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September 11, 2015

Robert E. Feldman, Executive Secretary  
Attention: Comments  
Federal Deposit Insurance Corporation  
550 17th Street N.W.  
Washington, DC 20429

RIN 3064-AE37

Dear Mr. Feldman:

I am submitting this comment on the FDIC's notice of proposed rulemaking, Assessments, RIN 3064-AE37, on behalf of the Council of Federal Home Loan Banks, a trade association whose members are the 11 Federal Home Loan Banks (FHLBanks).<sup>1</sup>

We support the efforts of the FDIC to improve the current deposit insurance assessment system for small insured depository institutions that have been federally insured for at least five years ("established small banks"). Adjusting premiums to effectively reflect the risk posed by these banks is an important goal, and incorporating newer data from the recent financial crisis should further this objective. We are concerned that the negative value multiplier assigned to the "Core Deposits/Total Assets" ratio unnecessarily raises the cost for established small banks to use FHLBank Advances in addition to core deposits when it is prudent for them to do so. Unlike core deposits, FHLBank Advances provide these banks with highly effective liquidity and interest rate risk management tools, making it easier for them to meet their safety and soundness objectives. As a result, FHLBank members have typically used FHLBank Advances to substitute or replace more costly and more volatile deposits. We believe that any final rule should not include provisions that could have the effect of discouraging the use of FHLBank Advances for liquidity management and interest rate risk management.

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<sup>1</sup> Created by Congress in 1932, the FHLBanks are 11 regional banks, cooperatively owned and used to finance housing and community investment. Approximately 7,000 lenders nationwide are members of the FHLBank System, and the FHLBanks' 5,760 commercial bank and thrift institution members represent over 80 percent of all FDIC insured institutions in the country. The FHLBanks and their members have been the largest and most reliable source of funding for community lending for over eight decades.

As discussed below, we believe that the experience from the crisis demonstrates that access to and use of FHLBank Advances reduces risk, especially for smaller banks that may not have access to other liquidity providers. It is important to recognize the safety and soundness benefits afforded by the FHLBanks in this rulemaking process. We therefore urge you not to include in the final rule provisions that could have the direct or indirect effect of discouraging established small bank members from being active participants in the FHLBank System.

FHLBank members have been encouraged (and in some cases, required) by their regulators to develop multiple sources of reliable liquidity, and evaluate those sources in a stressed environment. While most sources of funding may have proven unreliable during the financial turmoil that began in 2007, the FHLBanks demonstrated their reliability as a liquidity provider notwithstanding tremendous market dysfunction and extreme stress.<sup>2</sup> This is a role that the FHLBanks have performed repeatedly since they were established by Congress in 1932. As recently as 2008, the Congress recognized that a primary mission of the FHLBanks is to provide liquidity to their members.<sup>3</sup>

FHLBank Advances play a crucial role in helping to strengthen the banking system during periods of stability as well as crisis. Not only do Advances serve an instrumental role in helping banks with their liquidity needs, the variety of Advance products, programs and tenors enable member banks to manage interest rate risk. In a future rising interest rate environment, FHLBank Advances should continue to play an important role in helping banks control their asset liability and liquidity exposures.

Members use FHLBank Advances to fund new originations and existing portfolios of mortgages, to purchase mortgage-backed securities, and to manage the substantial interest rate risk associated with holding mortgages in portfolio. Some members layer in term Advances alongside their deposits, altering the duration profile of their liabilities to better suit their assets and mitigate risk. Other members use shorter-term, on-demand liquidity to offset unexpected deposit runoff or to take advantage of an opportunity to quickly add assets. By enabling members to effectively manage their balance sheets, FHLBank Advances help members lower their risk as well as the cost of extending credit to U.S. consumers.

Access to FHLBank Advances can reduce the amount of low-yielding liquid assets a member would otherwise hold to ensure the same amount of liquidity. In addition, because

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<sup>2</sup> Unlike deposits, funds from Advances are not subject to unexpected fluctuations due to circumstances outside the control of an FHLBank member. The recent credit crisis has shown that deposits may be lost due to disintermediation arising from a variety of factors, both expected (e.g., term promotions in a particular market or the existence of higher returns to depositors on alternative assets) and non-expected (e.g. perceptions that an institution is close to failure or FDIC take-over). The credit crisis also showed that the money and capital markets have not functioned well as long-term, stable providers of wholesale funds, even for those institutions that can normally look to Wall Street for replacement liabilities.

<sup>3</sup> Section 1201 of the Housing and Economic Recovery Act of 2008 (“HERA”), Pub. L. 110-289, 122 Stat. 2654 (2008), codified at 12 U.S.C. 4513.

members may originate loans that are not sold in the secondary market, Advances can serve as a funding source for a variety of loans held in portfolio. FHLBank Advances can also provide interim funding for those members that choose to sell or securitize their mortgages. FHLBank Advances can also be a source of funding to smaller lenders that may not have access to all of the funding options available to larger financial institutions.

