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January 12, 2015

Mr. Alfred M. Pollard
General Counsel
Federal Housing Finance Agency
400 7th St. SW, Eighth Floor
Washington, DC 20024

Re: Comments on Proposed Changes to Federal Home Loan Bank Membership Requirements/RIN 2590-AA39

Dear Mr. Pollard:

The Credit Union National Association (CUNA) appreciates the opportunity to submit comments to the Federal Housing Finance Agency (FHFA) regarding its proposal on membership requirements for Federal Home Loan Banks (FHLBs). By way of background, CUNA is the country's largest credit union advocacy organization, representing our nation's state and federal credit unions, which serve over 100 million memberships from around the country.

Summary of CUNA's Comments

CUNA is adamantly opposed to the proposed regulation and urges FHFA to withdraw it. We do not believe the proposed changes are warranted or required to meet statutory requirements. Moreover, we do not believe the agency has provided sufficient analysis as to why the proposed membership requirements are needed. Most important, we are concerned the proposal would require FHLB-member credit unions to make business decisions that may not be in their members' overall best interests. If this proposal does move forward, at a minimum, we urge FHFA to correct the disparate treatment between banks and credit unions as discussed in this letter.

The proposal would require all financial institutions that are FHLB members to hold one percent of their assets in "home mortgage loans" on an ongoing basis. The proposed regulation suggests that FHFA is considering raising this requirement to as high as five percent in the future. While financial institutions currently must meet a one percent-of-assets threshold to become FHLB members, there is no current requirement that FHLB members must maintain the threshold.

All FHLB-member credit unions—but only certain FHLB-member banks—would also be required to hold 10% of assets in "residential mortgage loans" on an ongoing basis. As with the one percent test, the 10%-of-assets threshold would have to be met by the institution in order to become a FHLB member, but there is no requirement now that members must ensure the threshold level is continued in order to remain a member. By statute, for initial membership, the Federal Home Loan Bank Act exempts from the "10 percent" requirement any "community financial institution" or "CFI," defined as FDIC-insured banks with less than $1 billion in average total assets (adjusted annually for inflation) over the preceding three years. Under the proposal, FHFA has decided to maintain the "CFI" exemption without any variation. As a result, no credit union can be considered a "community financial institutions" for purposes of maintaining membership if the rule is adopted as proposed. If this proposal does move forward, at a minimum we urge FHFA to correct the disparate treatment between banks and credit unions.

The Proposed Regulation is Unnecessary, as Financial Institutions are Engaging in Sufficient Mission-Related Lending Under Current Rules

The research and data FHFA provided in the preamble to this proposal show that the vast majority of FHLB members – roughly 98 percent – already comply with the proposed requirement to hold at least 10 percent of assets in "residential mortgage loans" on an ongoing basis. For the remaining two percent, roughly half have more than 9 percent of their assets in mortgages. However, if the proposal is adopted, rather than allowing a commitment to housing to develop organically in the normal course of business, the proposal would require credit unions to constantly monitor their mortgage loan levels and face the loss of FHLB membership if they fail to maintain lending levels that are not required by law.

We believe the existing FHLB structure is sufficient to ensure mission-related lending is always a major priority for member financial institutions. Each credit union must buy stock in the FHLBs, meet the 1% and 10% requirements at the time the institution initially seeks membership, provide "eligible collateral" related to housing when it seeks an advance from its FHLB, and be subject to random selection every two years by FHFA to complete a Community Support Statement.

This structure creates a natural check and balance: if a FHLB member does not make sufficient mission-related loans, or hold sufficient mission-related assets, it will not have collateral to pledge. Further borrowing will not be allowed until that collateral is available. This existing structure does not require on-going tracking, artificial asset tests, and does not create balance sheet management stress for financial institutions, yet still achieves FHFA's overall objective of promoting mission-related lending.

We recognize FHFA has an interest in ensuring that FHLB members maintain a commitment to housing finance. However, we do not believe that this proposal is necessary to achieve that objective, especially since the agency has not demonstrated that the proposed changes are warranted in light of the results the current system has produced**.**

The Proposal Could Cause Unintended Harm to Credit Unions, the FHLB System, and the Housing Market

There is no way to know with precision what the impact of the proposal would be, and the agency has not provided sufficient analysis regarding the proposal's impact. Our preliminary analysis leads us to conclude that the proposal would have numerous unintended consequences for credit unions, the FHLB System, housing finance and communities.

A. The Proposal Would Require Credit Unions to Needlessly Alter Business Practices

This proposal would create major compliance responsibilities for credit unions, which will be forced to maintain a close watch over their balance sheets to ensure they meet an arbitrary asset requirement on an ongoing basis. Because credit unions will need to continually monitor the amount of assets directed to housing, the regulation would artificially distort balance sheet management practices. The proposal would decrease the flexibility of credit unions to manage their assets and liabilities in response to changing market conditions.

