State of Washington

DEPARTMENT OF FINANCIAL INSTITUTIONS
DIVISION OF CREDIT UNIONS

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Sent via FHFA Web Portal:
www.fhfa.gov/open-for-comment-or-input
Copy to: RegComments@fhfa.gov

Subject: Federal Home Loan Bank Membership – RIN 2590-AA39

Dear Mr. Pollard:

The Division of Credit Unions of the Washington State Department of Financial Institutions (“WDCU”)[1] is writing this letter by way of official comment to the notice of proposed rulemaking dated September 12, 2014 (“Proposed Rule”), of the Federal Housing Finance Agency (“FHFA”).[2] The Proposed Rule, in our view, would establish unnecessary and counter-productive home-loan asset thresholds[3] as a condition of both initial and ongoing membership in a Federal Home Loan Bank (“FHLB”).

Ease of membership in FHLBs has been a key factor in assuring *liquidity* for community-based financial institutions – including Washington State-chartered credit unions[4] – by providing them with a ready source of low-cost wholesale funding for their operations. This, in turn, has enabled FHLB-member credit unions and community banks and thrifts to continue to remain viable in their service areas, including as a source of long-term residential home lending at a reasonable cost. While the promotion of long-term residential home lending is the

[1] The Washington State Department of Financial Institutions, as a whole, regulates Washington State-chartered commercial banks, savings banks, savings associations, trust companies and credit unions, and licenses or otherwise registers consumer loan companies, mortgage servicers, mortgage brokers, check cashers and sellers, payday lenders, money transmitters, currency exchanges, broker-dealers, investment advisors, private placement issuers, franchisors, and business opportunity offerors.

[2] 79 FR 54848 (September 12, 2014).

[3] Specifically, the Proposed Rule would change the requirements of membership in a FHLB from demonstrating at least one percent (1%) of assets in *long-term* home mortgages at time of *joining* a FHLB to requiring a one percent (1%) minimum on an ongoing permanent basis (“One Percent Rule”). Moreover, the Proposed Rule would also require that ten percent (10%) of a member’s assets be in *residential* mortgage loans in order to maintain membership (“Ten Percent Rule”).

[4] WDCU charters and is the primary regulator for *60 credit unions* in Washington State.

primary function of the FHLB system, FHLBs have over time beneficially expanded their mission, providing a range of financial products and services that member institutions rely on to address their operational and market needs. This has been necessary to aid its member institutions in maintaining proper liquidity, managing interest rate risk, and meeting loan demand – the general operational concerns which, if not addressed, would make it difficult for these community-based institutions to stay in business at all and, as a *consequence*, continue making long-term residential home-loans.

As we emerge from the general financial crisis and the economy improves, community-based financial institutions will increasingly need balance-sheet tools to effectively manage interest rate risk and liquidity. Moreover, on account of sensitivity to interest rate risk, WDCU has concerns about the credit unions it regulates holding long-term mortgage portfolios. However, the Proposed Rule, in our view, could undermine access to FHLB membership, thereby stifling credit union liquidity and making management of balance sheets and interest-rate risk significantly more difficult, especially for smaller institutions. This is particularly true when federal and state prudential regulators are mandated to emphasize these critical aspects of safety and soundness. Accordingly, we urge that FHFA not move forward with the Proposed Rule.

If, however, FHFA moves forward to adopt the Proposed Rule, we request that FHFA consider the following specific changes:

1. <u>Maintain Current One Percent Rule</u>**.** FHFA has indicated that it will increase the afore-mentioned One Percent Rule to some higher threshold, such as two percent (2%), or possibly as high as five percent (5%), as part of the Proposed Rule process. Specifically, FHFA has sought public comment on whether setting the minimum required home mortgage loans-to-total assets ratio at a percentage greater than one percent (1%) of a FHLB member's total assets would be more consistent with the statutory intent and, if so, what the appropriate percentage ought to be in a final rule (if any). Such an increase in the One Percent Rule would require that a number of WDCU's regulated credit unions increase their long-term mortgage holdings in order to maintain membership. This would come at a time when to do so would be unduly risky. A number of WDCU-regulated credit unions hold between one percent (1%) and two percent (2%) of their holdings in long-term residential mortgages. These institutions would need to inordinately micro-manage their levels of long-term residential mortgages in order to maintain FHLB membership. WDCU is of the view that the One Percent Rule is sufficient.

2. <u>Extend CFI Exemption to Credit Unions</u>. As you know, there is presently a statutory exemption from the afore-mentioned Ten Percent Rule for a federally insured community bank[5] with less than $1 billion in average total assets (adjusted annually for inflation) over the preceding three years – known under the Ten Percent Rule (and its exemption) as a *"community financial institution"* ("CFI"). Congress has not prohibited FHFA from extending by rule an exemption from the Ten Percent Rule to *credit unions* similarly

[5] Any State bank (including commercial banks and savings banks) insured by the Federal Deposit Insurance Corporation ("FDIC").

situated in size. WDCU therefore urges FHFA to extend the exemption from the Ten Percent Rule to a federally insured credit union[6] with less than $1 billion in average total assets (adjusted annually for inflation) over the preceding three years – i.e., recognize that, in this regard, credit unions are CFIs within the FHLB system the same as community banks.

3. Alternative: Do Not Impose a Preferential, Unequal Playing Field Between CFIs and Other Institutions. The NCUA and WDCU are strongly emphasizing that state-chartered credit unions maintain access to liquidity. FHLB membership is an important source of liquidity for the 60 credit unions that WDCU regulates. At present, there is no shortage of long-term credit available for home financing. Credit unions generally have excess lending capacity and are aggressively competing with each other and with other financial institutions to attract long-term borrowers. Accordingly, as WDCU sees it, the Proposed Rule would not operate to increase the consumer public's access to home mortgage loans.

4. Maintain Current Appeals Process. WDCU supports continuation of the appeals process when an applicant is denied membership. FHFA has proposed eliminating the appeals process on the grounds that: (1) FHFA's ombudsman may hear complaints or appeals; (2) there is an existing, separate process for regulatory interpretation of applicability; and there has apparently never been an appeal from denial of an application to the FHFA. In WDCU's view, this is not sufficient to maintain the appearance of fairness in the FHLB system. WDCU believes that appeal to the FHFA Director from a denial of a FHLB membership application ought to be made. WDCU is not otherwise opposed to streamlining of such an appeal process.

In conclusion, WDCU believes that the Proposed Rule is unnecessary at this time and, as currently written, would be counter-productive to the mission of the FHLB system. If, however, FHFA decides to move forward with the rulemaking process, WDCU urges the following alternatives: (1) FHFA should ***not*** increase the present One Percent Rule; (3) a credit union the same size as a CFI should be entitled to the same exemption to the Ten Percent Rule as a CFI (i.e., a small community bank); and (3) FHFA should maintain its current appeals process for FHLB membership denials.

Respectfully submitted,

WASHINGTON STATE DEPARTMENT OF
FINANCIAL INSTITUTIONS

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By:

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[6] Credit unions insured by the National Credit Union Share Insurance Fund (NCUSIF) administered by the National Credit Union Administration ("NCUA").