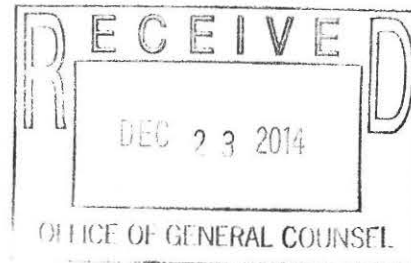




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Alfred M. Pollard, General Counsel
Attention: Comments/RIN 2590-AA39
Federal Housing Finance Agency
400 Seventh Street SW, Eighth Floor
Washington, DC 20024



Re: Notice of Proposed Rulemaking and Request for Comments – Members of Federal Home Loan Banks (RIN 2590-AA39)

Dear Mr. Pollard:

The FHFA has requested comments on a notice of proposed rulemaking (NPRM) regarding membership eligibility requirements for the FHLB System. The NPRM states that it seeks to address the System's housing finance mission and in doing so would fundamentally change the nature of the System in ways not authorized or approved by Congress. The approach taken by the FHFA in the NPRM to address these concerns, and indeed the basis for some of the concerns raised by the NPRM is fundamentally flawed, running counter both to Congressional intent for the System and to the plain meaning of the Federal Home Loan Bank Act (the Act). We detail our issues with the approach taken in the NPRM below and urge the FHFA to withdraw the rulemaking so that substantial changes can be made before moving forward.

The Proposed Rule's New Membership Requirements

The NPRM would revise the FHLB membership rules in two fundamental ways. It would impose, for the first time in the history of the System, on-going mortgage asset tests – with different tests for members of different sizes.

Under the NPRM all FHLB members would be required to hold, on an ongoing basis, one percent of assets in "home mortgage loans" as defined by the FHFA in order to satisfy the requirement that an institution make long term home mortgage loans. Further, all depository institutions that are not Community Financial Institutions (CFIs) – defined by FHFA as depository institutions at or below \$1.108 billion in assets – must also comply with an ongoing requirement that at least ten percent of their total assets are in "residential mortgage loans" as defined by FHFA. The current test to ensure that eligible

members make home mortgage loans is a one-time test upon application for membership. A prospective member must demonstrate that it has such long-term mortgage assets on its books at the time of application but has never before in the history of the System been required to comply with an ongoing test. Under the NPRM members found to be out of compliance (based on a rolling three year average) would be given one year to return to compliance. If the member remains out of compliance for two consecutive years, their membership would be terminated and would be cut off from all FHLB liquidity and services.

The NPRM runs counter to the clearly authorized mission activities of the System and to the plain meaning of the authorizing statute with regard to eligible members of the System.

Chartered by Congress in 1932 to provide liquidity for housing finance to what were then known as building and loan institutions (now savings associations) and insurance companies – the primary lenders for mortgage finance at the time, the scope of eligible membership in the System and the mission of the System have consistently been expanded by Congress in the intervening eighty two years. In 1989 membership was expanded by Congress to all federally insured depository institutions, including commercial banks and credit unions. In 1999 and in 2008 Congress expanded the categories of collateral eligible to be pledged by members for FHLB liquidity and in 2008 Congress formally recognized the FHLB's role in providing liquidity to their members without limiting that purpose to housing finance. Today, as the FHFA noted in the FHFA Strategic Plan: Fiscal Years 2015 – 2019, the Federal Home Loan Banks' "core mission is to serve as a reliable source of liquidity for their member institutions in support of housing finance and community lending."

In recent years, the FHFA has also acted to further authorize additional categories of collateral beyond those tied to housing finance, including federally insured student loans (authorized in 2009) and loans made by Community Financial Institution members of the System for community development purposes in 2010.

These actions, both Congressional and regulatory, make clear that the mission of the FHLB System has been expanded beyond housing finance. Inexplicably, the FHFA has proposed this rule in an apparent attempt to reestablish a nexus between FHLB membership requirements and the mission of the System as established by Congress. However, the rule would have the effect of substantially limiting the mission of the Federal Home Loan Banks in providing reliable liquidity to their members. By focusing membership requirements solely on residential mortgage loans and home mortgage loans, the rule ignores the many other categories of mission related assets a member may hold on its books.

