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May 29, 2020

SENT VIA ELECTRONIC TRANSMISSION

Federal Housing Financing Agency
Division of the Federal Home Loan Bank
Regulation
400 7th Street SW, 7th Floor
Washington, D.C. 20219

Re: Federal Home Loan Bank Member Request for Input, February 2020.

Dear Federal Housing Financing Agency,

The Kentucky Bankers Association (KBA) is pleased to submit this response to the Request for Input (the "RFI") from the Office of the Federal Housing Financing Agency (FHFA) where "the goal of FHFA's current membership review is to develop a set of principles and requirements of general applicability to address these and other membership issues on a consistent basis."[1] The KBA understands that this RFI is "guided by the twin objectives of ensuring that the system remains safe and sound and able to provide liquidity for housing finance through the housing and business cycle, and ensuring that all members have an appropriate nexus to the housing finance and community development mission of the FHL (Federal Home Loan) Banks" ("FHLBanks") (the "Purpose").[2]

After consulting with representatives from the Kentucky Bankers Association's one hundred and sixty-one (161) member institutions ranging in asset size from twenty-one million dollars ($21,000,000) to over three hundred and seventy billion dollars ($370,000,000.00), the Kentucky Bankers Association submits the following comments to the RFI:

- No regulatory action in response to the RFI should limit liquidity to FHLB members;
- No regulatory action in response to the RFI should adversely impact the eligibility of existing, permanent members;
- Any new entrants should be determined by Congress and be equivalent to currently eligible members and be admitted with current safety and soundness standards;
- Any new entities considered for membership should have a clearly demonstrated nexus to housing and/or community development at the time they join.

[1] RFI, page 2.
[2] RFI, page 2.

1. No Regulatory Action in Response to the RFI Should Limit Liquidity to FHLB Members

"The FHLBanks carry out their public policy function primarily by providing low-cost loans, known as advances, to their members. These must be fully secured by one or more specific types of collateral, including residential mortgage loans and residential mortgage-backed securities."[3]

"FHLBanks provide low-cost wholesale funding to their member institutions to help those members, in turn, provide long-term home mortgage loans to consumers at a reasonable cost. The FHLBank members benefit from a lower cost of funds, which in general improves their competitiveness with non-members who do not have such access and improves their ability to manage liquidity and other risks."[4] FHLBanks serve as an important source of liquidity for its members, including Kentucky banks.

One of the questions posed by the RFI was whether there should be restrictions on advances to a single member.[5] It is the KBA's opinion that the answer to that question is a resounding "no".

FHLB members rely on FHLBanks for liquidity at all times but even more when the country is in crisis. Nothing is more exemplary of that fact than the FHLBanks' efforts in offering additional liquidity by accepting loans made through the Small Business Administration's Paycheck Protection Program as collateral when making advances to their members.[6] "It is designed to serve smaller banks who don't have access to the Federal Reserve's Paycheck Protection Program Liquidity Facility."[7]

If the RFI leads to liquidity limitations, the partnerships between the FHLBanks and their members would be significantly limited, if not harmed. FHLBanks have shown their ability to effectively manage and provide liquidity in a safe and sound manner whether times are good or bad. Limiting liquidity would likely have a "trickle down" effect in not only harming FHLBanks, but ultimately the members and communities they serve.

For these reasons, the KBA believes that no regulatory action in response to the RFI should limit liquidity to FHLB members.

2. No Regulatory Action in Response to the RFI Should Adversely Impact the Eligibility of Existing, Permanent Members

Kentucky banks and many other lenders rely on FHLBanks for liquidity. If the FHFA were to create new regulatory action in response to the RFI, it could adversely impact the eligibility of existing, permanent members. In addition to creating additional, unnecessary compliance costs, the loss of eligibility for an institution could have devastating effects for the institution and its customers.

FHLBanks have shown their ability to effectively and efficiently manage their membership. FHLBank membership is robust and FHLBanks take appropriate measures to mitigate risk. There is no reason to change a system that is not broken.

