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FORUM ON THE FUTURE OF THE FEDERAL HOME LOAN BANK SYSTEM

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Harrison Fregeau: Take a seat, it's 9:20, we're going to get started here. All right. And then for everybody online and in-person, hello, my name is Harrison Fregeau, I am the executive editor for Boston University's Review of Banking and Financial Law, and I'm going to serve as the master of ceremonies for today's event. Thank you all for joining both in-person and online. We've got a great lineup of speakers here today, and it kicks off with my friend and colleague, the editor in chief of BU's Review of Banking and Financial Law, Megan Miller. Megan, come on up.

Megan Miller: Great. Thank you, Harrison. And good morning, everyone. My name is Megan Miller, and on behalf of the Brookings Institution, Boston University School of Law, and our law school's Review of Banking and Financial Law, it is my privilege and pleasure to welcome you to this symposium on the purpose and direction of the Federal Home Loan Banking system. We are so excited you're here, and we hope you will find this to be a valuable and insightful experience.

Before we jump in, though, there are so many people we need to thank for making this event possible. First, thank you to the Brookings Institution for your collaboration with BU Law and our journal RBFL in making this event happen. And thank you for the beautiful space here today. I'd like to thank Aaron Klein of the Brookings Institution for his valuable leadership and thoughtful guidance throughout the event planning process. And I'd also like to thank Megan Waring for her impeccable administrative coordination and attention to detail and for texting me the address of the event this morning.

Thank you so much to Boston University School of Law, especially the panel of professors that selected our journal, the Review of Banking and Financial Law, by selecting us as winners of the Law School Symposium competition and supporting our collaboration with Brookings. Thank you to Professor Corn Hurley, who recommended this idea for a symposium topic, coordinated outreach with Brookings, and offered such helpful and consistent guidance throughout the entire process. And a big thank you to Harrison, our Journal's executive editor for symposia for taking this project on. Harrison wrote a beautifully comprehensive and detailed proposal for this symposium that ultimately won us the competition. He was incredibly involved and dedicated to the symposium, all while balancing full time law school obligations, and all on a volunteer basis. So really incredible.

And thank you to all donors and staff of the Review of Banking and Financial Law. Many of our journal's operations beyond the symposium are done by full time law students on a volunteer basis, and endeavors like this symposium would not be possible without the support of our 3L management staff and especially our 2L staff editors, many of whom are tuned in on Zoom right now. So hello and thank you. They do so much of our heavy lifting and editing for our journal. And to all of you here in person and on Zoom, thank you for spending your Friday morning with us, we really appreciate it.

And then finally, thank you to all of our panelists and moderators. We're really excited to hear your expertise and insights into this complex body of regulation. Thank you especially to Director Sandra Thompson of the Federal Housing Finance Agency, the overseer of the FHLBs, for agreeing to be our keynote speaker and for offering your expertise on the subject. So Director Thompson has recently announced a 100-year review of the FHLB system. She and her administration have organized listening sessions and roundtable discussions aimed at determining the best path forward for the FHLBs. This symposium topic was inspired by this systematic review, and we hope it will be helpful for the FHFA, and ultimately for the unhoused and under-housed in the United States.

The FHLBs were established at a time when most mortgages lasted 1 to 5 years and homeowners made a 40 to 60% down payment on their property. After the Great Depression, these banks served as much needed lenders for the purpose of financing, housing and community development. However, the United States housing and finance markets have changed dramatically over the past century, as have the activities of the FHLBs. Housing affordability is at an all-time low in the United States. Meanwhile, the FHLBs assets have grown to nearly $1 trillion, while their membership has remained largely unchanged.

Many focusing their attention on the future of the FHLBs are concerned about the FHLBs acting as a lender of last resort. Some argue that being a government sponsored enterprise that also backs risky home loans remains vulnerable to systemic risk in the financial system. Others are concerned about the FHLBs inter-agency relations, including with the Fed and the FDIC. Some have highlighted the vast powers of the FHLBs on other agencies and private entities, including the super lien, which gives the FHLBs priority in the bankruptcy code and on collateral claims for member institutions. This might ultimately complicate any future conservatorship relationship. We look forward to discussing all of these topics and more, keeping in mind that we're all here for the same reason, which is that we believe in making the system better. And once again, welcome. Thank you very much for being here today, and I'll welcome Harrison back to introduce our first panel. Thank you.

Harrison Fregeau: Thank you so much, Megan, for that wonderful introduction. Without further ado, I'm going to turn this over to our first panel I'm going to introduce here. We're going to have this start off with the mission and purpose of the Federal Home Loan Bank system. To join us, our panelists will be Lisa Rice, the president and chief executive officer of the National Fair Housing Alliance, Luis Cortes, the founder and chief executive officer of Esperanza, Julieann Thurlow, the chair elect of the board of the American Bankers Association, and George Collins, former chief risk officer at the Federal Home Loan Bank of Boston. Here to moderate this particular panel is Telis Demos, a columnist for Heard on the Street of the Wall Street Journal. Telis, the floor is yours, everybody, please feel free to come on up. Thank you.

Telis Demos: Good morning, everybody. I'm Telis Demos from the Wall Street Journal and let's, let's just, let's let's get right into it. And maybe before, you know, before the first time you speak, maybe a brief introduction of yourself and a little bit of your perspective, you know, what informs your perspective. But let's just get, get into the discussion. So why don't we start out, Reverend Cortes, you know, as a, as a as a board member of a Federal Home Loan Bank, why don't you help us or tell us how you would define the mission and purpose of the Federal Home Loan Banks and how, how you see it from, from, from where you sit and how you would define that?

Luis Cortes: Okay. Hi, everybody. I'm Luis Cortes. I run a nonprofit organization in Philadelphia called Esperanza, we do housing, economic development and education. I served 20 years on the board of the Federal Home Loan Bank of Pittsburgh, ending my, my term this past December. And how do we, well, the answer is twofold. I have a perspective of what it is, and my fellow board members had their perspective of what it is. So my fellow board members perspective is that it is a cooperative; they own it. It is owned and operated by the cooperative for the cooperative. It makes money for the cooperative. The role of government is not recognized. It's not under, I believe that for many members, it's not even understood. My perspective is that it is a GSE, and as such, it has some government impetus that makes possible the entire business, the entire business system. So from my perspective, the 10% affordable housing piece, which is what I'm arguing for, should be higher, the 10% is less than what a capital gains tax would be in our country.

So we have a system that is sponsored by the government that makes billions of dollars and redistributes those dollars to its members and the government gets a pittance of it, 10%, which, by the way, my fellow board members call the tax. And it might be a tax. But the question is, if you're making billions off of government impetus, what should be the tax? 10%? Or is it a 50/50 partnership? So, so to me, that's how I would answer the question. It depends where you sit and how you want to define membership. And I think it's up to the FHFA to begin to define the the mission of the agency.

We were created when there were Hoovervilles all over this country, and we were created because banks needed an impetus, a push to create housing, affordable housing. We're in the same situation today with a great need for affordable housing for 30 to 80% AMI. Yet the Federal Home Loan Bank system has not yet found a way, though I am convinced they can if they want to. They have not found a way to address that need.

Telis Demos: Lisa Rice. How would you sort of describe the extent to which the the home loan banks live up to their, what do you see as their obligations with regards to homeownership, to, to accessibility, affordability, equitability? You know, how would you, how how would you describe the mission and to what extent do you think they are living up to that, that stated mission?

Lisa Rice: Thanks, Telis. That's a great question. Hi, everybody, my name is Lisa Rice. The National Fair Housing Alliance is the nation's only national civil rights trade association dedicated to eliminating all forms of housing discrimination. So we enforce the bevy of the nation's fair housing and fair lending laws. And I want to pick up on a thread that Pastor Cortes laid down. When the Federal Home Loan Bank was created in the 1930s, we had a very different financial construct. We had a very different way, right, of disseminating our issuing credit to consumers to allow them to gain access to homeownership. I mean, in those days, where you bought a home was primarily through getting balloon interest loans, right. So you get a balloon note at the end of that balloon, your full principal is due.

The Federal Home Loan Bank systems, along with Fannie Mae's precursor and the other sort of bevy of federal and agencies that were created under those suite of New Deal programs completely altered the way that we provide mortgage credit to Americans. And it a law, allowed for this sort of innovation of the long-term fixed rate mortgage, fully amortizing mortgage vehicle, right, that is so incredibly popular and very unique across the world, across the globe. The problem is that product wasn't made universally available to people based on their eligibility. It was a product that was primarily made available to white Americans, but not people of color, like Black people and Latinos and Native Americans, etc.

And the reason it wasn't made universally available to everybody in our society was because these agencies, when they were first established, they actually had race-based laws, race-based rules and policies, right. And we've heard a lot about those race-based policies that created, it not created redlining, but institutionalized redlining, and institutionalized right, systematize the association between race and risk in our financial markets that is still with us today. Residential segregation, appraisal bias, the dual credit market, right. All of these are outbursts of these very biased policies and, and, and prescriptions that the Federal Home Loan Bank system and the Federal Housing Administration Agency and others put in place, right.

And the Federal Home Loan Banks have not done what they should be doing to rectify, to remedy those harms, those damages excuse me, that they cause, as I said, those systems are still with us today. And the Federal Home Loan Banks really should be about the business of rectifying, of remedying these systems that are still causing disparities. The Federal Home Loan Banks, because they are a GSE, I agree with Reverend Cortes, they are a government sponsored enterprise. And that means that they have an affirmative obligation to further fair housing. They have to abide by the Fair Housing Act. So one of the things we'd like to see, in addition to elevating the amount of their profits that they invest in affordable housing, we'd like to see them fulfill that affirmatively furthering fair housing mandate and, and explore all of their systems, their processes, their programs, their products to make sure that they are expanding credit for underserved groups.

Telis Demos: Thanks, Lisa. Maybe let's, maybe, George, maybe you could speak to you know, underlying a lot of this discussion is obviously this, this notion of, of the FHLBs being GSEs and having public obligations as a result of that. How would you, is that a fair way to characterize the nature of their government support? And, and how would you sort of define what that is, what that looks like, some of the benefits that they receive from it and then the extent to which it's, it's fair for, for for the public to, to sort of expect as part of their mission for that to be given back in some way, shape or form.

George Collins: Thanks. George Collins. I was chief risk officer at the Home Loan Bank in Boston for 20 years and worked closely with Corn Hurley for 12 of those 20 years. And one thing that I think is worth noting is that having worked at the Home Loan Bank for 20 years, the general intention of the banks is good. We try to do the right thing. There are tradeoffs, and sometimes you go in a direction that you might not want to go in, but generally speaking, management and the board, the members, I think all were pushing in the same direction towards a good outcome, and that's something that I was quite proud of having worked for an organization like that.

I do think that some of the trade-offs that have been made over the course of the past 20, 30, 50, 90 years have been against some of the things that you just raised as it relates to the GSE purpose and how can they focus their efforts on a go forward basis that substantiate and build that relationship between what they can do as it relates to helping community banks, helping affordable housing initiatives, and maybe a little bit less towards growing and getting bigger and making more money.

And I think that if you split it apart, you can see that a good part of the value of the home loan bank system is derived from its government affiliation. And there's been papers about that over the course of the past several years at least saying that what is the value of the government subsidy. And you see numbers of 5 to $6 billion, which I think is sounds about reasonable to me. I don't think there's that much money to be distributed freely to the members in order to, to make the system work. But I do think that there, there are, there is income within the system that can be redeployed more consistent with its mission and more consistent with its role as a GSE. And I think that that number is significant.

Telis Demos: Julieann, maybe you could talk a little bit about the business of the, of the, of the Federal Home Loan Banks when it comes to liquidity provision and supporting its member banks, and how you see that as. First of all just just how significant and important is that role that they play in our banking system today and to what extent does does that activity support some of the mission-based things that that that other folks are raising?

Julieann Thurlow: Sure. So I'm Julieann Thurlow. I'm president of Reading Cooperative Bank in Reading, Massachusetts, we’re a mutual bank, we're a cooperative. So I have a very, I'm familiar with the governance of a cooperative, much like the Federal Home Loan Bank system. Community banks rely on the Federal Home Loan Bank system. And when it is foundational as far as a liquidity source, when it was actually founded, banks, I love your conversation about what a mortgage looked like.

If you actually told consumers what the Federal Home Loan Banks responsibility is to them, they probably wouldn't be interested if you called it a Federal Home Loan Bank, but if you told them that the 30-year fixed rate mortgage was going away, that would matter a whole lot to them. And the reason why a bank can hold a 30-year mortgage on its balance sheet when your consumer deposits all of your checking accounts are actually funding that. And you can take that checking account balance and leave at any time you want and go to the bank down the street and the Federal Home Loan Bank system and the borrowing capacity, the ability to have access to liquidity.

Yes, during the pandemic, we were flooded with cash, with PPP balances and other stimulus that was provided, and it shored up our balances. We paid down our Federal Home Loan Bank borrowings. But then just about overnight, inflation has drained consumers accounts and we've now needed to go back to the borrowing window. And the first place we go is the Federal Home Loan Bank system. And the reason why we can go there immediately is because we have pledged collateral and have that relationship that's been built up. So the flexibility and the access to credit for consumers at any time when they want to go to a bank is because of the liquidity sources provided by the Federal Home Loan Banking system. And that really was foundational.

What has evolved over the years is really the housing focus. And it's not just homebuyer, it's actually affordable housing, just access, we do have an affordable housing crisis here and in our country, especially in our cities and especially in our immigrant cities. And something can be done. And I think there are a bunch of people in the room here today and at this table that have some ideas about that. And I think we really can get to come together and advocate about how we can actually make things work better. But I do want to make sure that, you know, that the, the needs of community banks and the access to that, that credit when needed, how it actually smooths out the system ends up adjusting for stresses that actually happen, when you actually look at what's, what happened in 2007.

I think there have been comments about the fact that the banks aren't writing mortgages today because technology has taken the mortgage origination process outside the bank. There still are a, there are a patchwork of community banks across this nation that their balance sheet, 60, 70, 80% of their balance sheet are residential mortgages for consumers that actually buy homes in their communities. And they are, the consumer is better off when their loan is actually serviced locally, and they can walk through the front door of a community institution. Not sure if that covered what you were looking for, but I could talk for a long time about the purpose and the use and the utility of the Federal Home Loan Bank system.

Telis Demos: And I'm interested in, the extent to which, you know, the, the two missions that we're talking about here or the two, you know, purposes of the, of the Federal Home Loan Banks as as as a key part of the of the banking system and providing that that service to large and small banks. And it's, it's, it's, it's statutory and other you know perceived obligations in housing, you know, to what extent can those two things work in tandem. And so maybe, maybe, Lisa, you know, could you talk a little bit about how the Federal Home Loan Banks' relationship with its members can can, through through that that that it can maybe achieve you know, this this the the the housing mission as well as continue to serve its member banks and sort of be effective in that way.

