



March 29, 2023

The Honorable Sandra L. Thompson
Director
Federal Housing Finance Agency
Constitution Center
400 7th Street, SW
Washington, D.C. 20024

Regarding: FHLBank System at 100: Focusing on the Future

Dear Director Thompson:

The Community Bankers Association of Illinois (“CBAI”), which proudly represents nearly 300 Illinois community banks, appreciates the opportunity to provide our additional and current observations and recommendations regarding the Federal Housing Finance Agency’s (“FHFA” or “Agency”) comprehensive review titled – *FHLBank System at 100: Focusing on the Future* (“Comprehensive Review”). CBAI agrees with the Agency’s statement that “The FHLBanks have been a critical source of liquidity for their members for the past 90 years, especially during times of market stress, such as the Great Recession and the outset of the COVID-19 pandemic. The FHLBanks also support low-income housing and community development directly by offering a variety of programs to their members, including the Affordable Housing Program, the Community Investment Program, and the Community Investment Cash Advance Program.” CBAI acknowledges the Director’s statement that “As the Federal Home Loan Banks approach

CBAI is dedicated to exclusively representing the interests of Illinois community banks and thrifts through effective advocacy, outstanding education, and high-quality products. CBAI’s members hold more than \$80 billion in assets, operate 860 locations statewide, and lend to consumers, small businesses, and agriculture. For more information, please visit www.cbai.com.

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their centennial, FHFA will conduct a comprehensive review to ensure they remain positioned to meet the needs of today and tomorrow.”

Background

The overwhelming majority of CBAI’s nearly 300 community bank members are also members of the Federal Home Loan Bank of Chicago (“FHLB-Chicago,” “FHLB-C,” or “Chicago Bank”). In addition, many of our members have or are currently serving in various leadership positions in the FHLB-Chicago. Our members truly value the excellent relationship they have with the Chicago Bank and they use many of the products and services that the FHLB-C provides for the benefit of their banks as well as their customers and communities.

As an aside, my experience with the FHLB-Chicago spans decades, earlier as a career-long community banker and now as an advocate for Illinois community banks. I am perhaps uniquely situated in having seen the many benefits the Federal Home Loan Banks (“FHLBank(s)” or “FHLBs” or “Banks”) provide their members from several different perspectives, including in times of financial stress like we experienced during the financial crisis in 2008/2009, the Covid pandemic in 2020/21, and more recently with the failures of Silicon Valley Bank and Signature Bank.

Ownership and Capitalization

CBAI wants the ownership and the capitalization of the Banks to be given consideration equal to its importance, in discussions about the future of the FHLBs. The members of FHLBanks contribute their funds to purchase capital stock which together with the retained earnings constitute the Banks’ capital base. It is upon this strong base that everything else the Banks do is built and made possible including providing services to its member-owners and significant support for affordable housing and community development.

There is no requirement for a bank to be a member of an FHLB. Membership is completely voluntary. Therefore, the focus of the FHLBs today is where it should be on serving the needs of its members, and they do so by attracting and retaining them, and by providing products and services that the members find valuable.

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A variation of a saying comes to mind and accurately describes the reality of ownership and capitalization of the FHLBs and the many worthy causes which are the beneficiaries of the FHLBanks' income – “No members, no money, no mission.” During the Comprehensive Review, CBAI cautions policymakers to be aware of the importance of the foundation on which the FHLBanks are built to ensure that the FHLBs will be able to continue to fulfill their missions well into the future.

Interdependence of FHLB's Operations

The FHLBanks have three distinct uses for funds from their operations which include: funding for mortgages and asset-liability management, liquidity for members' short-term needs, and housing finance and community development. Once a delicate balance has been achieved, any changes will by necessity impact one or more of the others.

For example, if FHLB advances (“Advances”) are curtailed because of limitations on membership, or limits on the amount of Advances to certain members, the income the Bank earns on Advances will decline. If Advances income declines, it is logical that the Bank's income will decline and the amount the Banks contribute to affordable housing and community development will decline. Some are advocating for limits on Advances for various reasons, but no one will be happy with the reductions in income and funds contributed to worthy causes if Advances' income declines – but this will be the inevitable result.

