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

January 8, 2015

Re: Notice of Proposed Rulemaking; Request for Comments – Members of the Federal Home Loan Banks

Dear Mr. Pollard:

The Illinois League of Financial Institutions (ILFI) is submitting this comment to express concerns about the Federal Housing Finance Agency's (FHFA) notice of proposed rulemaking and request for comments on "Members of the Federal Home Loan Banks" published on September 12, 2014. For the reasons described below, we respectfully request the withdrawal of this proposal.

The Illinois League of Financial Institutions (ILFI) is a statewide banking trade association dedicated to furthering the viability of thrifts and community banks in Illinois.

Prior to assuming the post of President of the ILFI, I served as an Assistant Commissioner of the Illinois Office of Banks and Real Estate. As a banking regulator for more than 15 years, I observed numerous instances of across-the-board regulation and the unintended consequences of such actions. This approach can penalize otherwise well-capitalized community based thrifts and banks as well as insurance companies in the specific case of this proposed rule. A litmus test to retain membership in the Federal Home Loan Bank System is unneeded and seemingly contrary to the intentions of the Congress.

As shareholders and customers, thrifts, banks, and insurance companies view their access to FHLB of Chicago advances as critically important because the liquidity allows them to offer an array of loan products to their customers that they might not otherwise be able to offer. The FHLB of Chicago's products such as advances, letters of credit and the Mortgage Partnership Finance® Program are tremendous resources that enable financial entities in Illinois to better serve this state's home buying, small business and agricultural customers.

The proposed rule would impose, for the first time ever, on-going requirements for members to meet as a condition of remaining a member of the FHLB of Chicago. The proposal would require a member to hold at least 10 percent of total assets in residential mortgage loans at all times. An additional test would require the maintenance of at least 1 percent, and contemplates as much as 5 percent, of assets in a separately defined group of long-term home mortgage loans. Failure to meet either proposed test would result in the eventual termination of membership.

The practical consequences of this proposal would be severe. A thrift or bank's ability to rely on the liquidity provided by the FHLB of Chicago, particularly in times of economic distress, would be seriously undermined if the FHFA is allowed to establish requirements that must be met simply to remain a FHLB of Chicago member. This has never been the case in the 82-year history of the FHLBs. Membership in the FHLBs has been steadily expanded by Congress over the years, never contracted and never once given - restricted. With the imposition of such a requirement, thrifts and banks could never be assured that when the next financial crisis occurs they will have continued access to FHLB liquidity. And even if thrifts and banks meet the proposed threshold today, they would need to continually manage their balance sheets with the proposed requirements in mind going forward. Future decisions regarding asset allocation would need to bear these requirements in mind.

A direct consequence of this rule would also necessitate additional examination reviews by the prudential safety and soundness regulators to question thrift and bank liquidity policies and procedures. Most Illinois thrifts and many banks list access to the FHLB Chicago as their first line of defense when there is a problem with liquidity. Your proposed rule would raise the possibility that membership in the FHLB could be called into question and access to liquidity placed in doubt at a critical economic time in the future. This in turn will force the primary regulators to require thrifts and banks to have additional back up liquidity sources and probably back up resources to the back ups. This additional scrutiny and concern is solely raised by adoption of this rule which is a primary reason why the ILFI opposes it.

All financial institutions in Illinois, even the traditional thrifts, make a variety of loans. The proposed rule effectively mandates a portion of balance sheets to be devoted to long-term home mortgage loans (meaning a term to maturity of five (5) years or greater) at all times as a condition of remaining a FHLB of Chicago member. Asset allocation potentially could become over-invested in housing related assets at the expense of small business lending and other commercial loans, consumer loans or other asset classes. This result also would contradict the intent of Congress, which has explicitly recognized the FHLBs' mission of providing liquidity to members **without limiting that purpose to housing finance**. By seeking to establish a housing finance nexus that all FHLB members must meet, the proposal does not appear to recognize the legitimate uses of FHLB funding beyond housing finance activities.

This proposal could lead to the politicization of FHLB membership. If the FHFA can require ongoing eligibility requirements for members, what is to prevent it from increasing those thresholds, or imposing entirely new requirements, in the future? This proposal might simply be the first of many such eligibility requirements imposed upon FHLB members, purportedly in an effort to ensure a sufficient housing finance nexus is maintained at all times by members. The FHFA director is a political position, appointed by the President and confirmed by the U.S. Senate. What would prevent a future FHFA director from requiring FHLB members to hold yet more housing loans or other types of assets on their balance sheets in order to achieve a certain political agenda? Such fears are not unfounded. Past Administrations from both political parties increased housing goals for Fannie Mae and Freddie Mac in an effort to increase the level of homeownership and serve politically favored constituencies, with disastrous results.

