United States Senate

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS

WASHINGTON, DC 20510–6075

March 31, 2023

The Honorable Sandra Thompson
Director
Federal Housing Finance Agency
400 7th Street SW
Washington, DC 20024

Dear Director Thompson:

Thank you for initiating a review of the Federal Home Loan Bank (FHLBank) System. Your effort to include the perspectives of a variety of organizations, geographies, and communities has provided important insights into the current function of the System. As Chairman of the Senate Banking, Housing, and Urban Affairs Committee, I would like to offer the following comments for your consideration as you prepare to write your final report on recommendations for the future of the FHLBank System.

Our financial system has transformed since Congress passed the Federal Home Loan Bank Act in 1932. We have gone from a financial system dominated by thrifts, building and loans, and insurance companies limited to operating within a single state, to a system of community lenders and national and international holding companies doing business across state lines, some with sophisticated capital markets operations. The FHLBank System of the 1930s was the first and only tool at the time to support longer-term, more affordable mortgage lending. Today, the system still supports longer-term mortgage lending, particularly lending done by community lenders, but it has also proven to be a critical source of liquidity to members in ways often unconnected to housing, particularly during times of market stress.

Congress and the Federal Housing Finance Agency (FHFA) have taken some steps to modify FHLBank System requirements to account for these changes. Congress created the Affordable Housing Program (AHP) and Community Investment Program (CIP) and required members to hold a minimum of 10% of assets in residential mortgage loans when they join the FHLBank System to verify that new members operate in our housing system. FHFA updated Affordable Housing Goal requirements and membership standards and created the Community Investment Cash Advance (CICA) Program to support the low-cost capital critical for housing and economic development activities serving lower-income populations. However, despite Congress' focus on these important, mission-focused activities, they remain a relatively small portion of the system's activity.

As our financial system evolves, the FHLBank System must also evolve to ensure that it is still meeting the housing and community development needs it was established to fulfill, and that we are appropriately monitoring the role the FHLBanks play in the safety and soundness of our broader financial system. To ensure that the System is prepared to meet the challenges we face today, please consider the following as you prepare your report.

Safety and Soundness

Events of the past month have demonstrated that FHLBank advances are a critical source of liquidity for financial institutions during times of system-wide stress. Following the failures of Silicon Valley Bank and Signature Bank, the FHLBank System provided record levels of advances to help banks strengthen their liquidity positions. The System's size and ability to fulfill large volumes of advances quickly makes it an important piece of our financial framework. FHLBank actions. Its decision to extend advances may have implications for prudential regulators and for the broader financial system.

It is critical that the FHLBanks and FHFA are in close and timely communication and coordination with state and federal banking and credit union regulators, as well as insurance regulators, about the financial soundness of and liquidity requests from institutions and that they are acting on the most current information. In today's financial marketplace, making decisions based on last quarter's call report data may not be consistent with financial stability. Additionally, to the extent that financial institutions are members of multiple FHLBanks, advances from one FHLBank may be obscured from other FHLBanks for some time. FHLBanks with members operating across districts should similarly coordinate among themselves, with FHFA, and with prudential regulators in real time to assess whether the amount of advances going to a single institution is appropriate.

FHLBank advances have also grown increasingly concentrated in a few large institutions. As of December 31, 2022, all but one FHLBank had more than 40% of its advances outstanding to its top five members, and one member was among the top five advance holders at two different FHLBanks.[1] While each FHLBank sets policies to manage the amount of advances a member can draw relative to that member's assets, as institutions grow in size, those policies do not limit the risk that a single member could pose to an FHLBank. FHFA should consider whether limits both on an individual member's advances relative to assets and in the amount of advances an FHLBank has to a single member are necessary to manage evolving risks.

If FHFA, the FHLBanks, or prudential regulators do not currently have the authorities required to appropriately assess and communicate about a member's financial stability or advance activity, FHFA should recommend legislative changes to ensure that the FHLBank System can contribute to financial stability.

Fulfilling the FHLBanks' Housing and Community Development Purpose

Congress established the FHLBank System to support the nation's residential housing market. Advances based on single-family and multifamily mortgage loans, low-cost CIP and CICA advances, Acquired Member Assets (AMA) programs, and AHP awards still provide critical support. But CIP, CICA, AMA, and AHP programs remain relatively small compared to the large amount of advance activity the FHLBanks conduct, particularly with the largest institutions, and the dividends they provide.