Lisa Rice: Sure, happy to speak to that. Please excuse me, I'm dealing with allergy issues this morning. Yeah, you know, that's a very important question, I think, Telis. I used to serve on the advisory board for State Farm Bank before State Farm decided to end the company. I, and there, you know, it was really amazing to me the relationship that State Farm Bank had with its Federal Home Loan Bank member that, that it was a member of. And it really valued that relationship in part because of the, I guess I would say customizability, right, of what the Federal Home Loan Bank was able to do in order to support this institution that wanted to provide access to credit and really had taken its affordable housing mission very seriously.

So if you were to ask State Farm Bank, who would you rather go and borrow funds from? They'd say, well, I mean, they had their own funds, right, as an insurance company. But then the next one on the list was their Federal Home Loan Bank. Right. So there is some utility there, obviously, but they're, I think that the Federal Home Loan Banks can do more to provide supports, information, training, procedures to their member institutions to help them deliver more on their, what should be their affordable housing goals and their fair housing goals.

So putting together training programs around how you devise specialized programs like special purpose credit programs, special purpose credit programs are allowable under the Equal Credit Opportunity Act. They are a very unique way to circumvent what is a very unfair system right now, you heard me talk about that previously. The special purpose credit programs allow financial institutions to use a tailored way to reach underserved markets. But they're highly complex. They're a very difficult instrument to put together. And one thing that the Federal Home Loan Banks can do—because they have, you know, a bevy of attorneys and policy analysts and things of that nature—they can really put together a special purpose credit program product that they can then make available to their member institutions, thereby expanding access to credit for a group who really, really needs it.

Small dollar mortgage loans is another area that many of us, right, have a lot of angst about because consumers who are purchasing a home under $150,000 find it very, very difficult in many areas to access credit. One of our members called us— not one, several— because they had gone to bank, they had, consumers had gone to banks to try to get a small dollar mortgage loan. And the bank actually told them, well, at that price point, you can just put it on your credit card. Right? So there's this whole area of lending where we're missing, right, the ability to serve people, hardworking people who need access to credit so that they can gain homeownership opportunities.

Telis Demos: Julieann, maybe you could, look like you want to chime in there. Like, you know, are there, how can banks do a better job of helping close some of those credit gaps? And can they, can can the the Federal Home Loan Banks help them facilitate that?

Julieann Thurlow: So I actually like what you said about training banks to look at opportunities. And I think the Boston Federal Home Loan Bank was creative in creating the Jobs for New England program, and more can be done. So we recognize there are financial gaps, and I like the idea of bringing in training and thinking about how we can be more creative about utilizing the Federal Home Loan Bank funding.

There's, on an annual basis, we provide surveys for the activities that every single bank that borrows from the Federal Home Loan Bank reports on the activities around community development, around first-time homebuyer programs, expanding and recognizing that there are other ways that you can actually help the community and, and thinking about what other things we could be doing and what other programs. The regional nature of the Federal Home Loan Banks means they are a little more focused on what the challenges are in that market area.

So being very thoughtful about creating programs that work in their district and encouraging bankers to identify problems in the field that could be solved through a partnership with the Federal Home Loan Bank. There are, advances are less expensive when they're actually used for community development purposes. So again, encouraging banks and making that connection so that we can actually be, have a home run together would be wonderful.

Telis Demos: Reverend Cortes, go ahead and jump in.

Luis Cortes: So I want to read what the Federal Home Loan Banks say they are, because I think it's important to start from where the system believes it is. They do a combined financial report, and in 2021, the combined financial report says the following, the Federal Home Loan Banks public purpose is enhancing the value of membership for member institutions, which includes the value of the cost differential between a Federal Home Loan Banks' advances and other potential sources of funds— this is not me speaking, this is the system explaining who they are— as well as the potential for dividends.

When you read that and then you look at in 2019, the Federal Home Loan Bank system put out $2.1 billion worth of dividends and gave $362 million for affordable housing. In 2020, $1.6 billion in dividends and $315 million for affordable housing. In '21 $1 billion in dividends— that was a bad year— and $200 million for affordable housing, actually was $201 for affordable housing. The FHFA has the space to explore how to change this.

So I, I really feel the FHFA's role is to, first of all, define what is the mission of the bank. It started out as liquidity and affordable housing. Today, affordable housing doesn't show anywhere in the documents that the F, that the system puts out other than the 10%, some members call it a tax, some of my board members call it a tax and others say it's the 10% we have to give. Some banks do a little more, but it's less than one additional percent bank-wide, right. And system wide. So I think there's, there's things that need to happen.

The other side, to that also is the FHFA— I'm trying to figure out how to say this quickly— when you're a bank, the incentives for the, for the bosses who make good salaries, their incentives do not include affordable housing. They just don't. If a board members, if the board members don't see affordable housing as part of the mission, it doesn't translate into incentives for the CEO and for management. Therefore, there'll be no new programs, especially if you try to create a new program and you have the, and the FHFA has the capability to create a finding against you because something went wrong with the new program. So as Chair of Affordable Housing, I went through that where we tried something different and Mr. Calabria's team came and said, you should not have done that.

So what's what's the, what's the learning to management? Don't do it. If you're going to get a finding on something that's special and different, you are not going to ever do it again. So it's, it has to be, come from two places. The system needs to be forced to recognize its affordable housing and the reg, and the regulator can do that. But the regulator also has to create the space for the system to respond.

Telis Demos: George, maybe you can talk about from, from, from a risk officer's point of view. You know, how much of the, the, the the the profit that, that the system generates every year, what, is there room for more of that to be put towards some of these goals we've talked about, some of these affordable housing initiatives, while still kind of protecting the, the banks from, from risk. You know because there's you know, so much of this debate is, is well, they, they get taxpayer support, but we don't want to ever have to bail them out. So, you know, can, is there space for, for the banks to to to for the, for the system to spend more money on some of these initiatives, spend some of that profit while still retaining sufficient earnings to protect itself, I guess, like what is the flexibility there?

George Collins: So I think there's two answers to that question. The first is, is that I believe that the banks are operating in a way that's pretty risk-averse. So there's not a whole lot of risk being taken. And therefore, what dividend, should the dividend, should the capital owners or capital contributors earn on that capital? And it should be, I think, relatively low because the amount of risk is, is low. So put those two hand in hand. And I would say that the dividend in my mind has gotten a little bit lofty based on some of the comments that we've heard just this morning. So, so that would be the first component of the question.

And then the second one is the retained earnings. And what do we, what should the banks want to do with the retained earnings, if you have too much retained earnings or about even if you want to manage the the organizations quite conservatively and say, okay, the capital level is about right, but certainly going forward, the banks do not need to add to their retained earnings base. I think it's almost getting to the point where they tripping over too much capital.

So why would you not therefore allocate some of that money that had previously been dedicated towards building retained earnings and push it off towards this more mission related activities that everyone on the panel here seems to agree with universally, that more can be done as it relates to low income housing and even community bank support, which I think is a key component of making the system work towards its, its mission. So but I think there's quite a bit of money there to reallocate given where the banks now stand.

Lisa Rice: And tell us, can, I feel compelled to chime in here, because I really want to press the point that fairness in the system is safety and soundness. When financial institutions do not fulfill their fair housing and lending obligations, they're more likely to be in danger of not being safe and sound. We saw that with Washington Mutual, we saw that with IndyMac, where Washington Mutual was engaging in unfair predatory practices that put the system in jeopardy, did put the system in jeopardy, right. So want to make sure that there's no sunlight between— and we've heard Governor Barr talk about this here recently— that fair housing, fair lending, fairness is safety and soundness. Those two things are inextricably linked.

Telis Demos: Maybe, you know, on that topic of who are the members of of of the the Federal Home Loan Bank system. Julieann, do you think that that that the that it's the, you know, who is in the system who is who it is benefiting who who is participating in it is is currently, you know, fulfilling those, those two missions. Obviously, there was, you know, some controversy in the news recently about, you know, a bank that was in the sort of the, that supported, you know, cryptocurrency companies using FHLB advances which, you know, caused some discussion about, well, is is this a bank that that should have access to that system.

So maybe you can sort of give, give some perspective on, on you know whether, whether we need to, it would be appropriate to, to expand, narrow, redefine the the the membership to to as as as Lisa was saying, you know to to ensure that we're supporting the kind of institutions that that that have those two things aligned.

Lisa Rice: I'm sure I think I'll, I'll take that in two steps. So first of all, as far as membership, 97% of the membership of the Federal Home Loan Bank system are banks under a billion. I have heard it or read at some point the conversation around who were the biggest borrowers. But if you actually look at from a pro-rated standpoint which banks are borrowing and how much of their balance sheet or their liabilities are sourced from the Federal Home Loan Bank, you will find that banks under a billion are also the financial institutions that are most utilizing and most relying on the Federal Home Loan Bank system for their liquidity. We don't have access to capital markets, particularly if we were a mutual and a cooperative that does not have shareholders. So the smaller the bank, the higher the, the demand for or need for the Federal Home Loan Banking system.

As far as your reference to Silvergate, and that kind of brings in the whole super lean concept and the risk to the system. When you borrow from the Federal Home Loan Bank, you borrow based on the assets on your balance sheet, and that is the pledge. And I do know there is some consternation about the super lien, but it actually does work so that taxpayers are not on the hook.

Early, early in my career, during the banking crisis in Massachusetts and in New England, I actually worked for the FDIC. And the FDIC, I'm sure is not happy to pay the Federal Home Loan Bank system for their their loans so that they have access to the full collateral. But the FDIC does have the division of liquidation and the Federal Home Loan Bank system doesn't.

So an orderly liquidation of banks assets, if they cannot sell the institution to another institution much like this, yeah, let's not postulate. But as far as that liquidation process comes to a loss and if there is a loss to the FDIC fund, it actually then turns to banks and increases the premiums that are charged for that insurance. The FDIC, although it's a regulator, is also an insurance fund, and the banks are the ones that actually pay in for the premiums for that insurance coverage. So it is a cycle and it is, it does work so that the, the Federal Home Loan Bank system doesn't sustain a loss and neither does the FDIC because the banking system itself will sustain and will repay that. So that takes care of the liquidity side of the equation.

I, you know, again, I wholeheartedly agree we do have affordable housing crisis and there are ways that programs can be developed that are very specific to communities, communities of color that actually do not have access to credit. And I think it would be really great for the institutions that are members of the Federal Home Loan Bank system to come together and think about how we can be very intentional about the type of programs we talk about appraisals not actually, you know, appraisal bias in, in low-income communities and in communities of color. There are always gaps to financing. So there are opportunities for us to be creative about creating programs that actually can help depending on where the community is.

The other challenge that I also see is the fact that the definition of low income for which funds can be sourced is much too low. When you actually in, let's see, cities in Massachusetts, I believe one in four household, households pay more than 50% of their income for rent. There is a problem; that family is never going to be able to save enough to buy a home. So how do you actually make adjustments for that or think creatively about how we can actually address the real challenges that are happening on the ground?

Luis Cortes: One of the things that has concerned me over the decades now is always the statement, you know, we could look at filling gaps or we can do this or that, and then very little actually happens. So from my perspective, the only way that the system will actually change is if if it's directed and and the system has significant resources and can even create more significant resources for affordable housing without creating hazard or risk, right. Because that's, those are key issues.

So if you look at in the third quarter figures for 2022, the investment income from restricted retained earnings, they are $6 billion in a bank in the system, it's not the bank, it's in the system, $6 billion. Those $6 billion are excess retained earnings that came from the REFCORP in 2011 when the system, when we finished paying off REFCORP, a decision and a conversation had to be had about what was going to happen with the REFCORP revenues. And when we had that conversation, one of the fears was that there'd be a government taking of the 20%. It was, and it was a good, there's a historical precedent for that fear. So it wasn't abnormal for a board to have that conversation. I was part of that board.

When we have the conversation, one way to keep the funds was to stick it under safety and soundness, right. Because who's going to take away funds that are for safety and soundness? And the truth of the matter is, we needed it for safety and soundness because some of the banks were undercapitalized at the time. So it made sense to do in 2011. Fast forward to 2022, there's $6 billion in excess retained earnings. This year, that $6 billion is going to create $375 million of risk-free income. That is more than the amount of dollars that are coming from the 10% AHP. If you were to take that $6 billion and make it a guarantee fund, you are now going to create over $1,000,000,000 of subsidy for affordable housing.

Now, this is a simple layup. It hasn't been done— layup is a basketball term, but yeah, because they've got to be careful, I'm talking to bankers— so, so, so to, so to me, the AHP fund program could provides credit support to achieve the greatest positive impact. If you leverage the $365 or $75 million, if you leverage it, you're going to have over $1,000,000,000 a year created, over $1,000,000,000 a year created, and a fund that continues to grow without taking risk, additional risk to the system. And that ultimately is the goal. How do we create significant change for significant need, not how do we have another study that says, oh, we need more money for housing? We know that already.

Julieann Thurlow: Okay. So I, I think it does bear mentioning that the capital stock of the Federal Home Loan Bank system is actually owned by its members. And so the retained earnings actually does belong to the Class B stockholders of the Federal Home Loan Bank system. And so I don't think anybody would be advocating for taking encouraging programs and allowing and, and through regulation, because it is not the regulator's decision, it actually is Congress's decision when you talk about things at that level or changing the mission and purpose.

But programmatically, I think you can actually achieve the same result by encouraging programs, much like you're referring to a guarantee program that actually funds particular activities within communities that actually need that type of investment, that encourages banking institutions. And that is the whole purpose and mission was to encourage banks to lend so that you didn't have bumps in the system. Clearly, there are bumps in some communities and using the system and constructing a program that would actually meet that purpose without an actual taking does change the story.

Lisa Rice: So, Julieann, I would say that there are major barriers in some communities, right? Not just bumps like huge roadblocks. And the Federal Home Loan Bank can do a lot to knock down those roadblocks, through things like special purpose credit programs. We wrote a paper, the National Fair Housing Alliance and the Center for Responsible Lending, wrote a paper for the GSEs to establish a first-generation homebuyer program that would greatly expand housing opportunities for underserved markets. So we have to do big thing, we can't do incremental things if we are going to crack this nut. We have to do big, bold things in order to really make a difference. And the Federal Home Loan Bank system has the wherewithal and they have the assets to do big, bold things.

Telis Demos: And George, maybe, you know, within, you were talking about the conservatism of the way that, that, that the banks are run, you know. Are there ways that that the bank can can essentially take more, that the banks in the system can take more risk by changing some of the, the ways that they lend to, to members? And I think maybe by expanding the type of collateral or giving special treatment to collateral, that is, you know, that, that achieves some, some, you know, some other part of the mission. Are there things that that, you know, aside from, from taking the profits of the system as it is and putting it to work, are there things that, that the FHLBs could do differently about that core business that could achieve some of these things and maybe, you know, essentially use use some of their risk capacity in that in that way?