A similar concern exists as to the ability to terminate the memberships of current FHLB members without any showing of cause. Under the proposal, the current memberships of captive insurance companies would be terminated regardless of the amount of home mortgage loans they hold on their balance sheets. This would occur despite the fact that captives are insurance companies, which have been eligible to be FHLB members since the FHLBs were created by Congress in 1932. If the FHFA can terminate the memberships of a certain class of insurance companies, it raises a legitimate concern as to what, if anything, would prevent the FHFA in the future from terminating the memberships of other types of current members, potentially any Illinois thrift or bank, for any reason the FHFA sees fit. Such an outcome would destroy any confidence in the FHLBs as sources of stable and reliable liquidity. The FHFA would be opening a Pandora's Box if it approves the rule as proposed.

The overall intent of this proposal seems to restrict and narrow FHLB membership, resulting in fewer members. As some members have their memberships terminated, and others, such as smaller members, are encouraged to reduce their usage in order to avoid crossing the arbitrary threshold for community financial institutions, there is concern about the destabilizing effects that would result. These actions will inevitably lead to smaller FHLBs with fewer assets, reduced profits, lower retained earnings, and a decreased market value of equity and capital stock. Additionally, as usage contracts and profits decline, fewer dollars will be available to support the FHLB's economic development programs. The ability of Illinois thrifts and banks to serve their communities through valuable products such the FHLB's down payment assistance grants, Community Investment Cash Advances and Affordable Housing Program grants would be harmed.

Beyond these destabilizing effects, this proposal does nothing to help strengthen the overall financial system. Since the financial crisis, the nation's prudential regulators have increasingly emphasized liquidity planning in an effort to prevent another crisis from occurring. Illinois thrifts and banks have painstakingly designed liquidity plans which rely on access to same-day funding offered by the FHLB of Chicago. The regulators understand and accept the vital role of the FHLBs in such planning. This proposal contradicts these efforts by undermining the reliance of banks on the FHLBs. In so doing, it threatens to weaken the broader financial system while doing nothing to help prevent a repeat of the financial crisis.

Nor does the proposal do anything to help repair and restart the struggling housing markets. Many community thrifts and banks rely upon the FHLBs' MPF® Program to access the secondary mortgage market. This innovative program has been popular with FHLB members because it allows access to the secondary mortgage market on competitive terms while retaining customer relationships. The traditional MPF products also pay participating members monthly fees to manage the credit risk of their own loans, in contrast to the guarantee fees charged by Fannie Mae and Freddie Mac. Rather than furthering this program, however, the proposal would only harm it by encouraging members to hold more mortgage loans on their own balance sheets, rather than selling them. Moreover, to the extent the proposal discourages FHLB membership and terminates existing memberships, it will only limit access to housing finance and the secondary market. Again, this seems to directly contradict the efforts of the Administration, the Congress, and others to increase the availability of mortgage credit, particularly for lower income families.

This proposed rule would also harm the financial system by adding to the growing regulatory burden on thrifts and banks that impedes their ability to efficiently operate and best serve their customers and shareholders. Thrifts and banks across the country are struggling under the weight of an extensive regulatory regime imposed in recent years, despite the fact that these entities were not the cause of the financial crisis. Recent legislative and regulatory requirements include the Patriot Act, the Bank Secrecy Act, anti-money laundering rules, the Dodd-Frank Act and accompanying Qualified Mortgage and Qualified Residential Mortgage rules, and new Basel III-like capital and liquidity requirements. This proposal from the FHFA only adds to this burden and may cause thrifts and banks to rethink the practicality of remaining an FHLB member.

In conclusion, the Illinois League of Financial Institutions, on behalf of our thrift and bank members, view the FHLB of Chicago as a critical partner. The reliability of the FHLB of Chicago as a liquidity source must be preserved. Threatening access to the FHLB of Chicago threatens thrifts and banks in Illinois, their customers and the communities in which they operate. This proposal would undermine the reliability of the FHLB of Chicago, discourage membership, politicize FHLB of Chicago membership, limit access to the secondary market and shrink the FHLB of Chicago's affordable housing and community development activities. **It will do nothing to help the effort of other banking regulators to strengthen the overall financial system or repair the struggling housing markets**. Despite these real and damaging effects, as a former regulator, I can see no specific benefits that would be achieved by this proposal. The costs clearly outweigh the benefits. For these reasons, I strongly urge the immediate withdrawal of this proposal.

I appreciate the consideration of our views and the opportunity to comment on behalf of the community thrifts and banks in Illinois who are members of ILFI and the FHLB Chicago.

Yours very truly,

Jay R. Stevenson
President