FEDERAL HOME LOAN BANK OF DALLAS

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January 12, 2015

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

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

Dear Mr. Pollard:

On behalf of the Federal Home Loan Bank of Dallas (the "Dallas Bank"), thank you for the opportunity to provide these comments to the above notice of proposed rulemaking published on September 12, 2014 (the "Proposal"), and for the extension of time that was granted by the Federal Housing Finance Agency ("FHFA") to comment on the Proposal.

The comments provided in this letter focus on the aspects of the Proposal related to new ongoing balance sheet composition requirements for members of Federal Home Loan Bank (each a "Bank" or "FHLB"). In addition, the Dallas Bank is submitting a separate comment letter that focuses on the principal place of business for insurance companies.

The Dallas Bank agrees with the FHFA that it is important to encourage our members to engage in activities that further the housing finance mission of the Federal Home Loan Banks. However, we believe that the current regulatory regime is effective in accomplishing this goal. For that reason, it appears the potential benefits of some elements of the Proposal are outweighed by the likely significant costs to the Federal Home Loan Banks and, more important, to our members.

Current FHFA Regulations Already Maintain a Mission Focus

Regarding the proposal to require all Federal Home Loan Bank members to maintain one percent of assets as long-term home loans and certain members to maintain ten percent of assets as residential mortgage loans, we do not believe the Proposal provides sufficient data in support of the proposed changes. In addition, we are concerned that the proposed changes could have far-reaching negative effects for our members.

The Proposal notes that an overwhelming majority (ninety-eight percent) of Federal Home Loan Bank members currently would be in compliance with the proposed balance sheet requirements. The Proposal cites this figure to establish that the proposed new requirements would cause minimal disruption to the Banks and our members. However, the statistic could just as readily be cited as evidence that the proposed balance sheet targets are already being met for the large majority of Bank members without the imposition of an ongoing asset maintenance requirement. Indeed, it appears the Proposal does not fully take into account the effectiveness of the current regulatory regime in maintaining the engagement of Federal Home Loan Bank members in mission-related activities.

Access to advances is one of the key benefits of Federal Home Loan Bank membership, and advances can only be accessed by members that pledge mission-related eligible collateral. Our members are able to borrow only when they have acceptable assets to pledge as collateral, and only to the extent they pledge that collateral. Overwhelmingly, those pledged assets are housing-related. In addition, advances with a term-to-maturity of greater than five years can only be used for housing finance purposes. Bank members also must hold capital stock in proportion to their advances activity. Further, in order to access long-term advances, members who are randomly selected every two years must complete a required Community Support Statement through which the member certifies that it actively supports the first-time homebuyer market.

All of these factors help to ensure that Federal Home Loan Bank members are engaged in activities consistent with the mission of the FHLB System. The fact that ninety-eight percent of Federal Home Loan Bank members already maintain mortgage-related assets at the desired levels demonstrates that the current regulatory regime is effective, and confirms that the FHFA's concern with members maintaining a mission focus is already being addressed without the need to impose new regulatory requirements.

<u>The Proposed Balance Sheet Requirement Risks Significant Harm</u>

Not only is a new balance sheet requirement unnecessary, it could come at a substantial cost to the Federal Home Loan Banks and, more important, to their members. Our members look to the Banks as a dependable source of liquidity in good times and bad. The balance sheet requirement would introduce uncertainty about an institution's ongoing membership status and future ability to access Bank advances. Members that cannot meet the asset composition requirements will face termination of their membership and lose the access to advances and other services that make FHLB membership valuable. In addition, members that <u>do</u> meet the proposed one-percent asset requirement for long-term home mortgage loans cannot be certain this minimum will not be raised in the future. Indeed, the Proposal suggests that the FHFA already has considered raising the requirement to two or five percent. The stability and reliability that our current and prospective members value may be significantly undermined by the imposition of an ongoing and possibly open-ended balance sheet requirement.

The proposed balance sheet requirement is especially troublesome for those Federal Home Loan Bank members that are designated as Community Financial Institutions ("<u>CFIs</u>"). (CFIs are depository institutions with average total assets below a threshold set annually by the FHFA,

$1,108,000 for 2014.) Under the Proposal, CFIs would not be subject to the ten-percent residential mortgage asset requirement. However, a CFI that grows to exceed the CFI asset threshold either organically or through merger would become subject to the ten-percent requirement. Historical data show that from 2008 to the present, more than three hundred Federal Home Loan Bank member institutions have either lost or gained their CFI status during that period. An asset requirement that is tied to a member's designation as a CFI would not only penalize the member's growth but would also introduce new uncertainty for members that operate near the CFI threshold.