George Collins: I think that exists, but it needs to be resolved in conjunction with the regulators that for the banks to do it, as was mentioned earlier this morning, to take action by management that raises the wrath of the regulator is something that we're discouraged from doing. We just we, we've always stayed away from that as a management group. So I think that that needs and that doesn't mean there aren't opportunities, one of the ways that you create that opportunity in my mind is to prefund the risks that you're taking.

So rather than taking the risk and saying, well, we'll make it up on earnings going forward, to set aside some of the money that has been accumulated over the course of time. So I think that and that's what we've talked about up here, is that I believe that that money exists within the balance sheets of the home loan banks in order to pre-fund some of the risk. And therefore, when you speak with the FHFA about incremental risk, it's not, it's less concerning if it's prepaid for. So everything's already set aside. So I think that that's an important consideration, but it's, it's probably not a big, a big issue.

One thing that I would like to raise as the discussion that just took place, talking about who can force the issue as it relates to who our, how our, is the capital and the earnings going to be reallocated. And I really think that it's in the best interest of the members to jump forward here. It's not the regulator, it's not the management, it's the members, because the members get a lot of benefit from the home loan bank system. And so preserving that on a go forward basis is something that I would like to think that the members would take the lead on.

Julieann Thurlow: I like how you put it. The members actually collectively coming together and identifying what the challenges are in their communities, the fact that you have regional banks, whether you are in a farming community or whether you're in downtown Boston, very different financial needs as far as those communities are concerned, recognizing where credit is not flowing and creating programs that actually can incent banks and actually use what you're referring to as retained earnings or excess capital as a mechanism to allow programs to be created.

Luis Cortes: Well, one of the things that I keep looking at is we talk about member stock and members put about 5% of the cost of that stock out of their pockets. The other 95% or so is borrowed from the very system. So when you're doing that, who are they, who's actually financing the stock? We are, the taxpayer. And then on that stock, they make X-amount of dollars, and then on that they create their dividend. And then on that they return 10% of the profit. So the real issue is do we allow banks to borrow 95% of their stock? That's a simple question. And I would say, sure, are you going to return on 90, what's our return on 95% of the stock? But we don't get that return. We don't get any return other than 10%, which I will remind everyone is less than the 15% we would get on a capital gains. These are capital gains systems.

So we are getting gamed by the membership. We are in fact being used. The liquidity is important, member banks need it. If the GSC did not exist, they would have to pay a lot more for it and the big banks would, they wouldn't necessarily care. So we should look at this as, if, as a business proposition, we are providing liquidity, we are providing financing, we as government, which is us, the citizens. And in return, we're looking for a better return for the community in the area of affordable housing.

Telis Demos: Lisa, what, we're coming up on our time here, but I wanted to to to let you have the opportunity to weigh in on this conversation we've just been having here and I guess arguably have the last word for now. Do you think that members can step up and, and sort of take on these responsibilities, or do you think that, that there needs to be some change in, you know, the members stated and or obligations, you know, as members of the system or are there changes that need to be imposed regulatorily or statutorily. You know do you think that that that there's something that it can't be done sort of from, from just within the system as it as it is today. But but that something needs to to to push members in a new direction.

Lisa Rice: Yeah. Thanks, Telis, for the question. So I think they, they can, members can do that and they are obligated, they are currently obligated to do so because they have to as a, the Federal Home Loan Bank as a GSE is obligated, it is mandated to affirmatively further fair housing. Now the problem that we have is that the Federal Housing Finance Agency hasn't done all that it can and should do to enforce the Fair Housing Act obligation on the Federal Home Loan Bank system. So not only can it do it more, it has to.

And I must reiterate the statement that I said before, I'm trying to disabuse us of this notion that fair lending is risk. It's not, stop connecting those two. That's the, the comment that I was trying to make earlier. Part of what got us in this conundrum is associating, the association between race and risk. Disassociate that. Fair lending is not risky. Fair lending is safe and sound. I, and if I'm interested, I want to hear more, Pastor, about the program that you guys were told by the Federal Housing Finance Agency that you shouldn't have done, I want to hear more about that because that might have been an a violation of the Fair Housing Act for the Federal Housing Finance Agency to have told you that. But it is obligated to do it and it has to do it.

And I think we as taxpayers right, who support this system, have to push and compel the Federal Home Loan Bank system to live up to its fair housing and lending obligation. One way to do that is for Congress to require the Federal Home Loan Bank to report more about its fair lending activities in its annual reports.

Telis Demos: Well, I think, are we, I think, I think we're, we're up on time. Do we have time for any, any questions from the floor or should we. If anybody has any burning questions or something specific they'd like to address, maybe we have a minute or two for that. But notwithstanding that, I'd just like to thank everybody for, for your comments and, and participation. And I think, I think it was a, it was a pretty engaging discussion about the, what, what is happening, what should be happening, what can happen, what needs to change. So thanks, everyone, for, for being here today and and certainly look forward to, to the other panels. Thank you.

Harrison Fregeau: So thank you all for your words. For the people in person, we're going to be taking a 20-minute break and we're going to do panel two at approximately 10:35 am. And so for the people online, feel free to step away. We're going to start back up in 20 minutes at about 10:35 am Eastern time. Thank you.

Harrison Fregeau: Hello again, everybody. If we could take a seat and all gather back together, for all the people watching online, welcome back, hope you enjoyed a breakout, a little coffee and a little relaxation, whatever it might be. So at this time, I'm going to look to welcome up our second panel. The subject of this panel is going to be the Federal Home Loan Bank supervision and regulation, as opposed to mission and purpose as the first one went.

So I'd like to welcome up to the stage at this time our speakers. We've got Kate Judge, the Harvey J. Goldschmid professor of law at Columbia University School of Law. We've got Bruce Morrison, the former chair of the Federal Housing Finance Board. We've got Mark Calabria, the former director of the FHFA, and we've got Scott Frame, a Vice President at the Federal Reserve Bank of Dallas. Moderating this particular panel is John Heltman, the Washington Bureau Chief for American Banker. So, everybody, please come up. And John, the floor is yours.

John Heltman: All right, everybody, welcome to all of you in person and all of you tuning in out there, hi, Mom. So this one is about regulation and supervision of the home loan bank system. And I think probably the most logical place to start is to just kind of set the table and say, how are the home loan banks system or how are the home loan banks and the home loan bank system regulated? How do they interact with their banks primary regulators? And what are the kind of the levers that regulators can pull on the home loan banks? How about Mark, why don't you go ahead and talk to us about that? Yeah, there you go.

Mark Calabria: Okay, great. Thanks, John. So the Federal Housing Finance Agency is the primary regulator for the Federal Home Loan Banks, which, of course, followed the Federal Housing Finance Board that Bruce chaired, which of course followed the bank board before that. I used to quip internally that my objective was to make sure that the next crisis we wouldn't have to create a new regulator, change the name, to keep it consistent. So the Federal Housing Finance Agency has many of the same powers that the OCC or the FDIC or Standard Bank regulators have for the banks, capital, liquidity, mission regulation.

And in fact, you know, we were always very jealous when we were writing HERA in that the authorities over the banks are actually much more powerful than the authorities over Fannie and Freddie, which are often constrained in many instances. So tremendous amount of authority to set things like capital. Again, as we know, the single headed agency now removable at will. Again, that's the system, just like any other regulation. There is an attempt to work with the other regulators because an important thing to keep in mind is FHFA regulates the Federal Home Loan Bank system. It does not regulate the members of the Federal Home Loan Bank system.

So, you know, entities like Silvergate are not regulated by FHFA. FHFA would regulate the relationship. And its interestingly enough, of course, a reminder that the Federal Home Loan Banks themselves used to be up until I guess, the late eighties regulators themselves, which still has a bit of an overhang in the culture there. And again, the attempt is to try to make sure that they're safe and sound and fulfilling their mission.

John Heltman: Well, that actually, Bruce, that tees up a pretty good question, which is how has the regulatory structure of the home loan banks changed over time? Of course, from your time and before.

Bruce Morrison: I'll be the historian here. Mark made a good start on that. Well, when they were created in 1932— most of us were not alive then— they were really created along with their regulated entities, which are the S&Ls, which were created for the purpose of creating the long-term fixed rate mortgage, which we all take for granted. And for, from then until 1989, they were the regulator of the thrift industry, and they also were the insurer. They were like FDIC or what's called

FSLIC. They were, they performed that function, and they were the banks we know today providing funding.

Now, that's a three-way conflict of interest, which they took to the extreme of writing pieces of paper, which they called net worth certificates when certain of the institutions went, were insolvent. And of course, the federal government eventually had to write checks to cover those amounts. So that was a hopelessly improper structure, but not everything about it was improper. It was a very focused system. They, less than 10% of their balance sheets were investments. Advances were 90% of what they did. They didn't pay dividends. And because they were the regulator, of course, the, the members said aye aye, sir. And and that's how it worked.

So what happened in 1989, which is the is very that was the S&L crisis. For those of you who are keeping count, those, those functions, the insurance function and the regulatory function were moved elsewhere. The bank stayed, commercial banks were allowed to join, and the banks changed fundamentally in terms of that focus, and they became much more focused on profitability and payment of dividends. And the largest financial institutions in the country found it attractive to join. And there was a whole concerted effort of getting commercial banks to join.

So that was what was going on when I became chairman. And the big challenge of the time was can you regulate the mission of this system. And we're still talking about that, I think. And the answer is yes, but with great difficulty, because while, as Mark said, the statutes then and now permitted pretty unbridled regulatory action, this is Washington, and not every action goes without a reaction. And so there were reactions. And I had to write one of those famous letters I will not do this to keep from having a worse thing happen in an appropriation bill.

So I know about, you know, the banking industry going to Congress and saying, stop this guy before he kills again. And so, you know, there is, there is, there is a lot of potential. But, you know, there is, it is a very political environment. And you heard from a very articulate president of a community bank who is about to be president of the ABA, and that's one picture of the Federal Home Bank system, the one that Congress hears about, the part about the largest financial institutions being the largest borrowers, is one you hear less about.

Mark Calabria: You know, John, if I could add and maybe I'm a little biased, having worked on the act that created FHFA, but, you know, you talk to people there at the agency that were there at the board, and I think there is even one person there that was at the bank board is still there. You talk to the external constituencies and Congress combined the Finance Board and OFHEO the then regulator of Fannie and Freddie with the intent to essentially reduce the influence of any one entity on the agency. And let me be, from what I've heard, what I've seen, I think that very clearly worked. The ability of the banks or even the community banks to undermine the safety and soundness agenda is reduced relative to what it used to be. So there's been a success there in my mind.

John Heltman: Scott, I wanted to touch base on, so Mark, you made a good point, which is that the FHFA regulates the home loan banks, it doesn't regulate the home loan bank members. That's the primary regulator's job. Can you flesh out for us what the interaction between the home loan banks and the primary regulator is, like if a, if a bank wants to borrow from the home loan banks does, do they ask the Fed's permission? Does the does the Fed like check with the FHFA or sorry, with the home loan banks? What's that relationship like?

Scott Frame: To begin, I've kind of come at this as an economist from sort of the research side, that's looked at this rather than the supervisory side. But I have, I do have interactions with, with people that practice supervision. So the primary regulators don't have any particular say, certainly about any specific advance or anything. This is a business arrangement between the members and their home loan bank.

Now, my understanding is, especially for community bank supervision, you know, supervisors want community banks to have at least one form of access to sort of back up or government sponsored liquidity. And that can be the discount window, or it could be the home loan banks. And some have access to both. They tend, on average, more have access to the home loan bank system because it's a much more straightforward process. The borrowing is much more routine, where the discount window historically has been perceived as sort of a lender of last resort function. And, you know, the set-up costs of getting collateral arrangements in place can be a little, you know, more cumbersome, yeah.

John Heltman: Well, that brings us to the most recent episode of the aforementioned bank that helps crypto companies that shall not be named. And I guess like, my, well, I'm going to throw this to Kate is, is that episode a regulatory or supervisory failure or success or neither or is it just kind of a thing?

Kathryn Judge: Well, we still have a lot we're learning. But, but I think from what we know so far, at the very least, it's a reflection that the objective function right now of supervisors probably isn't optimal because it could very well be the case that if you're looking just at the riskiness of the Federal Home Loan Banks and the risk that they took on taking into account the collateral they demanded and the super lien that they were entitled to, that actually, from a risk management standpoint, which is like the primary function right now of a lot of the supervision, it may not have been that much of a problem.

On the other hand, you did have a bank where 90% of its depositors were crypto depositors, more than 90%. It suffered a bank run where it lost 68% of its deposits within a quarter. And so a lot of the really interesting questions there are not just like should this advance have been made, but who else was involved in the conversation. So it really goes back in some ways to your question to Scott over right now, we're in a point in time where crypto has come out of the blue to really be a transformative force in a whole variety of areas. And there's a lot of questions over what the spillover effects are, what are the the dynamics that we should be paying attention to?

And I think some of the really interesting question is, is not just like what this meant from the perspective of the risks for the banks that were involved, because there are obviously other banks, other federal banks that we now know were also lending to crypto, crypto-focused banks. But after looking at inside those banks, I mean, how much did the fact that they anticipated access to Federal Home Loan Bank advances change the types of risk that they were willing to take? So, so for me, the question is not is this a failure of supervision? But the more disturbing question is this might actually not have been a failure of supervision, which begs a much bigger question about the mission drift that really has been much of the conversation today. This is not a community bank that you're helping to support, and instead you're actually potentially, you know, supporting a bank that, that could corrupt the perception of safety and soundness of the banking system generally.

John Heltman: And that kind of brings me as I was jotting down my, my kind of plan of attack here a minute ago, it occurred to me that so in, you know, after Dodd-Frank, one of the big new words was macroprudential, right? Was, so banks or supervisors have always supervised banks for like are your, is your balance sheet right, are you know, are your investments too heavily in one thing or another? And then after the crisis, it was like, well, we need to look at not just the banks individually, but like the banking system more broadly for systemic risk. And it doesn't seem like there's much of a, apparatus for either the FHFA or the primary regulators or both or either to kind of take that view. I'm just gonna throw it out to the floor, Mark.

Mark Calabria: I mean, I would say we, we did much to the chagrin certainly of many in the mortgage industry. I tightened standards in 2020 and 2021. I think the real lesson, all due respect to my friend Scott, is when the Federal Reserve is intent on flooding the system with liquidity, almost nothing you could do as a macroprudential regulator's going to offset it. And that's the situation we are in because, again, we tightened standards throughout that time as the bubble was building. And you still had a bubble.