The small size of the FHLBanks' mortgage and community investment programs does not result from a lack of community need. There is a shortage of safe, affordable housing in every corner of the

---

[1] "Combined Financial Report for the Year Ended December 31, 2022," Federal Home Loan Banks Office of Finance, March 24, 2023, pgs. 61-63, available at https://www.fhlb-of.com/ofweb_userWeb/resources/2022Q4CFR.pdf.

country. One-in-four families pays more than half of their income for housing[2], and there is an estimated shortage of 3.8 million homes across the country.[3] Households of color are also more likely to struggle to afford their housing costs[4], and less likely to own their own home and to benefit from the wealth that homeownership can provide.[5]

The need for funding, whether to build, repair, adapt, or support a down payment for housing is acute. FHFA roundtable participants across the country reiterated the important role that limited AHP funds play in local housing and community development work, and AHP applications far exceed awards in every FHLBank district. Nonbank community development financial institution (CDFI) FHLBank members who serve underserved communities still struggle to access FHLBank financing nearly 15 years after Congress acted to include them as System members.

The System can and must do more to support housing and economic development. To ensure that the system is fulfilling its housing and community development mission, FHFA should consider:

- **Strengthening enforcement of the banks' existing community support program requirements, including technical assistance to members.** The current community support regulation requires the FHLBanks to provide technical assistance to members, promote and expand affordable housing finance, and encourage members to increase targeted community lending and affordable housing finance, among other activities.[6] Yet program participation levels and feedback from roundtable participants indicates limited availability of these low-cost products. FHFA should develop a method of assessing FHLBanks' fulfillment of this existing requirement to ensure that members and community institutions are aware of and able to benefit from existing products and services.
- **Revising and strengthening member community support requirements.** While all FHLBank members are required to meet minimum community support requirements to access long-term FHLBank advances, the current community support program regulation limits FHFA's review to a member institution's Community Reinvestment Act (CRA) performance and lending to first-time homebuyers.[7] Because CRA only applies to banks, some FHLBank members are only subject to the first-time homebuyer assessment. FHFA allows lenders to fulfill the first-time homebuyer test using tools that may not have any benefit for first-time homebuyers, like holding "mortgage-backed securities that may include a pool of loans to low- and moderate-income homebuyers."[8] Meanwhile, the requirement does not account for some member activities more closely tied to the FHLBanks' housing mission, including financing affordable rental housing.
  FHFA should reassess the community support requirement to ensure that it establishes a meaningful standard for all members and accounts for a range of ways that members meet affordable housing needs in their communities, including financing affordable multifamily

[2] "The State of the Nation's Housing 2022," Joint Center for Housing Studies of Harvard University, pg. 37, available at https://www.jchs.harvard.edu/sites/default/files/reports/files/Harvard_JCHS_State_Nations_Housing_2022.pdf.
[3] "Housing Supply: A Growing Deficit," Freddie Mac, May 7, 2021, available at https://www.freddiemac.com/research/insight/20210507-housing-supply.
[4] "America's Rental Housing 2022," Joint Center for Housing Studies of Harvard University, pg. 32, available at https://www.jchs.harvard.edu/sites/default/files/reports/files/Harvard_JCHS_Americas_Rental_Housing_2022.pdf.
[5] "Quarterly Residential Vacancies and Homeownership, Fourth Quarter 2022," Census Bureau, January 31, 2023, available at https://www.census.gov/housing/hvs/files/currenthvspress.pdf.
[6] 12 CFR 1290.6
[7] 12 CFR 1290.3
[8] Id.

rental housing and providing local housing partners with low-cost advances through CIP or CICA. FHFA should also require that members have not had a fair housing or fair lending violation in the preceding five years. Institutions that exhibit partners or practices of housing or lending discrimination are not serving the entire communities where they do business and should not benefit from the FHLBank System's tools.

