October 6, 2014

Alfred M. Pollard, General Counsel
Attention: Comments/RIN 2590-AA39
Federal Housing Finance Agency
400 Seventh Street SW, Eighth Floor
Washington, DC 20024
email: RegComments@fhfa.gov

Re: Members of Federal Home Loan Banks
Notice of Proposed Rulemaking, RIN 2590-AA39

Dear Mr. Pollard:

I am the former President-CEO of the FHLBank of Indianapolis. Before my retirement I spent the last few years of my career at the Bank building the insurance company business, including serving Michigan captives. I have invested a great deal of time on this matter, and felt it necessary to take the time to comment on this important rulemaking.

Advances May Be Safely Made to Insurance Captives

As for background, to ensure our FHLBI board of directors and staff had complete understanding of the risks and opportunities, we first closely studied the insurance industry and market opportunities. Two unique factors exist in our Indianapolis district. The first is that nearly 70% of all member assets are comprised of insurance companies. Secondly, Michigan has a very workable captive insurance law and an effective state regulatory regime. Based on these market factors, starting in the mid-2000s, we hired insurance underwriting expertise, enhanced commercial real estate valuations and collateral liquidation plans, clarified the Michigan secured creditor laws, and developed a close working relationship with the Michigan insurance regulators. We also facilitated FHLBank System discussions and assisted in the development and implementation of the FHFA's Advisory Bulletin AB 2013-09 concerning FHLBank credit products for insurance companies.

The FHFA's proposal now suggests that captives and reinsurance companies be disqualified and their membership terminated. During my tenure as CEO, we built captive lending to well over $1 billion and the FHFA never articulated a safety-soundness concern unique to captives. My experience is that the risks of captive lending are no different than the risks we take with our other members. Our credit underwriters, corporate risk managers, legal, external audit and internal audit teams all concurred with my assessment.

Similarly, the public comment FHFA received from the FHLBanks on Advisory Bulletin AB 2012-N-14, dated December 3, 2012, confirms that no special safety-soundness concerns exist with captives, and I respectfully request the FHFA reference that FHLBank System comment when considering this rulemaking. Notably, the resulting final version of AB 2013-09, published on

December 23, 2013, addresses the credit risk management practices for insurance company members, and it confirms that, if the guidance therein is followed, lending to captives and reinsurance companies may be done in accordance with both the mission and safety-soundness standards expected of an FHLBank.

After paying off FHLBank advances, including prepayment fees, in full, the FDIC and NCUA receivers prefer to take control of the collateral for such advances. This practice is entirely voluntary on their part, and beyond the FHLBanks' control. For all of our credit decisions, whether it be for an insurance company, credit union or commercial bank, we are prepared to liquidate the secured collateral we hold in the event of a member's default. The lever for repayment is not the FDIC or NCUA. The deposit insurers are merely a vehicle that allows for repayment because they prefer to liquidate the collateral themselves. This saves us from having to liquidate the collateral, but to my point above, *this does not change the credit risk for insurance company lending relative to FDIC or NCUA insureds*. It merely adds another step to the liquidation and repayment process.

Members are Regulated by their Primary Regulator, Not the FHFA

The FHFA should not, in its efforts to disqualify captives and other reinsurance companies, create a definition of permissible insurance products for our insurance company members. There is no Federal statutory basis for this, and insurance activities are under the purview of state law.

If the FHFA states in rulemakings the type of insurance that must be provided, should it also dictate product offering for other member classes? Obviously, it would be absurd for the FHFA to declare what products are or are not allowable for commercial banks or credit unions, and it is similarly absurd to do the same for captives and reinsurance companies. It is the responsibility of primary regulators, not the FHFA or the FHLBanks, to regulate members' business activities.

Automatic Member Termination is Unjustified

In my professional opinion, based on 30+ years as a credit officer of an FHLBank, captives do not present unique or dangerous credit risks. However, if the FHFA legitimately identifies such risks, then it should propose specific and workable safety-soundness regulations to address those concerns. Until such risks, if any, are identified and thoughtfully considered, the FHFA should refrain from implementing a penalty as drastic as the termination of an entire member class.

In its Preamble to the proposal, the FHFA expresses concern that, from a mission-related perspective, captives may be acting as conduits to provide advances to affiliated companies that are, themselves, ineligible for membership. This concern is misplaced. First, our FHLBI captives all use advances and pledge collateral tied to housing and community economic development lending or investment. FHLBank insured depository members often have holding company or affiliate structures (*e.g.*, bank holding companies, investment or mortgage banking operating subsidiaries or affiliates), that are not eligible, by law, for membership, yet these entities directly or indirectly benefit through the member's access to FHLBank credit products.

It is notable that the FHFA, in its proposed rulemaking, fails to articulate why captives present special safety-soundness concerns. Indirect references or suggestions of FHLBank mission creep are unfounded, especially given that our captives' activities are focused on multi-family and commercial lending. All of these activities closely align to our mission.

Although not relevant to our experiences in Indianapolis, certain captive activities could be deemed impermissible by the FHFA for FHLB liquidity lending purposes because the activities do not align with the mission of the FHLBank System (*e.g.*, credit card receivables, student lending or admiralty insurance). The FHFA could specifically eliminate these troublesome activities through the rulemaking process. Or if special risks are legitimately identified, additional risk-based capital or retained earnings could be considered. Again, a reasoned regulatory approach is far preferable than eliminating an entire member class.

