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FEDERAL HOUSING FINANCE AGENCY

12 CFR Part 1263

RIN 2590-AA85

Federal Home Loan Bank Membership for Non-Federally-Insured Credit Unions

AGENCY: Federal Housing Finance Agency.

ACTION: Final rule.

SUMMARY: The Federal Housing Finance Agency (FHFA or Agency) is adopting a final rule revising its regulation governing Federal Home Loan Bank (Bank) membership to implement section 82001 of the Fixing America's Surface Transportation Act (FAST Act), which amended the Federal Home Loan Bank Act (Bank Act) to authorize certain credit unions without Federal share insurance to become Bank members. The rule also makes appropriate conforming changes to FHFA's regulation on Bank membership. The final rule is substantially the same as the proposed rule, but includes one revision intended to streamline the application process for credit unions applying for Bank membership pursuant to the FAST Act provision.

DATES: Effective Date: [INSERT DATE 30 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER].

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SUPPLEMENTARY INFORMATION:

I. Background

Under the Bank Act, federally insured depository institutions, including state- and federally chartered credit unions whose member accounts are insured by the National Credit Union Share Insurance Fund (NCUSIF), have been eligible for Bank membership since 1989. Until recently, however, state-chartered credit unions without Federal share insurance were ineligible for Bank membership, except to the limited extent that a credit union certified as a “community development financial institution” (CDFI) by the CDFI Fund of the United States Department of the Treasury could meet the eligibility requirements applicable to CDFIs.¹

In December 2015, Congress amended the Bank Act to authorize the Banks to approve applications for membership from state-chartered credit unions without Federal share insurance (irrespective of their CDFI status) where specified requirements have been met.² Specifically, new section 4(a)(5) of the Bank Act provides that a credit union lacking Federal share insurance that has applied to become a member of a Bank shall be treated as a federally insured depository institution for purposes of determining its

¹ In 2008, Congress amended the Bank Act to authorize entities certified as CDFIs by the CDFI Fund of the United States Department of the Treasury to become Bank members, provided the CDFI meets the membership eligibility requirements established for such entities. *See* Housing and Economic Recovery Act of 2008, Pub. L. No. 110-289, section 1206, 122 Stat. 2787 (2008), codified at 12 U.S.C. 1424(a)(1). By law, credit unions—including state-chartered credit unions without Federal share insurance—may be certified as CDFIs. *See* 12 U.S.C. 4701-4719; 12 CFR part 1805.

² *See* Fixing America’s Surface Transportation Act, Pub. L. No. 114-94, section 82001(a), 129 Stat. 1795 (2015), codified at 12 U.S.C. 1424(a)(5).

eligibility for Bank membership, so long as the applicant's state credit union regulator has determined that it met all of the requirements for Federal share insurance as of the date of its application for membership.³ The new statutory provision also provides, however, that if the applicant's state regulator has not made a determination as to whether it met the requirements for Federal share insurance within six months of the date of its application for Bank membership, then the applicant shall be deemed to have met those requirements.⁴ Section 4(a)(5) also provides that, notwithstanding any State law to the contrary, the right of Banks to repayment of advances made to credit unions admitted to membership pursuant to that provision and Banks' interests in collateral securing such advances are to have protections and priorities similar to those that apply to advances made to, and collateral pledged by, members that are federally insured depository institutions.⁵

B. The Proposed Rule

On September 28, 2016, FHFA published in the Federal Register a Notice of Proposed Rulemaking (proposed rule) to amend FHFA's regulation on Bank membership, located at 12 CFR part 1263, to implement section 4(a)(5) of the Bank Act.⁶ The proposed rule, which referred to state-chartered credit unions falling within the scope of the new statutory provision as "non-federally-insured credit unions" (NFICUs), proposed to add a new regulatory section governing the Banks' acceptance and processing of membership applications from NFICUs, as well as the treatment of existing

³ See 12 U.S.C. 1424(a)(5)(A), (B)(i). Although the statutory text actually refers several times to "Federal deposit insurance," FHFA construes those references to mean the Federal share insurance that is provided to credit unions by the NCUSIF, in light of the evident purpose for which Congress adopted the NFICU amendments.