Bruce Morrison: Yeah, I think that we're focusing on the wrong regulatory question with respect to Silvergate. I don't know anything about the underlying transactions. I think it's kind of a primary regulator function that these people were so heavily invested in one aspect of the economy and therefore they, their risk was a particular profile. And I think there are a lot of questions for the primary regulators. This is a mission regulation question. Now, people can disagree. I have a very strong view that GSEs need mission regulation and it should be extremely severe. That is, it should be that GSEs should not exist unless they have a clear public purpose, and they perform that purpose and that it's not good enough that they're safe and sound. They have to be safe and sound, but not to the detriment of their mission.

And frankly, before the changes in HERA, there really was no mission regulation of the GS, of the housing GSEs or Fannie and Freddie. They, HUD had a responsibility, they had an office, and it was a joke, and they didn't do anything. Those things were consolidated into FHFA. The Finance Board always had both. As I said earlier, you can get in trouble by being too muscular in that regard. But in any case, that's where Silvergate raises questions. What kind of institution that has that profile in terms of their assets and their liabilities satisfies a test that is supposed to be about housing or economic development, because they weren't about that. They were market players of a certain kind, and they should never really have been able to get into the system. But they can because they just have to buy up some MBS and have certain amount of MBS on their balance sheet and they come and nobody looks again.

Mark Calabria: If I could make a follow up on this. So one of the overhang problems and Bruce gave a great part of the history, when commercial banks were let in, there was a test applied, asset-wise, you didn't have to worry about this and thrifts because you had the old qualified thrift lender test that made sure you supported a housing finance mission. The problem is the test was one and done. You could get this commercial bank test on the front end, 30 years later, completely different institution and still have your membership. And to his credit, my predecessors director Watt tried to do more annualized testing got a lot of pushback.

But I think one of the things that has to be on the table in the, and FHFA fully has the authority to do this is to have a more regularized asset test through the institutions. And the second thing I would note is, Congress has decided there is a purpose for long term advances. They have to support housing finance. The problem is Congress has been silent on short term finance advances. However, it has left it up to the regulator. Maybe Bruce can shed some light on this. When I walked in the door, the regulatory structure was anything under five years was a short-term advance and hence did not need to be tied to residential finance. I don't know how they ever came up with five years that, you know, maybe to channel the bill bond market something closer to one year or 180 days would make more sense. But the thing is, there's no statutory nexus between short term advances and purpose. And again, the thing that the regulator can do to fix this, or at least fix part of it, is simply shorten that window.

John Heltman: Well, that brings a question that was further, oh, sorry, were you going to say something, Scott?

Scott Frame: Yeah. I just want to follow up with Mark to just get a flavor of this. But going back to Bruce laid out the history very nicely. But you know, with FIRREA, it basically broke, broke the tight link between, by allowing banks is more diversified, you know, which had more diversified portfolios than thrifts, it sort of broke this link between the advance lending and the underlying collateral. And you can say, yeah, they're still pledging whole mortgages or MBS, but money is fungible. And so this can be used to finance pretty much anything. So related to that, though, I mean, it gets at this regulatory question of like, could you, even if you change that definition, are you really altering that dynamic?

Mark Calabria: You've touched upon the real problem here is that money is fungible. And even if you tie a purpose to the advances, I think that's an improvement. But your ability to really kind of enforce that at the end of the day, I mean, you know, again, let me qualify this with when I sat in the regulator seat, my perspective was Congress makes the laws, I carry them out, not my job to second guess the wisdom of the, of the legislative branch. But well, you know, again, I'm an article one guy at heart. But the real Faustian bargain here was you would have had a massive bailout of the savings and loan system. And so Congress created these REVCORP funding mechanisms. But there's no way that the thrift industry could have paid that, they would have all gone bankrupt. So the Faustian bargain was commercial banks, we will let you into this subsidy if you pay off the cost of the savings and loan crisis. And that was the original sin with this. And if they'd never done that, we'd obviously be in a different point today.

Bruce Morrison: Well, I think let's just be clear. They paid a tiny portion of the—.

Mark Calabria: Agreed, absolutely.

Bruce Morrison: The REVCORP obligation and the taxpayer could have paid the rest. I mean, these Faustian bargains are usually not so great. And of course, this is, and this is of course, this is, of course, how Freddie Mac got out from under and became a public company also, which was all about Congress papering over what had happened and the cost of it. So trying to make it appear to be less of a cost to the taxpayer we pay in the long run rather than upfront.

So I just would, would, would just focus there that there is space for doing things about collateral. The banks will want whatever collateral they can get their hands on, and that's the safety and soundness concern, and the regulator tends to think that's great. But you could have you can buy for Kate that you can let them take whatever collateral they want for for for collection purposes but tie the collateral specifically to a purpose. And I think you can get a lot farther down the road in terms of regulating what they are able to use the advances for, even though money still remains fungible.

John Heltman: This is the uncomfortable thing about being the middle panel between one about mission and one about solutions is that we're invariably going to delve into mission and solutions. So let's just do it, like, I mean, so, Mark, you brought up membership, right? And I guess we can start with a simple question followed by a more complicated question. Simple question is who can be a member of the home loan banks and complicated question, who should be a member of the home loan banks?

Mark Calabria: Well, so, so Congress has a list of basically as a laundry list of charters like commercial banks, insurance companies, thrifts, the CDFIs, that can be members. There have been attempts in the past by entities that don't qualify to essentially buy a charter of someone who does qualify to get it in. And I think we've kind of fixed that. Maybe more needs to be done on that. We've made a lot of progress. You had a lot of private equity, for instance, buying insurance companies and things like that. So that's the who, who can get in. Who should get in? And again, I'll repeat, I think the original sin here was letting the commercial banks in.

But, you know, that's long past. Unless you come up with some sort of definition of mission, I worry I know that there are conversations out there about letting non-bank mortgage lenders, and I think that would be a huge mistake. But only Congress can do that. And at the risk of perhaps making myself the most unpopular guy if I'm not already in housing financial company— that is what it is— I worry that, setting aside perhaps the quality of state level insurance regulation and the quality of federal level bank and thrift regulation, there are no prudential regulators for CDFIs, and they are a small amount of the system now, but it represents a loophole where in my concern you're going to have a lot of players unscrupulously look at this and say, well, I can't really get in via the insurance route, so I'm going to buy a CDFI and get in that way.

And you've got this where the system needs to figure out essentially how to be a prudential regulator of CDFIs. Again, I'd be the first to say that is not a real threat to the system today, but it creates an opportunity and where there is opportunity and subsidy, there will be people who try to find a way to leverage it.

John Heltman: Well, I think that question about membership also comes back to Bruce's point about mission, right? So it's like who can be a member? Like, so insurance companies, right. Why are insurance companies a member?

Mark Calabria: Because they used to be the biggest mortgage, you know, investors in America, decades ago.

John Heltman: Used to be, but they're not in general. Right. I mean.

Mark Calabria: They're still very big in the multifamily space. So, I mean, there are elements of it, but and I think there are things we could do that would encourage the insurance companies to get back into that space. But in the single family, they're not as big as they used to be.

John Heltman: And I guess that's what I'm getting at is that like if you want to get home loan bank advances to do home loan bank type stuff, maybe that kind of makes sense is.

Mark Calabria: Why you need an asset test for the balance sheet.

John Heltman: Well, tell me more about an asset test.

Mark Calabria: So I mean, it is what it sounds like. The regulator kind of goes in and again, it's similar to the qualified thrift lender test you used to have when we had thrifts and you're saying, you know, you're looking at and saying what percentage of your assets on your balance sheets, and I think we actually need to be aggressive about it and say, you know, this can't simply be that you buy agency MBS that, you know, you actually have whole mortgages on your balance sheet that, you know, you've originated, you've made, you service, you keep and that you're actually in the mortgage market.

Now, any number is going to be arbitrary. We can say 10%, 20%, 50%. That's all going to be part of the political process that comes out of it. But having an asset test where at least you've got some involvement in residential mortgages, you know, if that's what we believe the current purpose and direction of the system is, and that's implementable. I mean, again, assets change, it's a question of how frequently you do it. Everybody coming in as a commercial bank new member has to meet an asset test at the front end as I mentioned. And the question is, should that be ongoing?

John Heltman: Checking whether I'm on, oh sorry Kate, were you going to say something.

Kathryn Judge: I just want to add, it's a multi-prong way of trying to look at this, right. Because there's the question of who the members are, what is the nature of the assets they have, and then it goes back to Bruce's point in some ways about collateral. And significantly, all of this is completely apart from the conversation we're having this morning, which is what portion of the profits ought to be directed in particular ways and how should those profits be used.

Here, we're actually looking at the various activities that they're engaging in, and I think that is where a lot of the power lies. There's an important conversation to have about profits. There's a threshold conversation that we're having right now. And I would say it even goes beyond kind of just thinking about an asset test, and as part of the broader conversation we're facing right now over what is it we want as kind of a structure of a U.S. banking system, and what is the role that the Federal Home Loan Banks play in that?

And as this has been beautifully drawn out, we originally had the Federal Home Loan Banks because we said we wanted there to be thrifts and S&Ls creating particular types of credit. And so there was a tight correlation at that point in time. And probably also we didn't have access to the Fed, the one thing I'd add to the the history that has been so beautifully drawn out is until 1980, those entities didn't have access to the Fed. So as both we opened up the Federal Home Loan Bank system, but we also shifted who had access the Fed in ways that really mangle the distinction.

But there's something to be said for going back and saying those particular types of institutions that specialize in particular types of loans that we think for a variety of reasons are really helpful to the type of economy that we want to have and the type of services and financial services and products that we want to make available. And, and you can start to think about those things as co-determined questions over, do we, right now, we've had 400 mergers a year for the last 40 years, right.

So we've seen an incredible decline in the number of community banks and incredible growth in the assets of larger banks. And so part of the question is like, what role, and it affects things like housing, but it also has a huge effect on things like small businesses and so part of the question is like, what role can the Federal Home Loan Banks play if these are dynamics where we want to be more proactive in thinking about what is the credit availability and the structures to which that's happening?

John Heltman: I think one, sorry, go ahead.

Bruce Morrison: I think it's a really important point that there's a lot of discussion about how to use the profits and how much to tax the profits or to assess the profits to do good things. And that's fine as far as it goes. But the question is how do they earn that money and how much money do they earn? Because do you really need dividends in a system where people need advances? The benefit is the advances, right? You, they didn't pay dividends in the old days, and they don't have to pay dividends now. And the dividends are hugely leveraged as, as Reverend Cortes explained by borrowing the money to buy the stock. So that whole activity should be looked at as to whether or not that has to happen.

And then beyond that, you can decide, I mean, the 97% that were referenced as as community banks with billion or less assets. They're not the problem. The balance sheet is not them. The balance sheet is two other things, it's advances to very large financial institutions and investments. The only place they've ever lost money and they lost plenty. There's no need for those investments except to sustain the dividend production and the size of the system. If you had a community bank system, you could design it completely differently and you wouldn't have the financial disincentives that you currently have.

So there is room for a fundamentally different structure. Some of it has to come from Congress. Some of it could be done by the regulator. But I'd urge everyone who cares about what the Federal Home Loan Banks do to focus a little bit more on what it does, which is primary assets and less on what it does with its profits. Because if you fix what it does with its assets, then the other will, you know, be less important than what it's accomplishing with the trillion dollars.

Mark Calabria: I think Bruce makes an important point that I really just want to emphasize, you know, and the regulator could and should and we in we certainly were looking at this, the reason the system is incredibly profitable is because it's basically a big Bear Stearns Lehman. They, they they borrow short and then they invest in a whole bunch of long dated assets, ride the yield curve. And we know every 10 to 15 years that blows up your business model.

Of course, some of this goes back to the REVCORP obligations create a pressure to create profitability. And so again, they basically set up hedge funds on their balance sheets. And this is a real risk to the system. There's absolutely no rationale for the banks to have the size of balance sheets and investment portfolios they do today.

Bruce Morrison: But, Mark, we have to make clear, when I got into the chair, REVCORP was the explanation of everything. Yeah, it was $300 million a year. So we changed that to a percentage. You don't have to earn any profits if your assessment is a percentage. So Gramm-Leach-Bliley solved that problem and even Treasury supported that. So, so the point is—

Mark Calabria: I'm not blaming, you know.

Bruce Morrison: No no, what I'm saying is it's important to say that immediately the system used REVCORP was an excuse. When the excuse was withdrawn, nothing changed.

Mark Calabria: Agreed. Yeah. There's, there's no need, there's no need to ongoing again around these kind of balance sheets and try to create this kind of profitability. And it raises questions too, about are they overcharging for advances, I mean, and the need for paying these large dividends when you could be lowering the cost of your advances or not having these kind of balance sheets, which represent risks. All of that stuff needs to be, needs to be looked at.

John Heltman: This is great. It's like a self-driving panel. I don't even have to be here. I mean, keep going, guys, like.

Mark Calabria: Well, you know, I worked in the Senate, so I've got an excuse for filibustering and the House, you know, we get you, 2 minutes or something, is that.

John Heltman: I see the gentleman's time has expired. I just really had one more note that I, that I wanted to touch on. And that is the kind of the role of the home loan banks as like liquidity pool of choice in the broader banking system. And I mean, obviously the home loan banks make advances. That's not like a new feature. It's been around for a long time, but I think as, as we've discussed with the evolution of the system over time, you know, banks routinely go to the home loan banks for advances to meet their liquidity needs. And they do not routinely go to, say, the discount window to meet their liquidity needs and increasingly may not go to, say, the repo market if they can go to the home loan banks and get a better rate. Right. So is is that like is the home loan bank system adequately regulated as liquidity pool? And if and by whom ought that to be and that wasn't really a sentence. Who should be regulating that and, and how. Mark, go ahead.

Mark Calabria: So to me, part of the problem with the banks, as well as Fannie and Freddie is these were all entities that were created to be countercyclical, that they would be there in times of stress to provide a floor under the market. And unfortunately, they've all become very pro-cyclical. And certainly as the staff at FHFA got tired of hearing, I beat the drum every day. Countercyclical, countercyclical, countercyclical. That is the mission. That's the frame we should regulate them toward.

And again, for the other regulators, the Fed or FDIC, I certainly think it's appropriate to heavily examine banks that rely on advances for day-to-day activities rather than stressed activities, because, again, it's the time of stress where they're supposed to be there. And I do worry that because they've become so pro-cyclical, that they actually threaten their ability to be countercyclical. We saw this with Fannie and Freddie 2008, we actually saw this in March 2020 as well. So again, getting them back to thinking in a countercyclical manner is critical in getting the regulator to have that lens as well as the system I think is critical.

