January 9, 2015

Alfred M. Pollard, Esq., General Counsel

Attention: Comments/RIN 2590-AA39

Federal Housing Finance Agency

400 Seventh Street SW, Eighth Floor

Washington, D.C. 20024

**Re: Notice of Proposed Rulemaking; Request for Comments – Members of the Federal Home Loan Banks**

Dear Mr. Pollard:

​On behalf of Prospect Federal Savings Bank, a Member of the Federal Home Loan Bank of Chicago, this comment letter is submitted to express objection to the Federal Housing Finance Agency’s (“FHFA”) notice of proposed rulemaking and request for comments on “Members of the Federal Home Loan Banks” published on September 12, 2014. As outlined below, we respectfully request the withdrawal of this proposal.

Prospect Federal Savings Bank is a mutual savings bank, founded in 1909 and originally in the “Back of the Yards” area of the City of Chicago. We remain a community bank, with three locations in the Chicagoland area, and approximately $250 million in assets. Quite pertinent is that as a thrift, we have been members of the Federal Home Loan Bank of Chicago for 80+ years, going back to the inception of the FHLB System.

As a long-time shareholder, customer and Member we greatly value our relationship with the FHLB of Chicago. The FHLB-Chicago is a key partner to help us better serve our customers and our communities. For a smaller thrift such as ours, access to FHLB of Chicago advances is critically important. The FHLB’s products such as advances and the Mortgage Partnership Finance® Program are tremendous resources that enable us to effectively compete with much larger financial institutions and to serve our customers.

The proposed rule concerns us because it would impose, for the first time ever, on-going requirements for our bank to meet as a condition of remaining a member of the FHLB of Chicago. For an institution such as ours, the proposal would require us to hold between 1% to 5% of our total assets in long-term home mortgage loans. Failure to maintain this level would eventually result in the termination of our membership in the FHLB of Chicago.

While this requirement may not appear to the FHFA to be onerous, the practical consequences would be very severe and disruptive. Moreover, we have often observed instances where percentages, which initially appear easy to meet, are steadily adjusted upward. Philosophically, experience tells us to express this concern, which will be expanded upon later in this comment letter.

Prospect Federal’s ability to rely on the liquidity provided by the FHLB of Chicago, particularly in times of economic distress, could be seriously undermined if the FHFA is allowed to establish requirements we must meet to remain an FHLB of Chicago member. This has never been the case in the 82-year history of the FHLBs. Membership in the FHLBs has been steadily expanded by Congress over the years, never contracted. With the imposition of such a requirement, we could never be assured that when the next financial crisis occurs we, or other colleagues, would have continued access to FHLB of Chicago liquidity.

We are concerned this proposal could lead to additional restrictions upon FHLB membership. If the FHFA can require ongoing eligibility requirements for members, nothing would prevent it from increasing those thresholds, or imposing entirely new requirements, in the future. This proposal might simply be the first of many such eligibility requirements imposed upon FHLB members, purportedly in an effort to ensure that a sufficient housing finance nexus is maintained at all times by members. Such fears are not unfounded. Past Administrations from both political parties increased housing goals for Fannie Mae and Freddie Mac in an effort to increase the level of homeownership and serve politically favored constituencies, with disastrous results.

A similar concern exists as to the ability to terminate the memberships of current FHLB members without any showing of cause. Under the proposal, the current memberships of captive insurance companies would be terminated, regardless of the amount of home mortgage loans they hold on their balance sheets. This would occur despite the fact that captives are insurance companies, which have been eligible to be FHLB members since the FHLBs were created by Congress in 1932. If the FHFA can terminate the memberships of a certain class of insurance companies, it raises a legitimate concern as to what, if anything, would prevent the FHFA in the future from terminating the memberships of other types of current members, potentially including our bank, for any reason the FHFA sees fit. Such an outcome would destroy any confidence in the FHLBs as sources of stable and reliable liquidity. The entire financial industry, especially banking and insurance, are reliant upon confidence. We need the strength and stability in banking and insurance. The FHLB System is properly serving both industries as a partner.

The proposal seems to restrict and narrow FHLB membership, resulting in fewer members. As some members have their memberships terminated, and others are forced to reduce their usage of the FHLB of Chicago, we are concerned about the destabilizing effects that would result. These actions will inevitably lead to smaller FHLBs with fewer assets, reduced profits, lower retained earnings, and a decreased market value of equity and capital stock. Additionally, as usage contracts and profits decline, fewer dollars will be available to support the FHLB of Chicago’s affordable housing and community investment programs. Our bank’s ability to serve our communities through valuable products such the FHLB’s down payment assistance grants and Affordable Housing Program grants would be harmed.

Beyond these destabilizing effects, this proposal does nothing to help strengthen the overall financial system. Since the financial crisis, our prudential regulators, the Office of the Comptroller of the Currency (OCC), has increasingly emphasized liquidity planning. In our liquidity plans, we rely on our access to the same-day funding offered by the FHLB of Chicago. Our regulator understands and accepts the vital role of the FHLB-Chicago in our planning. This proposal contradicts these efforts by undermining the reliance of banks such as ours on the FHLBs. In so doing, it threatens to weaken the broader financial system while doing nothing to help prevent a repeat of the financial crisis.

The proposal appears counterproductive. It would hamper the effort to help restart the struggling housing market. Many community banks rely upon the FHLBs’ MPF® Program to access the secondary mortgage market. This innovative program has been popular with FHLB members, particularly smaller community banks, because it allows us to access the secondary mortgage market on competitive terms while retaining our customer relationships. The traditional MPF products also pay participating members monthly fees to manage the credit risk of their own loans, in contrast to the guarantee fees charged by Fannie Mae and Freddie Mac. Rather than furthering this program, however, the proposal would only harm it by encouraging members to hold more mortgage loans on their balance sheets, rather than selling them. If long-term mortgages are held by members, interest rate risk (IRR) will be increased. As a long-time thrift, we are all-too-conversant in living through a cycle where IRR was not merely a theoretical issue, but a very real problem. Many of our brethren succumbed during that period of time.

Furthermore, to the extent the proposal discourages FHLB membership or terminates existing memberships, access to housing finance would be constricted. Again, this seems to directly contradict the efforts of the Administration and others to increase the availability of mortgage credit, particularly for lower income families.

This proposed rule further harms the financial system by adding to the growing regulatory burden on small banks which impedes our ability to efficiently operate our businesses and best serve our customers. Community banks across the country are struggling under the weight of an extensive regulatory burden, despite the fact that we were not the cause of the recent financial crisis.

The FHLB of Chicago as an essential partner for our bank. Its reliability as a liquidity source must be preserved. Threatening access to the FHLB of Chicago threatens our bank, our customers, our colleagues and the communities in Chicagoland which we serve. This proposal would undermine the reliability of the FHLB of Chicago, discourage membership, potentially politicize FHLB membership, limit access to the secondary market and shrink the FHLB of Chicago’s affordable housing and community development activities. It will hamper the effort of other banking regulators to strengthen the overall financial system. Despite these damaging effects, there appear to be no specific benefits that would be achieved by this proposal. For these reasons, we request the immediate withdrawal of this proposal.

Your consideration of this comment letter is appreciated.

​ Cordially,

Steven F. Rosenbaum

Chairman & CEO

Prospect Federal Savings Bank

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