Parental ownership of a member using private or public equity, whether in a REIT or other corporate form, should be viewed favorably. This investment vehicle places more private capital at risk to support housing and economic development. By encouraging more housing and economic development private investment, our nation's reliance on the deposit insurance funds and ultimate risk to the taxpayers is reduced.

REITs Should Not Be Treated Differently Than Commercial Bank Holding Companies

The FHFA further suggests, in the proposal's Preamble, that REITs should not have access to FHLBanks. A REIT is merely a corporation that has made a tax structure election, analogous to a bank holding company that makes a Chapter S election. Like bank holding companies and other corporations, they are not eligible, by law, to be FHLBank members, which suggests that member eligible corporate structures below the parent (*e.g.*, captives, other insurance companies, or banks) should not be disqualified simply because of the legal structure residing above the member. Moreover, unique to captives, an FHLBank may take special safety-soundness precautions (*e.g.*, parental guarantees, making sure collateral resides with the captive or a subsidiary affiliate of the captive) to ensure it is not dealing with just a "shell" corporation or funding conduit.

The proposal suggests an FHLBank cannot get adequate financial information from the parent. This has not been our experience. Such information is easily and regularly obtained *as a requirement* in our advance lending contracts so that FHLBI may safely underwrite the captive, its parent, its subsidiaries and its affiliated companies. FHLBI also has field collateral underwriters to inspect, test and validate data received.

Insurance Companies Should Not Be Permitted to Forum Shop

The proposal (12 CFR 1263.4(b)) that insurance company membership can be moved unilaterally ties insurance company FHLBank district membership to where business activities and records primarily reside. The proposed change to the way principal place of business is determined gives the insurance company member the ability to shop FHLBanks based on where it locates its management team. To an outsider, such a change, on its face, may seem reasonable, but experience shows that it adds unnecessary risk to FHLBank operations. Often, insurance company members have large levels of private and/or public capital investments with many operating units and extraordinarily broad footprints. With computer technology, the movement of key decision makers and records may be done quickly and with little effort. Under the proposal to move membership, *only* the key decision makers have to relocate into another FHLBank district, making it extremely easy to hop from one district to the next.

Over time, forum shopping by insurance companies for the best advances and collateral terms will erode our regionally-based System. It is significant to note that the FHFA has never approved an adjacent district membership by convenience application, which is specifically authorized in the Bank Act (12 USC 1424(b)). Similarly, the Washington Mutual multi-district application in the early 2000s was withdrawn over concerns about forum shopping. Finally the three-part membership move test (12 CFR 1263.18(c)(1)) requires a diligent review to support a membership move, as well as the approval of the "losing" FHLBank board of directors. By rule and practice, historically, the FHLBanks and the FHFA discourage forum shopping. I believe that traditional approach to membership should remain.

There is no good public policy reason to afford special treatment for insurance companies. The charter location-state of domicile test, along with the three-part test that works for our commercial banks and credit unions, should also apply for insurance companies. The principal place of business definition should remain unchanged from what it was before the 2012-RI-02 regulatory interpretation as it relates to insurance companies. (A technical aside—I do not object to "allowing where the CDFI does business" standard to apply for CDFI membership because a federal bankruptcy trustee would be engaged if a non-insured depository CDFI fails. The issue of having a close relationship with the state insurance regulator does not generally apply for non-insured CDFIs. I do however believe the losing FHLBank should approve the CDFI membership transfer and in the event of disagreement, the matter should be appealable to the FHFA for a prompt final decision.)

If an insurance company's principal place of business is moved, the new FHLBank must then fully understand the state law that the receiving member is subject to *and create a working relationship* with that state insurance regulator. Our level of involvement with and understanding of the Indiana and Michigan state insurance regulators could not be duplicated if we were forced to cover the nation. Also our analysis of insurance state laws revealed there may be some states we would prefer not to do business with because, for example, the state has secured credit borrowing limits. However, since the losing FHLBank may have already extended credit, it makes it difficult for the receiving FHLBank to say no to membership. This is especially troublesome because, under the proposal, the insurance company, if not grandfathered under the proposal's Preamble, just has to notify the FHLBanks and move districts with a simple move of leadership and electronic records. While the receiving FHLBank is not obligated to assume the former FHLBank's advances, it makes it harder for the receiving FHLBank to deny advances going forward. I shudder at the thought of having a troubled insurance company unilaterally move using the proposed authority, especially if the move is to receive more lenient advance or collateral terms.

Under the proposal, commercial bank and credit union membership is still based on domicile or charter location, and it may be moved but only in an orderly way applying the three-part test with approval of the losing FHLBank. This same "principal place of business" definition should remain for insurance companies. All member classes will be treated the same (except CDFIs) and the risk of forum shopping is reduced.

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For the above reasons, I request that this regulatory proposal be withdrawn and the Regulatory Interpretation 2012-RI-02 with respect to insurance companies should also be withdrawn. Thank you for the opportunity to comment. The FHLBanks are very important to their member investors and the nation's economy. I am confident that the FHFA will carefully consider this and other public comments before finalizing this rulemaking.

Sincerely,

Milton J. Miller II