Kathryn Judge: I just want to echo that. I mean, I think it really goes back to the micro versus macro question that you asked early on and I don't think we're there. And part of the question, I mean, one is, first of all, they do have a much greater liquidity mismatch than they used to. So there is a possibility that there never used to exist, that they actually might not be able to roll over and expand. And traditionally, they have been able to expand and shrink with remarkable ease in many ways. I mean, if you look at the fluctuations over time, it's been huge. And it's partly because they balloon either when they're stressed in the market and suddenly everybody needs advances or when there's regulatory changes and they conveniently fit kind of the new needs that are being created on either sides of their balance sheet.

So there's been a lot of this elasticity built in, and that goes back to actually the supervisor question is like, are you trying to make sure that you are managing your risk or are you willing to assume some risks in the circumstances where there's actually a benefit to doing so? And those pull in very different directions. And I think part of what we saw I mean; I think Scott famously did a beautiful job with coauthors of looking at the role that they played in providing a huge amount of liquidity in 2007 to the banking system when there was a real need for liquidity.

But we also saw it took the Fed more than a year. I mean, there's more than a year between when that crisis started and when Lehman blew up. And so, like maybe actually a little more pressure early on and a little less liquidity provision would have helped people realize just how big the problem was, rather than kind of like allowing it to linger on and linger on. And so there is a muddying of the waters in having these multiple liquidity providers. And not only that, but they were increasing haircuts really significantly, which is what you want to do if you want to minimize your risk the system, you're like, all right, yeah, I'll take that collateral. But, you know, it was 5% yesterday, 30% today for the haircut alongside the super lien.

But that's very different than if what you're worried about is like the health of the banking system, like how many of the banks are actually going to be able to get through this. And so I do think that there's just a fundamental tension there over what are the risks that we want them to take and what are the ways that they could actually engage in a public service by assuming certain types of risks and avoiding others?

John Heltman: Kate, you said the magic word, super lien. And that's the word of the day. Like and I guess like my question that that leads me to wonder, is the, the primary kind of like public facing exposure to the home loan bank system is in the event of a failure, sort of losses from the deposit insurance fund, right. How, should the FDIC have more of a kind of supervisory role in protecting the diff by kind of maybe reducing exposures that the home loan banks can recoup?

Mark Calabria: I'm going to maybe dig into this just because I think I probably take a little more different, different take. And I don't even really like the phrase super lien. It's a collateralized lien. And it is worth saying that if commercial banks, instead of going through an FDIC process, went through a bankruptcy process, a bankruptcy court would look at this and say, yes, of course, secured creditors get paid before unsecured creditors and the FDIC is essentially an unsecured creditor in this case.

So I do want to be very clear and say there's nothing unusual about secured creditors being in front of the line. That's, that's normal for a resolution process. The problem, of course, is that the original purpose and structure of the banks is essentially be like debtor in possession financing where you hit a stressed environment, and again, no no DIP financer's going to come in if they've got to be at the back of the line. And the problem is it's become like normal financing for the rest of the time. And that's where it's ultimately at it with losses.

I think the problem with the FDIC perspective is it's a selection bias. They only see the banks that fail that come in and then see this and see the secured lien. They don't see the banks that don't fail. Again, Silvergate didn't fail. Other problems with it. If it had not gotten advances, it probably would have failed and would have been a cost of the FDIC. So again, I don't know anybody who claims the bankruptcy process is plagued by DIP financiers yet. I also am fairly certain that probably every corporate bankruptcy, every unsecured creditor hates the DIP financers. But again, it's an important part of the process.

Bruce Morrison: Well, I think the, the, the biggest problem with first of all, the super liens are not as perfected as they would have to be in bankruptcy. There's a shortcut that allows perfecting those security interests. More of a problem is the rhetoric of the bank system about never losing any money. Every time they transfer the loss from themselves to the deposit insurance fund, backed by the full faith and credit of the United States, they have done something that they deserve to be accountable for.

And, you know, that's sort of the IndyMac story. And so if there were a little bit more transparency or straightforwardness about what is going on when this happens, it would be less bothersome. But you will read over and over again, never lost a penny and the never lost a penny ignores two things, investment losses and super lien protections. And it's like everything else about the bank system that's obscure. Making it less obscure might make the debates a little easier.

John Heltman: I was going to add a few things there. First, coming back to Mark's point. It is true, you know, secured creditors are pretty far ahead in the in the priority of claims. But I believe what the super lien does is it takes it a step further and they actually stand ahead of all other secured creditors, including those that have perfected interests, which would include the Fed at the discount window. Now, how we've remedied that over the years is there are agreements in place and there's close contact and coordination between the Reserve banks and the Home Loan Bank in the same, same district.

Now, in terms of losses to the FDIC, and I think this will be something to explore as this group sort of moves forward in talking to, engaging with people at the FDIC that, you know, they do, it's been long understood that this creates a risk of a, of a higher loss given default for the FDIC. I know when Sheila Bair was, was chair, she explored the idea of tying deposit insurance premia to, to advance activity that got shot down. Now, what has happened is, is with Dodd-Frank, we changed the assessment base. And so it is broader across liability, total liabilities, not just deposits. And so some of it is getting captured there.

Another thing is in talking to people from FDIC, in the past, you know, bank failures come in, in bunches and then you have long periods where nothing happens and there can be periods where the FDIC's resources are constrained in order, you know, their ability or time to quickly resolve institutions. And so my understanding is anyway, that there is a lot of communication and coordination in those situations that goes on between the home loan bank and the FDIC. And so it's, I think the super lien is an important topic and absolutely important for this conversation. But I think, you know, the next level will be sort of like, okay, well, let's think about how that affects the way we deal with troublesome situations.

Mark Calabria: You know, just that on the previous panel, you know, I thought Juliann made an interesting comment when she talked about, okay, you have the lien and then the loss of the FDIC. And again, as she I think very fairly and accurate representative, that would almost always be recouped via higher assessments from the FDIC. So while she might not have intended this, what I heard is, okay, we've given a subsidy to banks over here that will later be repaid by banks.

And if we believe that the Fed, the Federal Home Loan Banks and the FDIC were all to some degree backed by the taxpayer, you know, maybe I'm taking a unified budget approach, if you will, it just you know, again, it's the bigger point about why, you know, I don't get really worked up about the collateralized place in line is if you get rid of the secured lending— you can perfect it differently, sure that's a great conversation to cite and I'm all for the FDIC pricing premiums— but if you get rid of the ability to come in and take collateralized preferred lending in a stressed environment, nobody will do it. And then the system goes away. And again, that's, that's an outcome that maybe is fine, but the system has no function if they can't have a front lien, no one's going to make secured lending in that environment.

John Heltman: The, there's something that was mentioned in the first panel, which was that like kind of like where will change come from? Like should it, does it need to come from like top down does like, this need to come from Congress or Regulators or do the members of the system itself need to kind of like insist upon, do they have an affirmative requirement to insist upon change? And I seem somewhat skeptical that anything might happen to accept because, I mean, like the home loan banks are a pretty sweet deal, like for members. And I sort of am skeptical of like banks voluntarily kind of giving up a golden goose. But that's my, you know, yeah. I mean, that's my idle speculation.

But I'm curious what you guys think about what would like cause if you have regulators kind of forcing a system to adapt and change in very specific ways, there tends to be like resistance to that. And so, like, I appreciate the idea of there being some kind of buy in and, you know, mutual understanding. I guess like my, let me condense that into an actual question, which is how do you see, what are the, what are the most important flash points in the regulatory structure over the home loan banks? And where do you see maybe the members themselves agreeing to changes and where do you see regulators having to kind of insist? Mark, you've been so good so far.

Mark Calabria: You know, General Rahm Emanuel never let a crisis go to waste, I mean, Silvergate has given us, given the regulator an opportunity to take some aggressive things that they could not do in normal times. And again, you know, ongoing asset test, changes in advances. You know, you could always also look at some other regulatory changes. So to me, that's where it's going to come. I certainly am sympathetic, and I don't want to at all minimize the great efforts that Carol and Senator Cortez Masto have done. But I would not bet on Congress passing anything on mortgage finance reform barring a crisis. So if we start to see failures and problems then maybe Congress does something, but it's not going to come from Congress.

But as you touched upon, I mean, certainly the members you know, the problem is that there's a huge chunk, well the observation is there's a huge chunk of members who really don't do a lot of advanced business, but they like the dividend and so they vote for the dividend. You know, those members who pay more for advances should probably push back on that and say, why are we dividending? You know, the members should push back on on allowing, you know, other non-banks in so certainly the members of the system have an incentive. And again I've never found ICBA to be shy about expressing to me what their belief in the system was.

And so I do think that there is an avenue there for the members to ultimately drive what's going on. But again, the regulators get, got an opportunity, a small window of opportunity to be aggressive. But I'm not counting on Congress to do anything at this point.

Bruce Morrison: I think the, we heard from Susan Rice this morning some really important things about mission. That is to say the sad fact that our financial system from the thirties to whenever you want to put an end to it maybe not yet has been racially discriminatory. And that's a real thing. And it's built into our economy in really fundamental ways that are, that are unacceptable. So if there's one thing that mission regulation could think about, it's how to address that. And it doesn't matter whether it comes from the top down or bottom up. I mean, everybody does have a title eight fair lending responsibility, and there's room for work there.

The other thing to be said is that my favorite idea is the creation of a 12th bank that uses the strengths of the Federal Home Loan Bank system going back to the thirties, which is to identify assets that are not supported by other mechanisms like securitization and to support them and to use that 12th bank to demonstrate what those markets are, that they can be safely and soundly addressed and that maybe other parts of the bank system will say, oh, this is a business, we can do this, which probably won't happen if you tell the other 11 banks what they have to do. But if you create something where the all the incentives are to do something that's needed but it's not being done, maybe it gets done.

Kathryn Judge: Can I jump in really quickly, because I know we're, we're at time so I don't want to say much—.

John Heltman: Last word.

Kathryn Judge: But we are at a really, I think, exciting moment, generally speaking. Yes, everybody should buy Mark's book. You can preorder right now, Amazon or Bookshop.org. But alongside doing that and we'll be back here for an event signings, I'm sure we are, I think at a really exciting moment where we're rethinking economic policy in really big ways. And so a lot of, we've talked a lot about the REVCORP bonds and the merging of, you know, basic like thrifts and banking and all the changes that happened.

But then there was a subsequent shift too where there was a bipartisan understanding that we wanted large multinational corporations supported by large multinational banks and transform the entire structure. And that's part of all the trends that we're talking about. That's part of what made housing finance so fungible with other forms of finance. And I think we're suddenly at a shift right now where you see both parties suddenly thinking in very creative and broad ways over well, what do we want the actual structure of the economy to look like? And maybe bigger isn't always better.

And I think what has not been fully fleshed out, so a lot of that's been happening in the competition space, but it was what has not been fleshed out is how do we have a credit creation system that supports the type of broader economy that is more diffuse in terms of where power and activity actually lie. And I think this can be part of that conversation, and that might be wishful thinking. But, but it's interesting to see things are happening right now that five or ten years ago nobody would have thought possible. So, so it's important to, to not just think about what's immediately practical in having these conversations.

John Heltman: Well, with no further ado, let's have lunch. Can, join me in thanking our panel.

Harrison Fregeau: Hello again, everyone. Just going to butt in here to get us prepped for panel number three, which is going to get into the FHLB reform aspect of it. So to introduce all our panelists, we've got Dennis Shea, who is the Executive Director of the Ronald Terwilliger Center for Housing Policy. We've got Aaron Klein, who is a Senior Fellow here at the Brookings Institution. We've got Michael Stegman, who is a Nonresident Fellow at the Urban Institute. And we've got Megan Haberle, who's the Senior Director of Policy for the National Community Reinvestment Coalition. And moderating this panel will be Katy O'Donnell, who is a reporter for Politico. So everybody can come on up. Thanks.

Katy O'Donnell Oh, sorry about that. Just to start off, I wanted to sort of broadly ask what you guys think the best use case is for these institutions going forward, both for the banks themselves, but also for the public interest. And Aaron, do you want to start?

Aaron Klein: Sure. I'm, I'm happy to. Look, when I try to teach and give lectures and I say there used to be a thing called a thrift that was different than a bank, you get blank stares from anybody under the age of 30. And at this moment, there really is no difference. So we have a weird structure where the home loan bank system was set up to be a lender of last resort for a parallel financial system when thrifts were different than banks and mortgage finance was different than consumer lending. That system doesn't exist.

So in a first, like in a theoretical world, you'd say, well, if the underpinning rationale for the creation of this system doesn't exist, then get rid of the system, right. But I think is it, is it Ronald Reagan who said, you know, the closest thing there is to to the afterlife or eternity is a temporary government program, right. These things are never set up to be temporary, nor I think, would anybody ever rationally expect them to go away. So the question then becomes, how can you use them best for the public purpose?

And I would posit the following kind of core hypothesis, which is that the government has decided to create government incentives for a wide variety of types of structures, nothing more than in the 1 to 4 family mortgage. Four family houses. Anybody here live in one of those? When you think about a American dream and homeownership, right, single family, we actually have duplexes, triplexes. We have a mortgage finance system that treats a four-family home the same as a one, but a five-family home totally different. All right. That doesn't make any rational sense.

And I think when you start looking at smaller unit spaces, as well as mixed use, right, where you have commercial and retail co-mingled, which is, I think, what the future of a lot of New Urbanists want to see in the world, you have a housing finance system that's very predicated on the distinction between commercial and residential and very focused on 1 to 4 or then much bigger units. So from a public policy purpose, I would like to think of using this kind of legacy system for a thing that doesn't exist anymore called a thrift and instead think about how can we develop a robust way to support markets for the types of physical units and dwellings and structures that a large part of society wants to create, which would be mixed use, you know, more than four units but say less than 49 space.

And the rationale I would give for why the government should preference these things is not necessarily a long list of why we want these things, which I think, you know, in terms of environmentalism, in terms of, of new urbanism, I think all those things are valid. But, but the other way is why should we put so much more subsidy into 1 to 4? And if you're going to have that much into 1 to 4, you ought to have an at least an equal amount into mixed use and other things. That would be my idea.

Katy O'Donnell How about you, Dennis?

Dennis Shea: Well, first of all, I want to thank Brookings and Boston University for giving me this opportunity to to speak today and participate in this panel. Years ago, about a decade ago, I worked with Bruce and maybe a few other Bruce Morris and a few other people on the BPC Housing Commission report, which outlined this amazingly in-depth plan for reforming the housing finance system. And Rebecca Cohen, here she was, she was a colleague of mine as well. And we had, you know, lots to say about Freddie and Fannie, lots to say about creating a new public guarantor and a guarantor for catastrophic risk. But we said virtually nothing about the Federal Home Loan Banks. Maybe a couple sentences were in that report that just said they did a good job during the financial crisis and providing liquidity for it, promoting advances for their members.