⁴ See 12 U.S.C. 1424(a)(5)(B)(ii).

⁵ See 12 U.S.C. 1424(a)(5)(C), (D).

⁶ See 81 FR 66545 (Sept. 28, 2016).

credit union Bank members that choose to become NFICUs by canceling their federal share insurance. As proposed, the rule would have codified the core concepts of a set of April 2016 guidance letters in which FHFA advised each Bank on the handling of NFICU membership applications under section 4(a)(5). The proposed rule also would have provided additional clarification on certain points. The details of the proposed rule are discussed in the section-by-section analysis of the final rule below.

The 60-day comment period for the proposed rule ended on November 28, 2016. FHFA received eight comment letters from seven separate commenters, which included one Bank, one provider of private credit union share insurance, and five credit union trade associations.⁷ Six of the commenters expressed general support for the proposed rule and none of the commenters expressed general opposition to the rule. Each commenter, however, requested one or more specific revisions to the regulatory text. FHFA carefully considered all of the comments and ultimately decided to adopt one of the suggested revisions. The comments on specific aspects of the proposed rule, and FHFA's responses, are discussed in the section-by-section analysis below.

Three commenters raised an issue regarding the treatment of NFICU members by the Banks that was not addressed in the proposed rule, which focused exclusively on membership requirements for NFICUs. Those commenters expressed concerns that Banks currently may be imposing on NFICUs advances collateral requirements that are more stringent than those for federally insured depository institution members—for example, by requiring that NFICU members deliver collateral to the Bank or by imposing higher discounts on collateral after an existing member terminates its federal insurance—

⁷ The comment letters may be viewed at <https://www.fhfa.gov/SupervisionRegulation/Rules/Pages/Comment-List.aspx?RuleID=566>.

and asked that the final rule prohibit such practices.

FHFA declines to amend its regulations to address those practices, in part because the request goes beyond the scope of the proposed rule and thus cannot be addressed in the final rule. Moreover, while FHFA's collateral regulations implement statutory requirements and establish minimum standards necessary to ensure the safety and soundness of the Banks, those regulations otherwise permit each Bank to make its own decisions regarding the terms on which it will lend to its members, including the amounts and types of collateral it will accept from particular members, the discounts on such collateral, and whether a member must deliver collateral to the Bank. This long-standing regulatory approach recognizes that the Banks are in the best position to assess the credit risks posed by particular members or by particular types of members within their respective districts. In recent years, as more insurance companies have become members and CDFIs have become eligible for membership, FHFA has issued guidance recognizing that Banks may establish different collateral requirements for non-federally insured entities to address the risks posed by the lack of a federal receivership process for such institutions.⁸

Notwithstanding that section 4(a)(5) of the Bank Act provides that the Banks' security interests in NFICU collateral are to have some of the same protections and

⁸ See FHFA AB 2013-09 (Dec. 23, 2013) (providing guidance on credit risk management practices to ensure Bank advances remain fully secured when lending to insurance company members), available online at <https://www.fhfa.gov/SupervisionRegulation/AdvisoryBulletins/Pages/AB-2013-09-COLLATERALIZATION-OF-ADVANCES-AND-OTHER-CREDIT-PRODUCTS-TO-INSURANCE-COMPANY-MEMBERS.aspx>; FHFA AB 2013-10 (Dec. 23, 2013) (outlining the criteria that FHFA examiners use in determining whether a Bank's advances are, as required by regulation, "fully secured" pursuant to a written security agreement that gives the Bank a "perfectible" security interest), available online at <https://www.fhfa.gov/SupervisionRegulation/AdvisoryBulletins/Pages/AB-2013-10-COLLATERALIZATION-OF-ADVANCES-AND-OTHER-CREDIT-PRODUCTS;-PERFECTION-AND-CONTROL-OF-COLLATERAL.aspx>.