The NPRM is harmful to the Federal Home Loan Banks, their members and the communities they serve.

The NPRM will make access to Federal Home Loan Bank liquidity far less certain. The imposition of on-going asset tests will result in member banks being unable to be certain of their future ability to meet the tests in all market conditions and maintain their membership and borrowing ability, especially in times of financial stress when asset values can erode rapidly. Uncertainty over the ability to borrow will harm the member bank's safety and soundness standing with their prudential regulator. Additionally,

member banks will face reduced flexibility in balance sheet management as they strive to ensure they hold the required mortgage assets on their books, even if other financial regulators express concern over holding greater amounts of mortgage assets on balance sheets. These problems are likely to be especially acute for banks that are approaching the Community Financial Institution (CFI) asset cap. A CFI that exceeds that cap, either through growth or merger, would be required to meet the 10 percent residential mortgage test or lose their FHLB membership. Thus, as they grow, they will have to distort their balance sheet management or face uncertainty as to their continued ability to borrow from the System, or both. A CFI that acquires another bank with fewer mortgage assets could fail the new test despite the fact that it may have increased its overall commitment to residential mortgage finance.

Uncertainty over continued membership eligibility also harms the entire Federal Home Loan Bank System. As members fall out of eligibility, their stock in the FHLB must be redeemed, destabilizing the capital of the individual Banks, and because the System is a joint and several one, of the entire FHLB System. While this may seem relatively inconsequential on an individual bank basis, taken as a whole, with members falling in and out of membership and in and out of their stock contribution, the entire System will be viewed by the prudential regulators and the capital markets as less stable and reliable.

With less certainty over future availability of liquidity, banks may pull back from financing certain projects and investments, harming the communities they attempt to serve. A community that might benefit from a bank's growth or merger could suffer if that growth was stifled due to concerns over continued membership eligibility.

There is no demonstrable need for the changes proposed.

The current method employed by the System to ensure that members engage in mission related lending is far superior to the tests proposed under the NPRM. Under the current method, a member may only borrow from a FHLB if it has eligible collateral to pledge. If a member does not make sufficient mission related loans, or hold sufficient mission related assets, it will not have collateral to pledge and will not be allowed to borrow further. This method is both efficient and elegant as it requires no on-going tracking and allows member institutions maximum flexibility while still ensuring that the System and its members remain focused on the broader mission of the System.

The proposed on-going asset tracking, however, will add regulatory burden for the Federal Home Loan Banks, the costs of which will undoubtedly be passed along to the members who borrow from the System, and ultimately to the customers of those member banks. The end result will be higher costs for credit. This could perhaps be justified if there was an urgent need to ensure or restore mission focused lending by the FHLBs and their members, but as the FHFA has admitted, there is no showing of such a need, as the System and its members consistently lend in a mission focused manner. It should also be noted that given the still fragile state of the American housing economy, now is not the time to impose further (and unnecessary) hurdles and higher costs on mortgage and housing related lending.

Conclusion

The importance of the Federal Home Loan Banks as a source of liquidity and other services to our respective members cannot be overstated. For that reason it is essential that the FHLB System remains well regulated and appropriately focused. While I appreciate and respect the FHFA's role in maintaining the safety, soundness and mission integrity of the System, we differ strongly with the direction taken by the FHFA on the membership proposal. I urge the FHFA to withdraw the NPRM. We urge the FHFA to revise this proposal so that it better reflects both the Congressionally defined mission of the System and the authority granted to the FHFA to ensure that the System and its members meet that mission.

Sincerely,

A handwritten signature in black ink, appearing to read "Mark R. O'Connell". The signature is written in a cursive style with a large, stylized initial "M".

Mark R. O'Connell

President & CEO

Avidia Bank