So I'm, I say that because I think it is really important that this effort is underway. I want to commend FHFA Director Thompson and Brookings and BU and Senator Cortez Masto for shining a light on what is the purpose, what is the value that the Federal Home Loan Banks are supposed to provide? I would say from my perspective at the BPC at the Terwilliger Center we're all about promoting housing affordability on a bipartisan basis.

And we see the housing affordability crisis, which we're experiencing today, as having three dimensions. One, the severe lack of supply to meet demand. Secondly, the need to preserve our existing affordable housing stock. And third, to provide demand side supports for households whose incomes do not match their, their housing costs. And I think if we're going to repurpose or tweak the Federal Home Loan Bank system, maybe more than tweak, I think a focus on, on housing supply, they could do a lot more in the area of housing supply. And I think this area of 5 to 49 multifamily, which has been traditionally underfinanced, is, is a worthwhile idea. So I want to share that with you, Aaron. Thank you.

Katy O'Donnell Megan.

Megan Haberle: Yeah, thank you. So I want to start by reinforcing the points that others have made throughout the day around the need for a serious institutional and structural shift. So taking the Federal Home Loan Banks from a point where they have a 10% affordable housing program, and that's viewed as a tax and an important program, but still kind of a boutique program, and to making sure that these kinds of public policy ends are really at the heart and soul of the Federal Home Loan Bank program. I want to also focus on not only the FHFA but also the community support requirements that are currently in place.

Currently, the Federal Home Loan Banks are required by statute to look at CRA performance, as well as performance for first time homebuyer support as setting a floor for that community support program requirements. I think that program could be expanded and used in a much more robust fashion to make sure that we're not only tracking advances, but deploying advances to the kinds of public purposes that we want to see. That also means an overlay and alignment with other aspects of our housing and community development system so that affirmatively furthering fair housing requirements that Lisa Rice was talking about earlier.

Also the CRA obligations, which advocates are hoping to see regulators gain a lot of traction on in the near future, making sure that those requirements better serve communities and are more specific going forward. And so bringing in an aspect of systems alignment and also an aspect of more robust, deeper community service to the Federal Home Loan Bank system I think is really critical as as a part of this endeavor going forward.

Katy O'Donnell And how about you, Michael?

Michael Stegman: Thank you. Let me just start by saying that the Federal Home Loan Banks at 100 initiative is incredibly timely and important. And there's a lot of speculation out there whether this is really going to be a serious exercise by FHFA or is it more perfunctory. And my view is that FHFA is taking it incredibly seriously, that it can do a substantial amount to re-knit the mission between providing liquidity to its members for the purpose of expanding essentially affordable housing finance, that it can do substantially more than just allocating 10% to affordable housing, but it can actually really do a whole lot to re-focus the members and the banks on its historical mission and has lots of opportunity through its administrative and regulatory authorities, as well as educating the public about what the home loan bank system was, is and can be in the future to contribute significantly more than it has to helping solve our affordable housing program.

And I just want to say that I was, I funded the BPC Housing Commission when I was at the MacArthur Foundation and the day that it formally began, I had a couple of weeks before been appointed to Treasury to lead the housing finance reform efforts in the Obama Treasury and ended up having to compete with BPC. But hard as we tried during our GSE reform days, we could not bring a Federal Home Loan Bank title to our proposed GSE legislation. There was neither Democratic nor Republican support for reforming legislatively the home loan bank system. And so we really have to rely, I think, much more heavily on what we can do through regulation and legislation over the foreseeable future.

Katy O'Donnell That's actually something I wanted to discuss. What do you guys think is kind of the most critical reform that can be done without Congress, given that there's sort of a very small likelihood that Congress will do anything here.

Megan Haberle: I can start. So I think, again, tracking the advances, but not only tracking the advances, attaching stronger strings to them and making sure that they're, you know, better defined. And I think also providing more discernment and nuance in what housing and community development should mean even within that tracking of advances. So we want to make sure the advances are attached to that core purpose.

But let's start to think in more detail about how do we service, you know, fair housing ends through those kinds of investments, how do we make sure that the kinds of considerations that we're looking at currently under the Community Reinvestment Act, so ensuring, for example, that housing development doesn't result in displacement, ensuring that there are tenant protections in place, you know, looking again at what FHFA is doing in other areas of its regulation and governance and bringing that kind of muscle level of detail into the Federal Home Loan Bank system, I think would be a great start.

Dennis Shea: You know, I'm not sure if this exists, I've read some of Khan, Khan Hurley's work on this issue, but not sure if this is a governmental assessment, but I think it'd be very helpful in terms of transparency to have an assessment of what is the value of the taxpayer benefit provided to the Federal Home Loan Bank system and what is the value of what the Federal Home Loan Bank system is doing for the taxpayers? And sort of a clear-cut assessment of that, I think would really promote transparency and public understanding.

Aaron Klein: So the nuclear bomb that can be dropped without Congress is designation as a systemically important financial institution or SIFI, which would transfer the home loan banks from FHFA to the Federal Reserve, right. And in the definition of of what makes a systemically important financial institution, the first thing is size. And they're worth $1 trillion. That's pretty big. The second thing is always called interconnectedness. You can look up anybody's paper, anybody's speech, Democrat or Republican, whatever. It always says size, but it's more than just size, its next word is always interconnected. There is nothing more interconnected by law than the federal non-bank system. Nothing else has joint and several liability of the entire banking insurance network, right. Definitionally, they're the most interconnected things they've, in the, right because their debt is issued systemically, not individually by bank, even though their incentives are often individually by bank.

So to answer your question, that's the biggest thing that could be done. Now, I don't think that's likely to be done. I've yet to see a case where FSOC has taken jurisdiction from one regulator and moved it to another, they were a federal regulator, state insurance regulators would be the first ones to pipe up and say, no, no, no. Absent that, there I think are a couple of other things, where the regulatory authority exactly lies in how much strength there would be there, you can look at single member, single district membership, you can look at capping advances so that no one bank has more than X per share, percent of advances from any one bank, those can be judged on safety and soundness and competition grounds regulatory.

The final thing the Regulator could do, which isn't as much of a big deal from a public policy perspective, or the true North star of this conversation, which I think has been rightly identified as, as affordable housing and fixing homeownership gaps and racial disparities and access to opportunities so that's a true North Star, right? But the thing that would really generate a lot of stuff that can be done totally regulatory is executive compensation within the banks, which is also another figure that hopefully we'll get a chance to talk about, I think has gone completely out of control and the regulator would have authority to engage in that.

Michael Stegman: The FHFA can certainly help dispel the myth of zero public subsidy. Absent the implicit federal guarantee, Standard and Poor’s says that the ratings for the Federal Home Loan Banks would be six notches below where they are today, which is comparable to U.S. government Treasury rates of borrowing. Secondly, FHFA, FHFA could stop the home loan bank system and individual home loan banks from lobbying. According to Open Secrets, in 2021, the system as a whole spent more than $3 million in lobbying fees and for government sponsored enterprises that receive the multi-billion dollars of taxpayer support, they should not be lobbying. FHFA should help fix the CDFI community financial institution problem.

We should not have just 64 CDFIs. The growth in CDFI membership went from 64 to 68 over the last few years. There's a real serious collateral haircut issue. FHFA could really help address that issue with helping third parties to help CDFIs provide collateral. They could, as Reverend Cortes talked about, use some of their restricted return earnings for first loss reserves. They could, FHFA could mandate the member banks use what the bank's system argues is part of their affordable housing commitment, the Community Investment Program advances and the community investment cash advance programs to support a whole lot more affordable housing and community development funding. And to give you an idea, reserve, advance total combined advances were about $351 billion in 2021, and the total advances in these two affordable programs totaled under $3 billion.

So there's just a whole lot more juice that can be really generated from FHFA kind of mandating more of, of its members, of its banks to support that. FHFA, and you have to really be careful about using the GSEs and the great things that I think FHFA has done to refocus the GSEs much more on their mission and equitable finance obligations because she wears, the director whereas two hats with the GSEs, both as regulator and conservator.

But I really do believe that through pricing and internal cross subsidies, the home loan bank system can support a whole lot more mission funding of affordable housing and community development activities than they currently are without increasing risk. Because what you would be doing essentially is reducing the costs on advances to mission-based organizations while increasing the markup on advances to non-mission institutions and businesses so that the overall economics and finance between risks and, and fees really aren't adversely affected.

I think that there is some work that should be done around board membership of banks, maybe looking at increasing the independent members on boards and looking a little more closely at who independent board members are. They shouldn't be former members of the board from member banks and so on. They should be more community representatives. I think that from the standpoint of compensation that Aaron just mentioned, the GSEs have a scorecard where that performance is tied to critical, mission critical activities. And certainly we ought to think about how that kind of incentive for meeting again, mission critical affordable housing funding can be, can influence compensation. And I agree with the single membership, there's no reason that seven you know, a commercial bank should be a member of seven different regional banks. And, and I agree on capping the advances to avoid concentration risk as well as a race to the bottom. Just to begin some of those thoughts.

Katy O'Donnell The next thing I wanted to discuss is the Silvergate episode. I'd love to get kind of a sense of your takeaways from that. I mean, it seems like there's this discussion of, you know, is this mission creep or did the system work as it was supposed to work? And do you think that this catalyzes reform going forward or is it does it make it sort of is does it place restrictions on the discussion around reform by making it more likely that the mandate will be reduced?

Aaron Klein: You know, I think it's a complicated question because the answer to a lot of it is just yes, right. You are, the system worked as it was intended. Mission creep, you know, Scott, one of the things in Scott Frame's great paper lender of next, last resort was you just looked at who in '06 and '07 the advances were going to and then you looked at who the biggest subprime lenders were and it just paired up. And in the most costly loss of any bank failure in American history on a nominal basis is IndyMac. And IndyMac was a huge user of the home loan bank system and aggressively arbitraged between the Seattle and the San Francisco home loan banks increasingly deteriorating, i.e., crappier subprime mortgages to fund their ongoing business model. And yes, the home loan banks recovered every penny they lent to IndyMac because they stood in front of the taxpayer who bear those losses.

Now, in Silvergate, we never quite got there, alas, I, I think it's a problem that we haven't had, that we didn't have a bank failure in the last two years. The only other time in American history we've had two years without a bank failure was '05 and '06, and the bank regulators went around Washington telling us all what a great job they'd done, instilling high levels of capital and properly managing bank risk, right. We have 5000 banks in America. Some should fail. If Silvergate failed, that would be fine. They tried a different business model. They went into some new technology. Didn't work out for them. Okay. That's capitalism. We need a little bit of failure. Without failure, right, well, does it feel like a normal country if 5000 banks operate in perpetuity? None failing?

The question, so I don't think it's that way. And when you say it's mission creep, I'm not sure how much the advance system today, because there's no difference in bank and thrift is tied to, as Mike's kind of eloquently coded, quoted, the actual mission in the statute. So hopefully it will be a catalyst for reform. But I tend to think its ability to catalyze reform was short circuited by the fact that the bank itself didn't fail. Yet.

Dennis Shea: Well, I mean, I don't have much more to add to that. But the fact that $4.3 billion in taxpayer subsidized advances were being given to an institution while there was a run on its deposits, was the Fed, was the bank in San Francisco aware that Silvergate was a major player in cryptocurrency? And what does that have to do with the mission of promoting, promoting housing?

So I think it helped catalyze or maybe crystallize the need for an effort like this to sort of examine what, what is the Federal Home Loan Bank system because most Americans do not know anything about it. I would say most policymakers in Washington don't know anything about it. And I would suspect that most people who, who participate in the banking housing space like I do, have an understanding that is limited of the system. So something like this helps catalyze interest. And, you know, we'll see, we'll see where it leads.

Katy O'Donnell Yeah, I agree about the, you know, the beneficial effect of sunlight being shown on some of these problems. I also think, you know, in addition to this issue around tracking advances, the governance plan around the board composition and membership is a really important one to emphasize. So currently there's a marginal presence of board members with a connection to a community, and that ratio should really be, be turned on its head, you know. And so we should have much more of a board presence, you know, from, from individuals coming from organizations, you know, with established community connections, community ties, knowledge of fair housing and fair lending and those kinds of qualities that really should be present in the governance capacity on the boards.

Michael Stegman: You know, the only thing I would add to my colleagues is that I think it puts the likelihood of mission kind of focused legislative proposals like Cortez Masto, which is intended to try to bring the mission back to the funding of liquidity. It actually makes it less likely that we could find legislation that would be just fine tuning at the margin to get us back a little more into the sweet spot of home loan bank funding of affordable housing and community economic development activities, because it raises these more fundamental questions about the future of the system, which Congress is not going to deal with. So I have no reason to believe that this transaction is going to have congressional transformational legislative implications. But I fear that it will kind of drown out these more subtle, nuanced, important legislative efforts to improve the affordable lending situation for the banks.

Katy O'Donnell Do you guys think the priority lien makes sense going forward? Is it creating moral hazard?

Michael Stegman: Again, pulling one thread from a very complex, interconnected system and say, well, we're going to keep the system in place, but we're just going to remove the super lien, it just doesn't make system sense. It has broad implications for collateralization and haircuts and other things. So certainly that can be looked at. There's no question that all the kind of scholarship and analysis indicates that the super lien for the banks increases expected losses for the DIF and, and so on. And so it raises the question of whether it should be paid for and whether it gets paid for through higher DIF to all banks or actually paid for by those who use the advance system by increasing fees and so on. But I really can't see pulling one piece and saying you're going to see any legislative efforts to single shot problems like that.

Dennis Shea: I mean, there have been a couple of studies that I've seen, University of Arkansas, Fed New York that says, yes, the super lien creates moral hazard and it makes the banks less interested in the credit worthiness of of their members. So, yeah, I, I'll defer to those experts, but to the Fed in New York and to those in University of Arkansas, but it seems to be the case.

Aaron Klein: So I have some sympathy to Mark Calabria's earlier point about, you know, there is one government and there is one public subsidy. But I also have some sympathy to the fact that we have accounting systems that are set up that don't treat the world like that, right. The Federal Reserve is treated very differently then the FDIC's deposit insurance fund that is treated very differently than the home loan bank system, right. And so what I think we have not through conscious thought, is a system in which the home loan banks stand in front of the other arms of the government. And that has to be coupled, per Mike's point, with the fact that they have joint and several liability of their debt.

And I think you have to couple those two things because if I'm a bank in city X and my profits are based on how much I can engender and my risk of if my bank defaults is pulled among everybody else, right. It's not my creditors who take haircuts. There's no situation in the market that's saying, oh, you know, Cincinnati is is being more aggressive than New York so we're going to trade their debt at a different rate. No, no. All the debt trades identically. And I can't, I structurally cannot lose. I can only force losses on different elements of the government. It, it gives rise to the classic wrong set of incentives you want for an institution where the more risk you get, the more profit you make, you personally, right. The President of the Des Moines Bank makes over $2 million a year, right, and that's tied to the amount of revenue there. And if there's a failure, well, someone else bears that consequence.