priorities that apply to interests in collateral pledged by federally insured depository institutions, a Bank might reasonably conclude that there remain additional risks inherent in lending to NFICUs, arising principally from the fact that the Banks have had no experience with the liquidation of a non-federally insured credit union. While the laws governing liquidation of federally insured credit unions are well known to the Banks and are uniform across the country, the Banks are less familiar with the laws governing the insolvency and liquidation of NFICUs, which will vary from state to state. Although the Banks have significant numbers of state-chartered credit union members, any that have failed to date would have been federally insured and, therefore, would have been liquidated by the National Credit Union Association (NCUA). If a Bank concludes that the characteristics of NFICUs give rise to incrementally greater risk that it should address through more stringent collateral requirements, then FHFA would not prevent it from imposing those requirements.

II. The Final Rule

An analysis of the primary revisions made by the final rule to FHFA's membership regulation appears below, followed by a discussion of the conforming revisions. Except as discussed below with respect to the timing of communications between an NFICU and its state credit union regulator during the membership application process, this final rule adopts without substantive change all of the regulatory additions and revisions set forth in the proposed rule. As described in more detail below, the final rule also makes a number of conforming revisions to other sections of the membership regulation, each of which appeared in identical form in the proposed rule.

A. Primary Revisions

The principal regulatory provisions regarding NFICUs include a new § 1263.19, setting forth the prerequisites that must be met in order for an NFICU to be treated as an insured depository institution for Bank membership purposes, as well as two substantive definitions located in § 1263.1.

1. Definitions of NFICU and Insured Depository Institution—§ 1263.1

The final rule adds to § 1263.1 a definition of “non-federally-insured credit union,” defining the term to mean a “State-chartered credit union that does not have Federal share insurance and that has not been certified as a CDFI by the CDFI Fund.” In conjunction with this, the rule also revises the definition of “insured depository institution” to include, in addition to federally insured depository institutions, NFICUs meeting the prerequisites of § 1263.19. As an “insured depository institution” under the revised regulation, a qualifying NFICU applying for Bank membership is subject to all of the eligibility requirements and other provisions of the membership regulation that apply to insured depository institutions generally, except where otherwise provided. Thus, a qualifying NFICU applicant is eligible for membership only if: it is duly organized under Federal or state law; it is subject to inspection and regulation under Federal or state banking laws, or similar laws; it makes long-term home mortgage loans; its financial condition is such that advances may be safely made to it (hereinafter the “financial condition” requirement); its management and its home financing policy are both consistent with sound and economical home financing; and it has at least 10 percent of its assets in “residential mortgage loans.”⁹ With the exception of the financial condition

⁹ See 12 CFR 1263.6(a), (b). The Bank Act exempts certain smaller depository institutions—“community financial institutions” (CFIs)—from the “10 percent” requirement, but defines CFI to include only institutions the deposits of which are insured under the Federal Deposit Insurance Act (FDIA) that have

requirement, an NFICU applicant must demonstrate compliance with each of those membership eligibility requirements in the same manner that is required of insured depository institutions generally. As discussed below, the final rule requires an NFICU applicant to demonstrate compliance with the financial condition requirement in the same manner as a CDFI credit union.

2. Prerequisites For an NFICU To Be Treated As an Insured Depository Institution—§ 1263.19

As proposed, the final rule adds to the membership regulation a new § 1263.19 (a reserved section under the existing regulation), which sets forth the prerequisites that an NFICU must meet in order to be treated as an insured depository institution for purposes of determining its eligibility for Bank membership. Paragraph (a) of new § 1263.19 addresses the treatment of NFICUs that apply for Bank membership, while paragraph (b) addresses the status of any credit union that is already a Bank member at the time it opts to become an NFICU by canceling its Federal share insurance.

a. Treatment of an NFICU Applying For Bank Membership—§ 1263.19(a)

In parallel with the inclusion of qualifying NFICUs within the regulatory definition of “insured depository institution,” new § 1263.19(a) provides that an NFICU applicant shall be treated as an insured depository institution for purposes of determining its eligibility for membership, provided that it complies with all of the requirements of § 1263.19(a)(1) through (3).