FHLBank credit products also aid members in asset and liability management. The FHLBanks can offer Advances that have amortization schedules that are structured to match the maturity and payment characteristics of mortgage loans. These Advances can reduce a member's interest rate risk associated with holding long-term, fixed-rate mortgages. In addition, an FHLBank may make commitments for Advances to a member covering a predefined period, aiding members in cash-flow planning, and enabling members to reduce funding risk. Each FHLBank develops its Advance programs to meet the particular needs of its members and offers a wide range of fixed and variable-rate Advance products, with different maturities, interest rates, payment characteristics, and optionality.

During the worst part of the financial crisis, the FHLBanks dramatically increased their lending to member institutions in every part of the country. Between the second quarter of 2007 and the third quarter of 2008, the FHLBanks increased their lending to members by \$370 billion, from total outstanding Advances of \$650 billion in the second quarter of 2007 to over \$ 1 trillion in the third quarter of 2008. The crucial role played by the FHLBanks was recognized in an extensive study prepared by the staff of the Federal Reserve Bank of New York. This study found that during the financial crisis the Federal Home Loan Bank System was "by far, the largest lender to U.S. depository institutions while most of the Federal Reserve's liquidity operations have been for the benefit of non-depository institutions or foreign financial institutions."<sup>4</sup> The backstop role played by the FHLBanks was also recognized by William Dudley, President of the Federal Reserve Bank of New York, who noted that when the interbank lending market dried up in 2007, depository institutions turned to the Federal Home Loan Bank System for needed liquidity.<sup>5</sup>

The FHLBanks are able to grow to meet member demand for Advances in financial panics because of the following: 1) their active and continuous market presence ensures investor awareness; 2) their unique funding and capital structure is designed to fulfill its legislative mandate in all economic scenarios; and 3) investor preference shifts from lower-quality and risky investments to higher-quality, low risk instruments, including FHLBank debt (Consolidated Obligations) during market distress. During the financial crisis the FHLBanks accessed the debt markets continuously throughout, and, as a result, reliably provided essential liquidity to members in the form of Advances.

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<sup>4</sup> Federal Reserve Bank of New York, Staff Report No. 357 at pages 28-29 (November, 2008).

<sup>5</sup> "May You Live in Interesting Times," Remarks of William Dudley, Executive Vice President of the New York Fed, October 17, 2007.

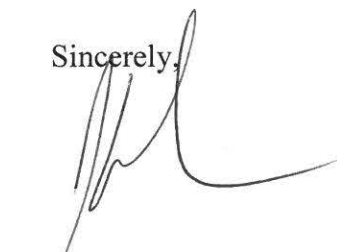
The resources of all 11 FHLBanks support the System's Consolidated Obligations. The System's Consolidated Obligations have always been highly rated and marketable. The FHLBanks are therefore able to safely and reliably fund increased demand for Advances from their members. Furthermore, as designed by statute, the capital of FHLBanks grows as demand for Advances increases because member institutions are required to capitalize additional Advances by purchasing FHLBank stock. This capital structure enabled the FHLBanks to grow safely and soundly during the financial crisis, fulfilling the liquidity needs of members throughout a time of extreme stress while simultaneously controlling risk because the member that borrows provides the capital for the borrowing.

The FHLBanks regularly interact with and monitor their members, reviewing among other things, federal regulatory reports and records relating to FHLBank members. The FHLBanks use the information available to them and, under certain circumstances, work closely with their members' primary regulators in meeting their members' liquidity needs in a prudent and responsible manner. In 2007 and 2008, the FHLBanks continued to provide liquidity to their members as long as there was sufficient collateral and, consistent with Federal Housing Finance Agency regulation and using their discretion, did so for capital deficient members, as long as the appropriate regulatory authorities did not exercise discretion to prohibit a member from additional borrowing from an FHLBank.

Therefore, recent history has shown that FHLBank Advances are a reliable source of funding in good times as well as times of economic stress. Consequently, we are concerned that the proposed assessment measures would penalize a bank for using FHLBank Advances, as opposed to increased reliance on deposits, for its funding needs. Since the proposed rule would not include FHLBank Advances in "core deposits," the proposed "Core Deposits/Total Assets" measure would raise the assessment amount on an established small bank that makes greater use of FHLBank Advances. Therefore, we urge you not to include in the final rule provisions that could have the direct or indirect effect of discouraging small bank members from using FHLBank Advances and being active participants in the FHLBank System.

Thank you for the opportunity to comment on the notice of proposed rulemaking on Assessments. If you have any questions I can be reached at 202 955-5737 or [johnvon@cfhfb.org](mailto:johnvon@cfhfb.org).

Sincerely,



John von Seggern  
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Council of FHLBanks