The FHLBs do not exist in a vacuum. They have evolved to become an essential component of the broader banking and financial system and our economy, and they have a working relationship with the banking regulators. Here again, decisions by policymakers to make changes to the Banks and the FHLBSystem will have far-reaching consequences and should be approached with the utmost caution – and proceed only with a broad consensus.

Advances

The past few weeks have proven beyond any doubt the critical importance of FHLB Advances. Some have proffered that fluctuations in Advances are evidence of a problem or the relevance of the FHLBSystem. This is an unfounded and reckless notion that should be disposed of once and for all.

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During the past few weeks and in the face of the failure of two \$100+ billion in asset banks, one being the 16th largest bank, the importance of certain and timely liquidity provided by the FHLBanks to all its member-owners proved to be an essential component of their liquidity stack. At times of financial stress like this, the funds supplied by the FHLBs support not only the members banks, but also the entire banking and financial system, and the broader economy. As the level of financial stress subsides, Advances will return to normal levels which is precisely what should happen.

Advances are fully collateralized, and the certain expectation is that they will be repaid in full and the FHLBs will not suffer any losses. Repayment in full is virtually assured as the FHLBs have never suffered a loss on an Advance – ever. This enviable track record keeps the cost of Advances low which benefits its member-owners and the uses for which those funds are borrowed.

Some have complained about not getting access to Advances because they are not regulated institutions, and others complain about the low collateral advance ratios, but these guardrails assure that the Banks will take no losses on Advances. Those who complain, and would risk the Banks suffering losses on Advances, must be aware that those losses would reduce the profits of the Banks and reduce the amount of funds available for affordable housing and community development. This would not be a desirable outcome, and the ability of the FHLBanks to limit its credit risk exposure regarding members and insisting on collateral “haircuts” must be maintained.

Membership and Eligibility for Products and Services

Members having certain and timely access to Advances and other services presupposes the criteria for membership is reasonable and consistent. Without these features, the value of Advances to the members and their regulators would be diminished. Currently, FHLB membership is available to regulated institutions that have a capitalization and capacity to hold eligible collateral. These institutions include banks, credit unions, CDFIs and Insurance companies (and should, but unfortunately no longer include captives of insurance companies.) Once membership status is conferred it cannot be challenged or denied except in highly unusual circumstances.

If membership is unduly restricted and access to services can be denied, the value of Advances to

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member-owners, the broader banking and financial system, and the economy would be seriously diminished. The timely access for needed liquidity should not be challenged or denied for not meeting arbitrary and/or continuing membership requirements (i.e., requiring members to maintain an arbitrary percentage of their assets in residential housing, or implementing a tracking mechanism for Advances) that have not existed in the past, have no good reason to exist today, and have not been approved by Congress.

Cooperative Structure

The FHLBanks are designed to work cooperatively with and not compete against their members, including community banks. CBAI believes the FHLBSystem and Banks should serve as a model for how a government sponsored entity should work cooperatively with and not compete against the private sector and community banks.

Regional Nature

Individual FHLBanks, in different regional districts, are informed by their member directors, officers, and members owners about the types of products and services that would help them best serve their customers and communities. This information is shared among the regions/districts and ensures that multiple expertise and experiences are brought to bear on complex and pernicious issues. CBAI supports the many benefits of a regional structure consisting of many district FHLBanks which will be lost by any centralization of ownership and management for the sake of “operational efficiency.”

Conclusion

CBAI recommends that after this Comprehensive Review has been completed, the FHFA should not disrupt the cooperative structure, regional nature, special functions, and unique purposes of the FHLBanks. Also, the Agency should not impose any additional membership or ongoing eligibility requirements that would undermine the certainty of continued membership and access to services. Also, there should be no additional distribution requirements that would reduce the capital which supports the Banks important products and services and provides a reasonable return on a member-owner’s investment.

Thank you for the opportunity to provide our additional and current observations and

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recommendations. We look forward to a continued dialogue with the FHFA as the FHLB System head towards its 100th anniversary – and beyond. If you have any questions or require any additional information, please contact me at davids@cbai.com or (847) 909-8341.

Sincerely,

/s/

David G. Schroeder
Senior Vice President
Federal Governmental Relations