And that's, that is the I, I don't think you can get to that. You, could you get to that just by attacking the super lien, possibly. But I think any solution has to address that holistic problem because otherwise you just, you have the wrong set of assumptions and incentives in place in this structure, and it's going to end up costing people a lot of money.

Katy O'Donnell The, in terms of the membership, should it be expanded to include non-bank mortgage lenders? Does that sort of necessitate tougher requirements for capital liquidity? Is this a conversation that's worth having?

Dennis Shea: It's an eight out of ten, sorry. Eight out of ten biggest mortgage originators are non-banks. So if the one of the purposes of the Federal Home Loan Bank system is to promote mortgage liquidity and promote homeownership, affordable homeownership, that suggests that maybe they should be in. The question is, how are they regulated? Again, I'm going to defer to these banking experts about the regulatory structures over banks and insurance companies. There seems to be a lot of regulation today over banks, insurance companies and not much regulation over non-banks. So if you talk about if you're going to bring the non-banks in who is the regulator, I guess FHFA could be the regulator. But it's a very interesting question.

Megan Haberle: Yeah. So I also you know, one key difference is the community reinvestment obligations that are placed on the banks. And already this is, you know, I would say setting a pretty low floor. So currently your community support obligation is a is under regulation a satisfactory CRA rating or above. So I would say, first of all, there should be sort of, you know, more stringency and nuance there, even placed upon the banks. Nonetheless, it is still a very key distinction that the banks have this community reinvestment obligation, they are being examined on that basis. Mortgage companies currently do not have that kind of community reinvestment, scrutiny or obligation. They could, there are states that have done that.

So Massachusetts, for example, does require that of mortgage companies. So perhaps if there are those kinds of conditions placed on the mortgage companies at the outset, you know, then I can see it beneficial for them to come in. But otherwise, there's a very uneven playing field that you have in place there. And I would also point to the insurance companies that are also off the hook for that kind of obligation. So I do think that's another sort of problematic area that might merit scrutiny going forward.

Michael Stegman: Yeah, this is, this is really a challenge if you kind of just step back, we have large numbers of commercial banks that have pulled back from the mortgage lending and rely very heavily on home loan bank advances. We have independent mortgage banks that account for 60% of all mortgage originations that are outside the system. On the other hand, the independent mortgage banks have increased their market share over the last 10 or 15 years from 15% of originations to 60%, all without having to have access to the advance window. IMBs really vary dramatically they're not all of one shape or size, and many of them don't address affordable housing needs at all. And it's not clear to me that they necessarily ought to be members. Congress will have to make that determination and certainly FHFA should not enable through back doors or loopholes for any huge new class of members to enter the system.

And then finally, when you look at the arguments that independent mortgage banks make to why they should be allowed access to the advanced window in membership, they speak to the periods of financial stress when they need more liquidity to either buy out loans from securities or to really service delinquent loans and so on. But the reality is that the advance window is open 24/7, 365 days a year. And that raises the question of whether there should be a different kind of class of membership or through pricing, such that the cost of advances are only in the money during extreme periods of stress. So there are a lot of, there are a lot of variables around which you can have this discussion, but certainly blanket membership to all IMBs is not something that I would subscribe to.

Aaron Klein: Well, the advanced window is really exciting me because America's payment system is about to close for the weekend in a few hours, which is going to cause tremendous hardship as people get overdrafts at which the, the Fed's payment system would operate as much as the home loan banks and the same hours as the home loan banks advance system. Juliann Thurlow said something that still has my mind buzzing earlier, which was that people are better off when they have their mortgage at a community bank and they can be serviced when they have a problem by going in and talking to a person. And that kind of resonated with me as kind of something that would be true.

Now, that is not the direction that the U.S. mortgage system is taking. We are going as fast as possible in 180 degrees in the opposite direction. And we're doing that because there's a series of efficiencies of technology and a series of incentives put in place towards commoditization of mortgages, often as a result of government financing and government subsidies. Whether the "free market" would get there on its own, we'll never know because we don't have such a free market. We have this existing market with these distortions, but they're moving us on this direction of commoditization where you get your mortgage from a faceless, you know, AI online and it gets processed through and then put into some other kind of mortgage commoditization box.

And for those people that exist in that credit portfolio and never run into a problem, which is a lot of people, it works really well and it's super cheap. For those who don't fit into that credit box or who run into a problem, the system really breaks down. And that therein lies a difficult question, which is how much do you want to design support for those folk? My natural instinct is quite a bit for a variety of reasons, including historical discrimination, including the existing structure there, and including creating opportunity for wealth building for for folks that are currently avoided, America is a minority prime nation. Less than half of Americans are prime credits. And so why do we keep building a system that works well for the winners of the system?

But this is all illustrative because if you let in those other groups that you're talking about, you're going to further advantage them in building this other system that works really well in these situations, but not for these folks. If you keep them out, then you're tilting the playing field a little more in the direction that it is. But I would argue not enough still being fully transparent that that does involve some amount of cross subsidization away from the people for whom that commoditized system would work well and towards the people who need to go in and talk to somebody because there's a servicing problem, I can't make my mortgage payment possibly because my child support and alimony payment hasn't come through because Fed wire closed at 5:00 or ACH closed at 5:00 on Friday and my spouse's payment is waiting.

Katy O'Donnell Got it. Well, I think that's all we have time for. But thank you guys so much. This was really interesting and hopefully this sort of sparked some conversation among the people who have the power to reform it. So thanks so much.

Harrison Fregeau: Oh, at 1:00, we're going to have Director Thompson up here with Professor Hurley in a fireside chat. And so we're just going to take the next 10 minutes to reset the stage and then we'll present that to you guys. All right, Thanks. Hello again, everybody. Let's take our seats. I'm happy to announce that we're going to proceed to our keynote fireside chat. We're going to have it be moderated by Professor Corn Hurley of BU Law School. And our esteemed guest is director Sandra Thompson of the FHFA, who has kindly provided her time here today. So I'll have them both come up. Thanks.

Cornelius Hurley: Welcome, everyone, and thank you for sticking around to see me. Now, Director Thompson, I can't tell you what an honor and a pleasure it is to be with you today and thank you for coming. Everybody in this room already knows who you are. You need no introduction. Years, nearly three decades in financial services, regulation in Washington, FDIC and now FHFA. So since I cannot properly introduce you, I thought about what I would do is embarrass you. Is that okay with you?

Sandra Thompson: It depends.

Cornelius Hurley: Well, you be the judge. We've been talking all day today about FHL Banks at 100. Tell me when you have ever heard of a regulator taking on the burden of revising the entire mission operations efficiency of the very industry that he or she regulates? I cannot think of any case like that. The closest thing that comes to my mind, many of you may recall Brooksley Born, who was the chairwoman of the CFTC, and she discovered that there was something called over-the-counter derivatives in the mid-nineties, and they might someday apris a problem. And she fought back against the masters of the universe, white male regulators, Alan Greenspan, Robert Rubin, Larry Summers, to name a few, saying that very thing that there needed to be regulation. And for her courage, she received the Profiles in Courage Award at the Kennedy Library.

Now, I'm not saying that you're going to win that, but you do have, I do have a few friends in Boston who I can speak to, so, so just be aware. But I thought I would ask you to tell us a little bit about yourself that we don't know and what it was in your background that caused you to launch this very, very ambitious and, dare I say, courageous endeavor?

Sandra Thompson: Sure. So first, thank you for the opportunity to be here. And I really wasn't expecting all this interest in this particular topic. After getting initiated as the acting director and then the full-time permanent director, you know, part of my responsibility is the home loan banks, unbeknownst to many people, because we spend so much time at FHFA on issues pertaining to Fannie Mae and Freddie Mac. And so I actually you raised a good point, I've been in Washington for 30 years, and I came to Washington and started working for the Resolution Trust Corporation, which certainly was the result of the savings and loan crisis. And then I had the opportunity to serve at the FDIC, and I was head of supervision during the Great Recession.

And so I have seen the impact of not paying attention to regulated entities. And it's part of my responsibility not just to pay attention to, you know, our role as conservator and regulator of Fannie Mae and Freddie Mac. But we are supervisor and regulator of the home loan banks, and they play such a crucial role in the housing finance sector. And that was evidenced during the pandemic. They certainly play a huge role for providing liquidity to community banks, which I think they do very well. But we had looked at the home loan banks over the years, but just different aspects. Like we looked at membership, we looked at the affordable housing program when we took a stab at revising the rule.

But the impetus for the change came because I started asking a lot of questions about like the supervision of the home loan banks and how it was going. And then, you know, I shouldn't forget the open letter you and Bill Isaac wrote to me and the American Banker that raised a lot, I did not. No, no, no. You know, I get letters all the time with suggestions. And, you know, I read it and I thought that there were some valid points in there. And I started asking lots of questions.

And my questions led to, you know, projects here, projects there. And I said, enough, let's just do a holistic review because I really want to understand, you know, the mission of the home loan banks as described by Congress, and to better understand whether the banks were continuing to fulfill that mission in a way that had been expected. And when I was thinking about it, like in 1990, there was like 14,000, you know, depository institutions. I think now there's probably less than 5000. And so the mortgage landscape has changed. Last year, the home loan banks celebrated their 90th anniversary. And I'm thinking going into the centennial, you know, are we positioned to be ready? I'm certainly not going to be around for that, but no I will not trust me on that. But no, but it's my job—

Cornelius Hurley: I can say that, but you can't.

Sandra Thompson: I could say, trust me. But, you know, it's my job to position the system to be ready for, you know, what is to come. And it was interesting because when we started the conversation, there were lots of people that had varying ideas, and I just didn't know that it would garner this much attention because it was really intended to be kind of a supervisory slash mission review of the entities that were responsible for regulating.

Cornelius Hurley: Yeah, well, great. Well, you raised the issue of mission, but before we get to a discussion of mission and your reflections on that, can you tell us your takeaways from the listening sessions and the roundtables that we've had thus far? And there's been so many of them and there are more to come, right?

Sandra Thompson: Yeah, there are. So we started the review in the fall. We had the listening session in Washington and then we thought it was important to get stakeholder input because once we announced that we were doing this review, people were calling in and they were writing in. So we wanted to make sure that we got robust stakeholder input, and you know we've got a request for input, input process where people can, you know, provide written input or, you know, they can participate in these roundtables.

But it was just so very interesting that there were so many people that had views on the Home Loan bank, you know, and I would say to a person there, the roundtables have really articulated that, you know, they do serve a purpose, they do serve a mission. They provide liquidity, you know, especially to community banks. But we've also heard that sometimes larger institutions have used the advances for, you know, balance sheet purposes specifically to be in compliance with their liquidity coverage ratio.

And so, you know, thinking about, I guess, you know, what were they designed for? What are they doing? Are they fulfilling the mission part? Because certainly when we think about the home loan banks, it's two prongs. So we've got liquidity and then we've got, you know, contributions to affordable housing and also to, you know, investments in community. So they're fulfilling their liquidity prong very well. But with regard to the affordable housing and community investment, I think they do a good job. But I think we've heard at every single roundtable that they could do better.

And then when you look at, you know, the advances, how are they being used? You know, it's called Federal Home Loan Bank for a reason. And so are the members using advances to promote, you know, affordable home lending or community investments or are they doing other things? And so I wanted some answers to those questions because the statute is very clear on what the roles and responsibilities of the Home Loan Bank are.

Cornelius Hurley: Yeah, it is. And I'm sure you're going to bring more clarity to it as time goes on. And speaking of time, we have a few lawyers in the audience here. And lawyers love process, you know. So can you, can you satisfy those eager lawyers by telling us what the process is going forward for this project?

Sandra Thompson: Sure. My first if I may take a point of personal privilege and acknowledge my former boss, Dr. Calabria, I didn't see you in the back. I just want to say hello and lots of friendly faces in the room. Lisa and Mike, Carol, Chris, Peter and Peter and I go way back to RTC, so having said—

Cornelius Hurley: You could've had this in the lunchroom.

Sandra Thompson: Yeah, we could've. Seriously, though. So the question that you asked was, what's the output.

Cornelius Hurley: Or what's.

Sandra Thompson: The process? Okay. So we've had the listening sessions, we've had roundtables, and we're taking notes furiously, and we did want this to be a transparent process. So we've got all the roundtable sessions are on the FHFA website. We're getting ready to kick off the second half of the roundtables starting on Monday in Las Vegas, and I think the team is going to Los Angeles and Boise, and I think we're going to have some virtual sessions that cover Hawaii and Guam and the U.S. Virgin Islands. So just to make sure that we're getting stakeholder input from all interested and interested parties and members, because the home loan banks cover all the United States, states and territories, and are they providing services to all of their members?

We think it's important to get as many perspectives as we can. Once we're done with the roundtables, it's going to, we're going to have a wrap up listening session and then we're going to draft a report that'll include some recommendations. Some of those recommendations will likely be to the Congress, and then there will be some recommendations that we FHFA will be able to implement.

Cornelius Hurley: And by recommendations, do you mean advance notice of proposed rulemaking or something more broad based than that?

Sandra Thompson: It could be all of that. And we are not just limited to one method of, I guess, communicating our changes, like the statutory changes, of course, will go to the Congress, but we could, you know, issue guidance or we could do rulemaking, or we could, you know, have some supervisory matters that we'd like to, to move forward.

Cornelius Hurley: Can I, can I press you a little bit on that? Well, how far do you think you can go as far as mission, collateral, membership, some of these hot button issues without having to go to Congress?

Sandra Thompson: Well, I did say that the report would include some statutory recommendations with regard to mission and specifically the item that comes up all the time and for many, many years are increases to the affordable housing program, because, of course, the mandatory 10% that is a statutory requirement. And, and if, but if the home loan banks wanted to do more than that, they've got voluntary programs that they're currently using. There's nothing that stops them from going above the minimum. And some of them do. And there are, there's nothing wrong with them making contributions to other voluntary district-specific programs because there's a lot of opportunity there. And so a little encouragement might help.

Cornelius Hurley: And pardon me if I could interject, there's nothing to stop you from giving them a better examination grade if they do go above that minimum.

Sandra Thompson: Well, I don't, you know, we've got.

Cornelius Hurley: I don't want to put words in your mouth, but.

Sandra Thompson: You know, we've got.

Cornelius Hurley: The same track.

Sandra Thompson: So we've got, you know, safety and soundness. And we do examine the banks for that. And we define our expectations through our exam procedures. And, you know, they know what to expect because it's very transparent. But I do think that there's more that they could do on the mission side. Yeah. In a safe and sound manner. Yes. Just say that.