As proposed, these provisions would have required that a Bank first obtain from

total assets below a certain threshold amount. See 12 U.S.C. 1422(10)(A)(i), 1424(a)(4). Because a credit union cannot obtain deposit insurance under the FDIA, it cannot qualify as a CFI regardless of its level of total assets.

an NFICU applicant all of the information that the Bank generally requires to process membership applications from federally insured depository institutions, including all of the information needed to demonstrate compliance with the general eligibility requirements for Bank membership. Once in receipt of all of those materials, the Bank would have been required to notify the NFICU that its application is “provisionally complete” and that, before the Bank may act on the application, the NFICU must: (1) request from its state regulator a determination that the institution met all eligibility requirements for Federal share insurance, as of the date of the request; and (2) subsequently, provide to the Bank acceptable documentation of the regulator’s response or lack of response to its request. The proposed rule would also have expressly required the NFICU applicant to submit such a request, in writing, to its state regulator and simultaneously provide a copy of the request to the Bank. The rule would have permitted a Bank to deem an NFICU’s application fully complete, and to act on the application as provided in § 1263.3(c),¹⁰ after having received from the applicant any one of the following items: (1) a written statement from the state regulator confirming that the NFICU satisfied all of the eligibility requirements for Federal share insurance as of the date of the request; (2) a written statement from the state regulator that it is unable or unwilling to make a determination as to the NFICU’s eligibility for Federal share insurance; or (3) a written statement from the NFICU certifying that it did not receive a response from its state regulator within the six-month waiting period provided for in the statute.

¹⁰ Existing § 1263.3(c) requires that a Bank notify an applicant when it deems the application to be complete and (with certain exceptions) either approve or deny the application within 60 calendar days of the date it made that determination. See 12 CFR 1263.3(c).

FHFA received comments on both the required timing of an NFICU's request for a determination from its state regulator and the type of documentation of that determination a Bank must receive to deem an NFICU's application complete under proposed § 1263.19(a). On the timing issue, several commenters requested that the final rule permit an NFICU applicant to request the determination from its state regulator at any time after initiating the membership application process, instead of waiting until the Bank has deemed the application provisionally complete, as would have been required under the proposed rule. Those commenters expressed a belief that most NFICUs would be inclined to request the determination early in the application process to enable the Bank to make a decision on the membership application at the earliest possible time.

With regard to timing requirements for the NFICU application process, the Bank Act uses the undefined term "date of the application" in establishing both the point in time as of which the state regulator must determine the NFICU's eligibility for Federal share insurance and the starting point of the six-month period during which the Bank and NFICU must await action by the state regulator. Specifically, section 4(a)(5) requires a Bank to treat an NFICU applicant as a federally insured depository institution if the NFICU's state credit union regulator either: (1) has determined that the NFICU met all the eligibility requirements for Federal share insurance "as of the date of the application for membership"; or (2) has failed to make a determination "by the end of the 6-month period beginning on the date of the application." In its April 2016 guidance letters to the Banks, FHFA construed the statutory term "date of the application" to be the date as of which the NFICU had submitted a "provisionally complete" application—that is, an application including all information and supporting materials required for the Bank to

act on it, except for the documentation regarding the state regulator's determination. Although the proposed rule did not use the term "date of the application," the proposed requirement that an NFICU wait until after the Bank has deemed its application provisionally complete to submit the request to its state regulator is based on the construction of that term adopted in the guidance letters.

