INDEPENDENT COMMUNITY
BANKERS of AMERICA®

November 1, 2022

Hon. Michael S. Barr
Vice Chair for Supervision
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551

Hon. Martin J. Gruenberg
Acting Chairman
Federal Deposit Insurance Corporation
550 17th Street, SW
Washington, DC 20429-9990

Hon. Michael J. Hsu
Acting Comptroller of the Currency
Office of the Comptroller of the Currency
Constitution Center
400 Seventh Street, SW
Washington, DC 20219

Sandra Thompson
Director
Federal Housing Finance Agency
400 7th St. SW
10th Floor
Washington, DC 20219

RE: Regulatory Alignment for FHLB Advances

Dear Vice Chair Barr, Acting Comptroller Hsu, Acting Chairman Gruenberg, and Director Thompson,

The Independent Community Bankers of America (ICBA)[1] is writing you to underscore our concerns that a regulatory inconsistency between the Federal Housing Finance Agency (FHFA) and the Primary Federal Regulators (PFR) is inhibiting otherwise safe and sound community

[1] The Independent Community Bankers of America® creates and promotes an environment where community banks flourish. ICBA is dedicated exclusively to representing the interests of the community banking industry and its membership through effective advocacy, best-in-class education, and high-quality products and services.

With nearly 50,000 locations nationwide, community banks constitute roughly 99 percent of all banks, employ nearly 700,000 Americans and are the only physical banking presence in one in three U.S. counties. Holding nearly $5.9 trillion in assets, over $4.9 trillion in deposits, and more than $3.5 trillion in loans to consumers, small businesses and the agricultural community, community banks channel local deposits into the Main Streets and neighborhoods they serve, spurring job creation, fostering innovation and fueling their customers' dreams in communities throughout America. For more information, visit ICBA's website at www.icba.org.

banks from ready, certain, and immediate access to advances from the Federal Home Loan Banks (FHLBs).

Unprecedented government stimulus activity during and in response to the pandemic resulted in community banks investing in low-risk U.S. Treasuries – a move that is rarely criticized as unsafe or unsound. Yet, as a result of the FHFA and the PFR maintaining inconsistent rules for community banks' tangible capital, unrealized losses in these reliably stable portfolios are now unnecessarily undermining community banks' access to liquidity. Without your immediate and proactive intervention and collaboration with FHFA in resolving this issue, community banks may soon be forced to realize what are now only unrealized losses – an unfortunate outcome that during unprecedented times could ignite itself to create a crisis and needlessly undermine access to liquidity amid a period of economic volatility and uncertainty. The PFR have the authority and the opportunity to take swift action now to avoid an outcome where on-paper losses and inconsistent agency rules cause and exacerbate an economic crisis.

The FHLBs – per FHFA regulations – determine creditworthiness for advances based on a calculation of tangible capital levels that is inconsistent with the updated accounting approaches adopted by the PFR. As it stands, the calculation of tangible capital reflects any unrealized gains or losses on Available For Sale (AFS) securities. As seen in recent months, rapid market shifts weaken the value of these securities, and this ultimately paints a misleading picture of capital levels by overemphasizing temporary unrealized losses. The PFR's capital rules, on the other hand, permit the exclusion of these losses when determining capital levels. This mismatch often results in a very different capital determination depending on which capital regime is used. In other words, a bank may be considered adequately capitalized by its primary regulator while having a negative tangible capital position according to mismatched FHFA regulations.

There are multiple approaches to resolve this regulatory inconsistency. The PFR may provide written authorization to a bank's FHLB, allowing the advances to continue. As you know, allowing for additional advances does not give rise to additional risk for the FHLBs, as their advances are fully collateralized and protected against any losses. It also does not prevent the PFR's ability to resolve a troubled or failing institution if necessary. Moreover, in the Basel III final rule, the PFR correctly predicted these present challenges around tangible capital levels, noting that including unrealized gains or losses as part of tangible capital levels would introduce substantial volatility on AFS securities and create additional challenges for smaller institutions in particular.[2] Cutting them off from FHLB funding is not an acceptable solution for these

[2] https://www.govinfo.gov/content/pkg/FR-2013-10-11/pdf/2013-21653.pdf, p. 62027

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institutions. Alternatively, FHFA may modify their existing regulations to align with the PFR through a new rulemaking or interim final rule. While both are viable options, ICBA is concerned neither will be considered or enacted absent a mutual recognition of the gravity of the situation coupled with ongoing collaboration between the PFR, FHFA, and all stakeholders.

It is crucial that FHFA and the PFR work collectively to prevent delays or denials in advance funding, which is so critical to members, particularly smaller community banks. Proper regulatory action now can prevent a needless negative outcome going forward. ICBA understands that safety and soundness is of paramount importance, but we suggest that neither has to be compromised in a collaborative effort to ensure prudentially sound banks continue to have access to FHLB advances that allow them to support their communities.

Sincerely,

/s/

Rebeca Romero Rainey
President & CEO

cc: Joshua Stallings, Federal Housing Finance Agency

Doreen Eberley, Federal Deposit Insurance Corporation

Rae-Ann Miller, Federal Deposit Insurance Corporation

Bobby Bean, Federal Deposit Insurance Corporation

Ryan Billingsley, Federal Deposit Insurance Corporation