chief Financial Officer, Group Head, Financial
Accounting and Markets

Federal Home Loan Bank of Cincinnati

Stephen J. Sponaugle
Executive Vice President, Chief Financial Officer

Federal Home Loan Bank of Dallas

Tom Lewis
Executive Vice President, Chief Financial Officer

Federal Home Loan Bank of Des Moines

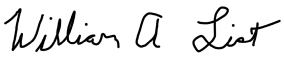
Federal Home Loan Bank of Indianapolis

Gregory Teare
Executive Vice President, Chief Financial Officer

Federal Home Loan Bank of New York

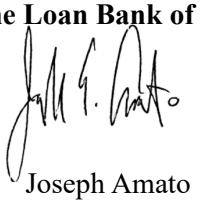
Vikram Dongre
Senior Vice President, Chief Capital Markets Officer

Federal Home Loan Bank of Pittsburgh



William List
Chief Capital Markets Officer

Federal Home Loan Bank of San Francisco



Joseph Amato
Executive Vice President, Chief Financial Officer

Federal Home Loan Bank of Topeka

Philip Bacchus
Senior Vice President and Chief Financial Officer

Federal Home Loan Banks Office of Finance

John Gerli
Chief Capital Markets Officer