The proposed rule would have required the state regulator's eligibility determination to have been made as of the date of the NFICU's request and would have measured the six-month waiting period from the date of the request. Section 4(a)(5) of the Bank Act does not expressly require that either a Bank or an NFICU applicant request a determination from the NFICU's state regulator. But, in that the statute allows a state regulator six months within which to make a determination if it wishes to do so, it is most reasonably read as presuming that the regulator has in the first instance been asked to make a determination. The proposed rule's use of the date of the NFICU's request for a determination, instead of the date the Bank notified the NFICU that its application is provisionally complete, to set both the date as of which the regulator's determination should be made and the starting date of the six-month waiting period reflected this reading of the statute.

Given the ambiguity of the statute on the issue, FHFA may reasonably construe the "date of the application" to be a point in the application process that is earlier than the date on which the Bank deems an NFICU's application to be provisionally complete, as requested by some commenters. FHFA had two principal reasons for proposing to require that an NFICU submit a provisionally complete application prior to officially requesting a determination from its state regulator. The first was to provide some

reasonable assurance that an NFICU applicant actually was committed to completing the application process prior to requiring it to submit a request to its state regulator. The second was that the concept of a “complete” membership application and the requirement that a Bank notify an applicant after deeming its application complete are already well established under the existing membership regulation.¹¹

FHFA is persuaded, however, that allowing an NFICU to request a determination at an earlier stage in the membership application process would result in a more efficient process than would the approach of the proposed rule. Accordingly, FHFA has revised the final rule to permit an NFICU applicant to submit its official request for a determination to its state regulator at any time after it has submitted its application to the Bank to initiate the membership application process. As under the proposed rule, the six-month waiting period will start on, and the state regulator must make the Federal share insurance eligibility determination as of, the date that the applicant submits the request to its state regulator. Specifically, § 1263.19(a)(1) of the final rule requires that, after an NFICU initiates the membership application process, the Bank promptly notify the applicant in writing that its application will not be deemed complete or be acted upon by the Bank until the applicant has, in addition to satisfying all other application requirements, requested a determination from its state regulator as required under paragraph (a)(2) and subsequently provided one of the types of acceptable documentation listed in paragraph (a)(3). Section 1263.19(a)(2) and (3) of the final rule are substantively unchanged from the proposed provisions.

As does the final provision, proposed § 1263.19(a)(3) would have required a Bank

¹¹ See 12 CFR 1263.3(c).

to deem an NFICU's application complete after having received any one of three types of documentation regarding the response or lack of response of the applicant's state regulator to its request for a Federal share insurance eligibility determination. As noted above, one of those types of documentation is a written statement from the regulator to the NFICU applicant that the regulator is unable or unwilling to make such a determination. One commenter requested that the final rule also include a fourth option under which a Bank could deem an application fully complete if the applicant's state regulator had previously provided direct written notification to the Bank that it would not make federal share insurance eligibility determinations for any of its NFICU regulatees. In advocating the suggested revision, the commenter reasoned that permitting a Bank to accept such a statement of general policy from a state regulator would relieve the regulator of "unnecessary administrative burdens" because the regulator then would not be required to address each individual NFICU request with the same response. The commenter also asserted that including such an option would streamline the application process for both the Bank and the NFICU in that, once the applicant had made the required request to its state regulator, the Bank could rely on the prior direct communication from the regulator to conclude that no individual response would be forthcoming and could act upon the application immediately.

For three principal reasons, FHFA has decided not to provide for the recommended option in the final rule. First, doing so would further complicate what is already somewhat complicated regulatory text.¹² Second, reliance on statements of

¹² Because FHFA received no information from any state regulators on this issue, it is possible, and perhaps likely, that some regulators will decline to provide such blanket statements to the Banks, rather than responding to the requests of their own regulated institutions. For that reason, the final rule would still

general policy received directly from a state regulator leaves open the possibility that the regulator's policy regarding these Federal share insurance eligibility determinations may change over time (such as when a successor regulator assumes office) without the knowledge of the Bank. Third, reliance on such general statements would foreclose the possibility that a state regulator, despite having a general policy against making such determinations, could in appropriate circumstances choose to convey to a Bank information about a particular institution that is relevant to its eligibility for Federal share insurance or its eligibility for Bank membership. While FHFA could include caveats in the final rule to address each of those drawbacks, any benefits to doing so are apt to be modest and would result in further complicating the regulatory text. Retaining the language of the proposed rule will also ensure that, in each case, the state regulator is aware that its regulatee is applying for Bank membership and that it has an opportunity to make a determination if it wishes to do so.