- **Assessing FHLBank compliance with existing CIP requirements, with an emphasis on the percentage of members participating in the program.** Member use of CIP varies by FHLBank but remains low. The System as a whole had just $2.656 billion in CIP and CICA advances in 2021[9], while overall advances were $351.3 billion.[10] Member participation in the program was also low – less than two percent of members participated at the majority of FHLBanks in 2020.[11] But FHFA roundtable participants doing housing and community development work expressed that access to low-cost advances like those available through CIP and CICA is critical for their housing and community development work.
- **Enhancing monitoring of each FHLBank's progress in meeting housing goals.** In its most recent annual report, FHFA found that the three banks then subject to housing goal requirements failed to fulfill most or all of those goals.[12] While FHFA has since amended the FHLBanks' housing goals assessment and will now require each FHLBank to meet housing goals in its programs, it is extremely concerning that the FHLBanks with the largest AMA programs failed to meet targets to serve low-income homeowners and small FHLB members. FHFA should monitor the FHLBanks' progress throughout the year in meeting their housing goal targets, particularly as banks begin operating under FHFA's new housing goal regulation, to ensure that FHLBanks' AMA programs are meeting the needs of serving low-income homebuyers and community financial institutions.
- **Supporting nonbank CDFI access to low-cost advances for housing and community development using new tools.** As FHFA's roundtables made clear, nonbank CDFI members continue to struggle to access FHLB advances. Haircuts for nonbank CDFIs' collateral are far higher than those for traditional bank collateral, making advances uneconomic for institutions trying to do housing and community development work. FHFA should consider additional tools to bolster nonbank CDFIs' ability to access advances with their existing collateral, like allowing FHLBanks to capitalize a loan loss reserve fund at each FHLBank to stand behind nonbank CDFI advances, allowing the FHLBank to advance greater amounts on the same pledged assets.[13]
- **Whether existing AHP levels are sufficient.** In 2022, the FHLBank system provided $355 million in AHP funding to members and community partners, while providing dividends of $1.372 billion to member stockholders.[14] In 2020, the system was only able to fund

[9] "2021 Mission Report: Affordable Housing Activities of the Regulated Entities," Federal Housing Finance Agency, June 6, 2022, pg. 24, available at https://www.fhfa.gov/AboutUs/Reports/ReportDocuments/FHFA-2021-Mission-Report.pdf.
[10] "2021 Report to Congress," Federal Housing Finance Agency, pg. 77, available at https://www.fhfa.gov/AboutUs/Reports/ReportDocuments/FHFA-2021-Annual-Report-to-Congress.pdf.
[11] "2020 Low-Income Housing and Community Development Activities of the Federal Home Loan Banks," Federal Housing Finance Agency, October 12, 2021, pg. 30, available at https://www.fhfa.gov/AboutUs/Reports/ReportDocuments/2020-Low-Income-Housing-and-Comm-Development-Activities.pdf.
[12] "2021 Report to Congress," pgs. 42-43.
[13] See, for example, "How FHFA Can Increase the Federal Home Loan Bank Affordable Housing Investments," Michael Stegman, Urban Institute, March 2023, pg. 5, available at https://www.urban.org/sites/default/files/2023-03/How%20the%20FHFA%20Can%20Increase%20Federal%20Home%20Loan%20Bank%20Affordable%20Housing%20Investments.pdf.
[14] "Combined Financial Report for the Year Ended December 31, 2022."

approximately 43% of AHP applications submitted, indicating that there is significantly more need than funds available to fulfill that need.[15] While most banks also operate voluntary, non-AHP grant and low-cost advance programs, those programs provided limited additional funding. FHFA should evaluate whether the amount the banks must contribute to AHP could be increased to further benefit communities and prospective homebuyers without undermining the FHLBanks' financial strength.

<u>Governance</u>

The FHLBanks' Boards of Directors and Affordable Housing Advisory Councils provide important leadership and direction for each FHLBank. But existing Boards of Directors may not fully capture the housing needs of the district or the expertise necessary to ensure that the FHLBank's activities are addressing unmet needs for underserved populations. FHFA should consider whether a greater proportion of each Board should be composed of independent directors, and whether additional expertise among those directors should be required. Alternatively, FHFA could consider whether Affordable Housing Advisory Council members should be included in more elements of the Board's decision making to ensure that affordable housing and community development expertise is integrated into all of the FHLBank's decisions, not just decisions on AHP allocations and CIP and CICA evaluations. FHFA should also consider whether existing compensation policies, including compensation of Board and FHLBank leadership, are calibrated to ensure that each FHLBank is meeting both the liquidity and housing portions of its mission.

Thank you for your leadership in initiating this review of the FHLBank System and for your consideration.

Sincerely,

Sherrod Brown
Chairman

[15] "2020 Low-Income Housing and Community Development Activities of the Federal Home Loan Banks," pg. 7.