A particular concern with the proposed asset maintenance requirement is that it focuses on only one method of providing support to the Federal Home Loan Banks' housing finance mission – holding mortgage assets on the member's balance sheet. Federal Home Loan Bank members engage in a range of activities and employ a variety of structures and business models. Consequently, members may support the Banks' housing finance mission by methods other than holding mortgage assets on balance sheet, including activities such as providing warehouse funding, maintaining a mortgage origination platform to support residential mortgage originators, and originating mortgage loans for delivery through the Federal Home Loan Banks' MPF Program. By focusing solely on balance sheet requirements, the Proposal fails to take into account members' other significant roles in supporting housing finance.

Introducing a new balance sheet requirement also could require members to artificially manage their year-end balance sheets to comply with the requirement, and could require members to manage greater interest rate risk than desired. In short, the imposition of an ongoing balance sheet requirement would make Bank membership a less attractive, and less valuable, option to both current and prospective Federal Home Loan Bank members.

In addition to the potential impact on current Bank members, the elimination of existing and potential members would result in decreased revenues for the Federal Home Loan Banks which would, in turn, result in decreased funding for the Banks' Affordable Housing Programs. Section 10(j) of the Federal Home Loan Bank Act requires each Federal Home Loan Bank to establish an Affordable Housing Program ("AHP") through which the Bank provides subsidies in the form of direct grants and below market interest rate advances to members who use the funds to assist with the purchase, construction, or rehabilitation of housing for very low-, low-, and moderate-income households.

During 2014, the Dallas Bank awarded $9.8 million in AHP grants to 33 affordable housing projects primarily within the Dallas district. Those grants will result in the creation or rehabilitation of 1,586 new housing units. Since the Affordable Housing Program's inception in 1990, the Dallas Bank has awarded more than $237 million in AHP grants to help approximately 44,000 families obtain safe, affordable, and quality housing.

In addition to the required Affordable Housing Programs that are tied to income, the Dallas Bank has also contributed additional funds to several voluntary programs including: (1) $10 million toward housing and economic development needs in the wake of Hurricanes Katrina, Rita, Gustav and Ike; (2) $1 million each year beginning in 2002 in economic development grants to businesses that qualify for a CICA economic development advance; (3) $225,000 each year beginning in 2002 in grants to assist qualified non-profit organizations that compliment development activities supported by the Bank's affordable housing, community investment, and economic development programs; and (4) $250,000 committed in 2011 to assist wounded warriors who were disabled as a result of their active military service since September 11, 2001.

The households and communities that benefit from the Affordable Housing Programs tied directly to net income, as well as those that benefit from housing and economic development programs voluntarily funded by the Banks, would be especially impacted by the Federal Home Loan Banks' decreasing income levels that would result from the Proposal.

The Proposal Conflicts with Congressional Intent

The proposed balance sheet requirements appear to be in conflict with the desire of Congress, which in recent decades has expanded both the range of institutions that may qualify for Federal Home Loan Bank membership and the types of collateral that Bank members may pledge to obtain advances.

For example, in 1989 the Financial Institutions Reform, Recovery and Enforcement Act expanded FHLB membership beyond savings banks, thrifts, and insurance companies to include eligible commercial banks and credit unions. In 1999, the Gramm-Leach-Bliley Act once again broadened the scope of the Federal Home Loan Banks' mission by expanding collateral eligible to be pledged to the Banks by CFIs to include small business and agricultural loans. Finally, with the passage of the Housing and Economic Recovery Act of 2008, Congress made clear that the FHLB System's primary mission had evolved from simply "housing finance" to a more general role as provider of liquidity to our members. The Proposal's narrow focus on housing-related assets appears to be in conflict with the expansive view of the Banks' mission that Congress has expressed through legislation in recent decades.

Conclusion

As noted above, we believe the current regulatory regime is adequate to ensure alignment between the Federal Home Loan Banks' mission and their members' business activities. Given the far-reaching effects of the regulatory changes included in the Proposal, the Dallas Bank encourages the FHFA to reconsider the elements of the Proposal related to imposition of an ongoing asset composition requirement on Federal Home Loan Bank members.

Thank you again for your time and attention to these important policy issues.

Sincerely,

Sanjay Bhasin
President and Chief Executive Officer