In addition, FHFA does not believe that adopting this recommendation would reduce the burden on the state regulators to any meaningful degree. The only burden that the proposed rule would have imposed on the state regulator in this respect is to provide individual responses to requests received from its credit unions, which could be easily accomplished by means of a form letter.

b. Treatment of a Credit Union That Becomes an NFICU When Already a

Member—§ 1263.19(b)

Mirroring the proposed rule, final § 1263.19(b) makes clear that an existing credit

have to include the proposed provisions requiring each NFICU to request such a determination and further requiring each Bank to await receipt of one of the three acceptable types of documentation before proceeding.

union Bank member that cancels its Federal share insurance may remain a member of its Bank as an NFICU without requesting a Federal share insurance eligibility determination from its state regulator, provided the Bank determines that the member has canceled its Federal share insurance voluntarily. A Bank could make this determination by obtaining a copy of the NCUA's approval of the credit union's request to terminate its Federal insurance.¹³ After becoming an NFICU, the credit union would remain subject to all regulatory provisions that apply to Bank members that are insured depository institutions.

Two commenters took issue with the use of the word "cancel" in proposed § 1263.19(b), as well as with the use of the word "terminate" in the proposed rule preamble, in describing the process a federally insured credit union would undertake in becoming an NFICU. Those commenters requested that the final rule instead describe the process as "converting" from Federal share insurance to private share insurance.

As the commenters noted, under the regulations of the NCUA, the word "convert" refers to "the act of canceling federal insurance and simultaneously obtaining insurance from another insurance carrier," while the word "terminate" refers to "the act of canceling federal insurance and mean[s] that the credit union will become uninsured."¹⁴ In advocating for the use of the word "convert" in referring to existing Bank members that become NFICUs, the commenters asserted that any existing member that cancels its Federal share insurance will simultaneously obtain private share insurance, rather than simply becoming uninsured. As a practical matter, that is likely to be true given that there appears to be no state that allows its credit unions to operate without either federal

¹³ A state-chartered credit union may terminate its Federal share insurance or convert to a non-federal form of insurance only with the prior written approval of the NCUA. See 12 CFR 708b.201(d), (e), 708b.203(d).

¹⁴ See 12 CFR 708b.2.

or private share insurance.¹⁵

As a legal matter, however, section 4(a)(5) of the Bank Act does not require a credit union to have private share insurance to become a Bank member through the NFICU process. The statutory provision refers to “credit union[s] which lack[] Federal deposit insurance” and does not require coverage by private, or other non-federal, share insurance as a prerequisite to qualifying for treatment as a federally insured depository institution for Bank membership purposes.¹⁶ In recognition of this fact, the final rule defines “non-federally-insured credit union” in terms of “a State-chartered credit union that does not have Federal share insurance” and does not otherwise require an NFICU to be covered by any type of non-federal share insurance in order to be treated as a federally insured depository institution.¹⁷

If FHFA were to accept the commenters’ suggestion and revise the rule to refer to members that have “converted,” the rule would then appear to impose upon existing members a private share insurance requirement that is not imposed by the statute. As indicated in the definitions quoted above, the NCUA’s regulations use the undefined word “cancel” to refer generically to the relinquishing of federal share insurance coverage without connoting either the existence or lack of an alternative form of share insurance. Accordingly, the final rule continues to describe members that become NFICUs as those that voluntarily “cancel” their federal share insurance.

¹⁵ The laws of some states allow for use of a state insurance fund by their state-chartered credit unions, but there are no longer any such state funds that provide primary share insurance.

¹⁶ Although the provision is entitled “Certain Privately Insured Credit Unions,” the statutory text contains no reference to privately insured credit unions and does not include coverage by private, or other non-federal, share insurance among the prerequisites that must be met.