B. The Proposal Would Harm the FHLB Stem and Result in Higher Cost Mortgages

The on-going asset tracking that would result under the proposal would also add regulatory burdens for the Federal Home Loan Banks. Under the proposal, each FHLB would be responsible for ensuring that its members are in compliance with these arbitrary asset thresholds. The FHLB would terminate financial institutions that do not comply. This would change the nature of the relationship between each financial institution and its FHLB from one of cooperation to one of enforcement. More to the point, the compliance costs of each FHLB will undoubtedly be passed along to the financial institutions that borrow from the system. The end result will be higher costs of credit for consumers. Given the still fragile state of the American housing sector, now is not the time to impose further (and unnecessary) hurdles and higher costs on mortgage and housing related lending. This proposal could also cause communities across the country and the housing market to suffer. That is because the net effect of the proposal could be to restrict access to mortgage credit for consumers because access to

the low-cost sources of funding provided by the FHLBs for credit unions could be jeopardized.

Uncertainty over a financial institution's continued membership eligibility would harm the entire Federal Home Loan Bank System. The FHLB system requires the purchase of stock by member financial institutions. However, institutions that are unable to meet ongoing requirements will need to redeem their stock. A large number of redemptions at a particular FHLB could change the capital structure at an individual FHLB, potentially destabilizing the bank. In turn, because the FHLB System is joint and several, this could have negative consequences for the entire FHLB System.

This outcome could have important implications regarding the desirability of the FHLB system as a source of liquidity for financial institutions. The possibility that FHLB members may fall in and out of membership—and in and out of their stock contribution—could cause the entire FHLB system to be viewed by the prudential regulators as less stable and reliable. This is not an academic conclusion; our own recent experience with the National Credit Union Administration confirms this is what will happen if FHFA adopts this rule. Credit unions fought for FHLBs to be included as sources of emergency liquidity for credit unions. However, NCUA's emergency liquidity rule, finalized at the end of 2013, did not allow FHLBs to be seen as an acceptable source—precisely because the agency saw them as too uncertain.

C. The Proposal Could Curtail Credit Union Mergers

CUNA is also concerned about the rule's potential impact on credit union mergers. Because the rule proposes arbitrary tests based on an institution's balance sheet for maintaining FHLB membership, credit unions that do not issue mortgages or own mortgage-related assets may be seen as undesirable merger partners for credit unions that are FHLB members—especially if the acquiring institution is close to the asset thresholds. Even though a merger may allow a financial institution to increase its commitment to mortgage finance in the long run, the proposal has the potential to stifle consolidation that would have benefitted credit union members.

The Proposed Regulation is Inconsistent With Other Federal Financial Regulations, and Puts the Safety and Soundness of Financial Institutions at Risk

We note that the philosophy behind this proposed regulation seems fundamentally at odds with regulations from other agencies. NCUA's proposed risk based capital rule and the Basel III-based capital rules for banks both limit

concentration in specific asset classes. Here, FHFA is *requiring* concentration in residential mortgages.

While FHLB-member credit unions would presumably retain more than 10 percent of their balance sheets in residential mortgage-related assets in any case—given that over 32 percent of aggregate credit union assets are in first or second mortgages—we think that individual FHLB-member credit unions should have the flexibility to dip below the 10 percent asset threshold without penalty if doing so is necessary for safe-and-sound asset and liability management purposes.

If this Proposal Proceeds, FHFA Must Correct the Unfair and Discriminatory Treatment Between Banks and Credit Unions

If there is going to be a regulation, FHFA should at least provide parity so that community banks and credit unions are treated equally for purposes of maintaining membership. While the FHLB Act does not allow credit unions to be considered "Community Financial Institutions" for purposes of securing FHLB membership, Congress has provided sufficient flexibility to FHFA in setting the requirements for maintaining membership to address this concern. All credit unions should be treated as CFIs for purposes of maintaining FHLB membership.

Conclusion

We urge FHFA to consider the uncertain but likely consequences that could flow from this proposal, and we believe that if the agency does so, it will conclude that it must withdraw the proposal. As then-Chairman Barney Frank of the House Financial Services Committee noted when FHFA first put out an Advance Notice of Proposed Rulemaking (ANPR) on this topic more than four years ago,

> [E]xisting regulations seem to me to be functioning properly, [and] I do not see a reason to change them now. As the FHFA notes in the ANPR, it does not have any evidence that significant numbers of members that were required to hold 10 percent of their total assets in residential mortgage loans in order to join the [FHLB] system have substantially reduced their holdings after becoming members … The FHLB system plays an important role in helping to provide liquidity in the financial system, and I believe that changes to the membership requirements could have the unintended consequence of disrupting the stability of the FHLB system while our economy is still struggling.

FHLB liquidity was a critical resource during the last financial crisis and the proposed regulation would limit its utility in a future crisis. We hope FHFA will

reconsider this proposal, and we look forward to working with the agency to ensure FHLB membership for credit unions is always accessible.

Thank you for the opportunity to express our views on FHFA's proposed rule on FHLB membership eligibility. If you have any questions about our comments, please do not hesitate to contact me at (202) 508-6736.

Sincerely,

Mary Mitchell Dunn
Deputy General Counsel