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[3] RFI, page 3.
[4] RFI, page 4.
[5] RFI, page 15.
[6] Hannah Lang, *Federal Home Loan Banks to Offer More Liquidity for PPP Lenders*, AMERICAN BANKER, April 23, 2020.
[7] Hannah Lang, *Federal Home Loan Banks to Offer More Liquidity for PPP Lenders*, AMERICAN BANKER, April 23, 2020.

For these reasons, the KBA requests that FHFA take no regulatory action that could impact the eligibility of existing, permanent members.

3. Any New Entrants Should be Determined by Congress and be Equivalent to that Applicable to Currently-Eligible Members and Be Admitted with Current Safety and Soundness Standards

The RFI asks whether additional members should be considered for membership. The KBA believes the FHFA should be careful in this consideration.[8]

First, the KBA believes that Congress has clearly mandated who is eligible for FHLBank membership. Any consideration of entities outside of those explicitly mandated should have Congressional approval.

Second, to the extent other entities are considered, the FHFA should look closely at whether such institutions would put FHLBanks at risk.

"The coronavirus pandemic has left the corporate sector scrambling for cash."[9] "Unfortunately, the global corporate sector went into the pandemic with unprecedented levels of financial leverage, largely because of the low-interest environment following the 2008 financial crises made it easy for companies to borrow."[10] "Leveraged loans to these companies are funded primarily by non-bank institutional investors, with the majority of cash raised by the issuers of collateralized loan obligations."[11]

On a more global scale, "Fallout from the coronavirus pandemic will likely expose funding and liquidity weaknesses of some banking systems in the Middle East, Turkey and Africa, at a time when they are needed to support their economies."[12]

With these liquidity weaknesses, additional entities will likely seek FHLBank membership for liquidity. These entities could place significant risk on the FHLBanks and, ultimately, liquidity risk to FHLBank members and their communities.

Any additional membership must be examined closely to determine whether they meet existing membership criteria. Even more importantly, such entities must adopt safety and soundness examination that the current membership is subject to through various governing bodies.

For these reasons, the KBA requests that any new members of the FHLBank system be mandated by Congress and that such entities be subject to the same scrutiny and review as its current members.

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[8] RFI, pages 13-14.
[9] Mike Harmon and Victoria Ivashina, *Managing the Liquidity Crisis*, ECONOMICS & SOCIETY, April 9, 2020.
[10] Mike Harmon and Victoria Ivashina, *Managing the Liquidity Crisis*, ECONOMICS & SOCIETY, April 9, 2020.
[11] Mike Harmon and Victoria Ivashina, *Managing the Liquidity Crisis*, ECONOMICS & SOCIETY, April 9, 2020.
[12] Stephanie Mery and Mohamed Damak, *Covid-19 Exposes Funding and Liquidity Gaps at Banks in the Middle East, Turkey and Africa*, S&P GLOBAL, April 6, 2020.

4. Any New Entities Considered for Membership Should Have a Clearly Demonstrated Nexus to Housing and/or Community Development at the Time They Join

As discussed in part three *supra*, if the FHFA determines that additional entities should be admitted to the FHLBank system, such entities should not only be subject to current regulatory review but must also align with the public policy goals of the FHLBanks.

It is important to remember the FHLBank's "mission of providing liquidity to support housing finance and furthering affordable housing and community development."[13] Any entity seeking membership to the FHLBank system must further that goal; not take away from it.

As many entities may see FHLBanks as a means to additional low-cost liquidity, the FHFA cannot forget the mission of the FHLBanks. Any entities not specifically furthering that mission should be ineligible both statutorily and for public policy purposes. Otherwise, the health of FHLBanks may be jeopardized and initiatives like those enacted by FHLBanks during the Covid-19 crisis may not have be possible.

For these reasons, the KBA requests that any new entities considered for membership have a clearly demonstrated nexus to housing and/or community development at the time they join.

5. The KBA Supports the FHLBanks

The KBA supports FHLBanks and their purpose. The KBA believes that with the considerations above, FHLBanks will continue to serve the communities, citizens, lenders and stakeholders of this country.

Thank you for considering our suggestions. If there are any questions, please do not hesitate to contact the undersigned.

Sincerely,

Debra K Stamper

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[13] RFI, page 1.