Cornelius Hurley: I know you weren't here for the sessions this morning, but that's a constant theme of what we heard is more, more, more and 20%, sure that would, that would be good. But maybe we can do more than 20%.

Sandra Thompson: Maybe you could. You know, we are dealing with a huge housing supply issue, and this comes up all the time. And people are so focused on, you know, what Fannie and Freddie can do. There are things that they can do, but there are other things that they just can't do by charter. And so thinking about it, well, we've got lots of regulated entities and, you know, federal home loan, you know, banks are the other regulated entities and how can they be helpful in contributing to the supply. When we look at some of the AHP projects, it's just a sliver of, you know, the capital stack on many of these projects. And so are there things that could be done that aren't being done, that should be done that we can encourage?

And certainly, I mean, the whole point and I think community banks are really well versed at this, it's just building upon in their communities and making loans to, you know, persons and projects in their communities. And so there just is, there are lots of things that could be done. And I, I actually met with the Home Loan Bank Council last week and I think they're open to and want to, you know, improve some of the things that they're currently doing.

Cornelius Hurley: Okay. Speaking of the Home Loan Bank Council, let's talk about the taxpayers for a moment, right. The Home Loan Bank Council denies that taxpayers have any role in the Home Loan Bank, that the taxpayer expenses are not, that the Federal Home Loan Banks do not get taxpayer support, right.

Sandra Thompson: You mean direct or implied?

Cornelius Hurley: Well, direct or, they don't say that. But would you agree that taxpayers are stakeholders in this process?

Sandra Thompson: Absolutely. The home loan banks are part of the financial sector and housing is a big part of that. And to the extent that there are ties to different entities in government that the home loan banks, you know, enjoy, certainly the debt that's issued has the implied guarantee, far as I could tell, implied from the United States government. Far as I can tell, the home loan banks aren't paying taxes as far as I can tell, there are a number of benefits that one gets from, you know, that the home loan banks are getting. And so I don't necessarily believe that it is, I don't think that the statement is exactly accurate.

Cornelius Hurley: Yeah. Well, it's important because it leads to other things. If you, if you deny that there's taxpayer support for this system, then it, it leads you to pay salaries, executive compensation on a scale that's beyond what I assume that you make or any and when I worked in the government, I didn't make $3 million a year. And we're coming on, we're, we're on the eve of all of the 11 banks filing their 10-Ks, and there could be some startling numbers coming out of that. Do you have any views with regard to executive compensation?

Sandra Thompson: Well, I know that I do have views with regard to executive compensation, but my views will be articulated, you know, at the end of the review. But it is a topic that's come up from time to time at various roundtables and at FHFA, we don't have the statutory authority to set the pay or establish a pay ranges. But we do have the authority to deny, but we are limited in what we can and cannot do. And so I think, you know, this is a topic that's come up, it'll be interesting to get all of the input to see kind of what recommendations we'll be making, you know, going forward.

Cornelius Hurley: Yeah. How about with respect to diversity at the board level, at the executive level of the 11 banks, are they doing enough?

Sandra Thompson: Well, I think the board composition is designed by statute, and many of the members, board members are member banks. And just by the nature of some of the members, it is probably less diverse than it could or should be. I think that what has typically happened in the past is that the independent directors have served in that role in terms of, you know, diversity of experience and other diverse characteristics. And, you know, there's always room for improvement.

But I do think that, you know, we do diversity and inclusion exams of each of the home loan banks and also the regulate, Fannie and Freddie. And so we do have exam reports where we talk about not just board diversity, but supplier diversity. You know, when they issue bonds, are they including diverse investment banking firms in their underwriting syndicates? And at what level? So there's always opportunities to improve.

Cornelius Hurley: Yeah. Well, I can only speak from the Boston Bank's perspective, and obviously I don't speak for them anymore, but the board took it very seriously. But there are institutional barriers, as you point out there, the directors are elected by the members and a lot of the members are non-diverse. And so you run into a problem there.

Sandra Thompson: I would say that that's true in many entities in financial services sector.

Cornelius Hurley: Absolutely it is. Yeah, it's not unique. But in terms of your reviews, are there any levers that you think you can pull to urge them on further in that direction?

Sandra Thompson: Well, I think that this is an area that they want to do better. And when we talk about diversity, not only is it just, you know, race, gender diversity, but it's also diversity with some of the board members, and in their experiences like the home loan banks, I think they have a little over 60 CDFIs you know that are members. And so just getting experience because I know a lot of community banks participate or serve on the boards in tribal districts, I'll use that as an example. You know, do we have any representation in districts that have significant tribal communities?

And so when you think about diversity, like I'm thinking about it from a holistic perspective, you know, who's, who's in your communities, you know, how are you serving them, what are their needs, and are you developing plans and programs and services to serve the needs of all of the people in your community? And even if you take one state like Illinois, for example, I mean, the needs of Chicago are certainly different than the needs of Champlain or even here. The needs of Gary, West Virginia are different and the needs of Beckley, West Virginia. And so just trying to figure out how do you meet the needs of the communities that you're supposed to serve in a thoughtful way. And so that will require having people on the board that understand the issues in the different communities that are supposed to be served.

Cornelius Hurley: So let's move on to a less controversial topic. Thank you. Skin in the game. Skin in the game, also known as the prior lien or the super lien. Yeah. Underwriting at the banks is a matter really of order taking. If the, if the member bank or insurance company is rated one, two, three or four, they must pretty much put in orders for loans or advances. That's not really underwritten. Is there any for.

Sandra Thompson: One, two, three or.

Cornelius Hurley: Four? Well, four, it's a little shakier. But is there a need for for the super lien anymore?

Sandra Thompson: Absolutely. Well, first of all, let me say this again. This goes to the purpose. So part of the purpose for the home loan banks is to provide liquidity. And this is especially true for community banks. And who's going to lend without the super lien. What I would say, because I've been on both sides of that trade, because, you know, you know, it is just really important. Especially and I worked ten years and the resolutions and receivership part of that agency. So I really understand the super lien in a way that many people do not.

But I do think it's important, like who else is going to lend if it's not there, especially to community banks who really need those advances to, in some cases, to shore up their balance sheet. And they are doing lending, you know, in the communities. But outside of that, you know, I think there is room for better coordination and cooperation and collaboration with some of the primary federal regulators for troubled institutions, because just because the home loan banks have, you know, lost a penny for whatever, because they've got the collateral, I mean, the losses to the DIF, to the deposit insurance fund are very real, and it will end up in the premiums that bankers will have to pay to the DIF, which ends up costing borrowers.

So it's like a circular argument. And so we are part of this financial ecosystem. And because the loss doesn't take place in one part of the system, it definitely takes place in another. And I think we have a fiduciary responsibility to one raise the awareness, and two to try to mitigate those losses. And really, again, especially for an institution that's going into receivership, I think it's just critical that we have, you know, better dialogue with FDIC on those institutions.

Cornelius Hurley: Yeah. And it, it raises the issue of market discipline, when does market discipline come into play versus the super lien, for example, is there, is there any market discipline as long as the bank is making advances, knowing that the super lien is in place?

Sandra Thompson: Well, I would look at it from supervision. I mean, what are my supervisory expectations for the FHFA as it relates to the safety and soundness of the home loan bank system? Who are they making advances to? You know, what's the condition of the bank? And we certainly don't have firsthand access to the reports of examination, but we need to be working with the PF, the primary federal regulator on that because we certainly don't want to be the last stop between, you know, viability and receivership, and that's just not the role. And so from my perspective, you know, there are things that, you know, we can do to strengthen our supervision and better define our expectations.

Cornelius Hurley: So you called me out on the floor a little bit ago.

Sandra Thompson: I was just asking.

Cornelius Hurley: Good. Just. So let me, let me ask you a question. When does that dialogue begin? Is it at the floor level or, I don't want to, I don't want to tease any questions out of you or answers out of you.

Sandra Thompson: Don't you worry, you won't. You know the dialogue is ongoing. And it got straight, it gets strengthened during times of crisis. Like certainly during the Great Recession, there was a dialogue between home loan banks and FDIC and the primary federal regulators. And even with this, with during the pandemic, certainly there's conversations that are ongoing and regulators do talk to one another. And I just think that when we're talking about troubled institutions, judgment comes into play. And that's the role of a supervisor, too. And we've got really good supervisors at both organizations. And I do think that those conversations, you know, really need to be had.

Cornelius Hurley: So we've, we've had terrific conversations today about affordable housing and housing in general. As Dennis Shea pointed out, quite rightly, it's a supply issue as well as an affordability issue. And, and Lisa Rice pointed out, which we don't, she didn't really need to we all know about it is the is the racial gap in homeownership. Do you see the FHL banks as at a process as contributing to close, closing that gap at all?

Sandra Thompson: Well, I think serving underserved communities, which include, you know, minority communities, rural communities, where there's a lack of financial services in the tribal communities that I mentioned earlier, I think it's a big part of that, when you think about what are the products and services that the home loan banks offer that can be helpful in those areas in a responsible way. What, are the members aware of all of the products and services that are offered? Are there pilot programs that the Home Loan Bank can undertake with some of their members to really try to address some of the liquidity needs in minority areas or rural areas or other underserved areas?

So I do think, you know, housing is a big part of the average person's balance sheet is like their largest asset. And there, there was a lot of wealth that was lost during the Great Recession, primarily by Black and brown households. And to the extent that there are programs that can provide sustainable loans to underserved communities, I think that, you know, that is something that we should absolutely explore. I really do want to be clear because one of the lessons learned from the crisis, you know, resulted in, you know, the ability to repay rule. People may like it or not, but, you know, the bad behaviors and practices that took place in 2000, you know, six, seven, eight, where people were getting loans they didn't understand, loans they couldn't afford.

What's the point of putting somebody into a house and then they've got to leave the house? You know, it's completely disruptive. So when I talk about affordability and access, it's with a sustainability from a sustainability perspective. Like one of the things that, you know, I've been thinking about like when people, you can pay your mortgage but you get into trouble, is there such a thing as a sustainability fund or is there such a thing as just trying to figure out, you know, are there better loss mitigation tools that can be useful, you know, for some of these member banks to take into consideration when these issues come up. But I do think that they have a role in providing, you know, liquidity to everybody in the community. As long as is sustainable.

Cornelius Hurley: I'm sure that will be reflected in your final report and recommendations. We're running out of time. And I just want to ask you, is there anything that I didn't ask you about that you want to unburden yourself with here today?

Sandra Thompson: I think I've unburdened myself plenty. I do want to reiterate that, you know, the home loan banks do play a critical role in the housing finance sector, in particular for community banks and I, that cannot be understated, and I've seen it firsthand as a person who had to take, my division had to take all of the failing bank cases up to the board during the crisis. And when I was there was like 305 over the, you know, 2008 through, you know, when I left. And that's a lot.

Now, you think about the institutions that are no longer there and why they're no longer there is there are things that the Home Loan Bank can do to really be helpful with the liquidity perspective in a responsible, safe and sound way that I think that, that really doesn't need to be forgotten. And so what they're doing for community banks is they're doing it well. And I don't think, there are some improvements that could be made. But again, you know, the status quo is not acceptable. And we are really looking to try to suggest or make some meaningful recommendations to improve the system and to improve the sector.

Cornelius Hurley: Excellent. I forgot to mention that I've been in touch with Brooksley Born just in the last few days, and she sends not only her regards, but her encouragement for you to do the very things that you're talking about doing today. And for all I know, Brooksley could be watching today, and, and I hope she is.

I'd like to bring this fireside chat to a close by quoting Senator Robert Kennedy. This is at the time of apartheid, so it's 1966. And and he gave his or what has been known as his Ripple of Hope speech. But I think it's totally appropriate for our circumstances here. And he quoted an Italian philosopher as saying, “there is nothing more difficult to take in hand or perilous to conduct than to or more uncertain in its success than to take lead in the introduction of a new order of things.”

And he went on to say, “there are perils along the road in that endeavor, and the most important peril is timidity.” And I know there are people in our industry, in the banking industry, that want you to be timid, but that's not the path that you, you have hewn for this project. And in that regard, I and I think everyone in this room encourages encourages you on. Congratulations.

Harrison Fregeau: I'm glad we actually had some applause for that. It was a good way of wrapping this up. So I get to conclude with some closing remarks. It's the virtue of being the first drafter of the schedule, as it turned out. I'm not going to speak too long. Just keep it relatively brief, a lot of it's thank you's. The first thank you goes to the weather, any time that you schedule a event in February, the fear is that it's going to be the 30 degrees and snowing DC and not be 60 degrees and sunny D.C. that we got and everybody showed up just fine. So thank you to all of you in the room, thanks to the 50 or so of you who arrived here today. Thank you also to the thousand people who watched online, that was a number that I certainly didn't fathom when I started this process. And I hope it's a sign of the interest that this event generates and that it can continue to generate as we progress through the FHFAs reform mission here.

I'd like to thank Brookings particularly by name Aaron Klein and Megan Waring. So along with his incisive commentary earlier, Aaron was instrumental in helping contact, identify people to join us. And I know without Megan, my job would have been ten times harder here just because all of the issues in setting up a symposium like this the logistics are always challenging, and she did a really masterful job. I'd really like to thank Corn Hurley, who was instrumental both in the inspiration for having this topic in the first place. You know, getting to chat with him, allowing me to write a proposal to BU, who I thank as well both for choosing this as the topic they elected to sponsor and then for financing and supporting this process throughout.

Lastly, I'd like to thank the speakers, you know, because ultimately if they don't come to this, there's no content for people to listen to. So we've got to invert that relationship. I really appreciated throughout the process how readily people came to join. You know, it was an instance where when I started this process, I couldn't say I was sure how quickly people would jump at this. And I was very pleasantly surprised that, you know, people really were eager to talk about this topic. And that's something I'm very grateful for, not just for the logistical aspects, but just as a sign that the project that we're undertaking here is worth doing.

There was a little bit of an elephant in that process, I didn't want to go without, you know, we, we did our best here to be as inclusive, inclusive as possible from all these different angles. And we, we tried our best to get a Federal Home Loan Bank representative directly on here. And unfortunately, the, the three that we contacted were unavailable and they were not able to send a representative today. So definitely wanted to just mention that. No matter what you think about the current FHLB system or about the reform process, I hope that this was an event that was meaningful to you, that can inspire you to continue what you were doing or to strive for something new in this whole process.

It's meant to be a starting point here. You know, if, if everything here ended with the symposium, then we wouldn't have accomplished our job. And I hope all of you continue to pursue your interests and your passion within this topic. We were fortunate enough to have the 100-year review announced by Professor or Director Thompson, and ultimately 100 years only comes around every once in 100 years. So we don't want to fail to take advantage of that opportunity. So I hope everybody who's interested in this topic takes advantage of the unique opportunity before us and wishing you all the best. And I'll conclude our program for today. Thank you so much.