¹⁷ The use of the term “non-federally-insured credit union” in FHFA’s rule differs from its use in the NCUA’s regulations. FHFA’s rule defines the term to mean a credit union without Federal share insurance, while NCUA regulations define the term to mean a credit union covered by a non-federal form of share insurance. See 12 CFR 708b.2.

B. Conforming Amendments

In addition to the primary revisions, the final rule makes a number of conforming revisions to part 1263.

1. Definitions—§ 1263.1

In addition to the substantive amendments to § 1263.1 that are discussed above, the final rule makes several amendments to that section that are intended merely to provide greater clarity, without effecting any substantive change. The final rule adds a definition for the term “Federal share insurance” that is identical to the definition appearing in the proposed rule and adopts verbatim the proposed revisions to the definitions of “CDFI credit union,” “community development financial institution or CDFI,” and “regulatory financial report.”

2. Membership Application Requirements—§ 1263.2

The final rule adopts without change the two revisions to § 1263.2 of the existing regulation that appeared in the proposed rule. The final rule revises § 1263.2(b), which requires a Bank to prepare a written membership application digest for each applicant, to expressly require a Bank to include in the application digest for each NFICU applicant a summary of the manner in which the applicant has complied with the requirements of § 1263.19(a). The final rule also revises § 1263.2(c), which requires a Bank to maintain a membership file for each applicant, to make clear that a Bank should include in the file for an NFICU applicant any documents required under § 1263.19.

3. Compliance With the Financial Condition Requirement—§ 1263.11

Existing § 1263.11 governs the manner in which Banks are to determine whether depository institution applicants, including insured depository institutions and CDFI

credit unions, are in compliance with the statutory “financial condition” eligibility requirement. As proposed, the final rule revises § 1263.11 to require a Bank to assess an NFICU applicant’s compliance with the “financial condition” membership eligibility requirement in the same manner as is required for CDFI credit unions.

The existing provision allows a Bank to deem a depository institution applicant in compliance with the financial condition requirement if: (1) the applicant has received a composite examination rating within the past two years; (2) it meets its regulatory capital requirements; and (3) its most recent composite examination rating was “1,” or the most recent rating was “2” or “3” and the applicant satisfies certain “performance trend criteria” pertaining to its earnings, nonperforming assets, and allowance for loan and lease losses.¹⁸ Although the regulation generally exempts federally insured depository institutions with a “1” exam rating from compliance with the performance trend criteria, FHFA did not extend that exemption to “1” rated CDFI credit unions (which, like NFICUs, are state-chartered credit unions without federal share insurance) in 2010, when it amended the regulation to accommodate CDFIs as members.

As the final rule does, the proposed rule would have revised § 1263.11 to treat NFICUs in the same way as CDFI credit unions by requiring all NFICU applicants, including those that had received a composite examination rating of “1” from their state regulators, also to satisfy the performance trend criteria. The rationale behind this approach is that both CDFI credit unions and NFICUs are state-chartered credit unions without federal share insurance, which warrants treating them in the same way for purposes of assessing their financial condition. Six commenters requested that the final

¹⁸ 12 CFR 1261.11(b)(3).

rule treat NFICU applicants in the same manner as federally insured credit unions by exempting NFICUs with an examination rating of “1” from complying with the performance trend criteria. FHFA has declined to make that change.

When FHFA amended the membership regulation to accommodate CDFIs as members, it described its decision to require even “1” rated CDFI credit unions to satisfy the performance trend criteria as a prudential measure.¹⁹ The Agency noted that, because such institutions are not subject to oversight by the NCUA and because they had not previously been eligible for membership, the Banks were likely to be less familiar with the state examination processes and ratings systems to which they are subject than with those that apply to federally insured depository institutions. To the best of the Agency’s knowledge, no CDFI credit union has been admitted to Bank membership to date.²⁰ Accordingly, the prudential concerns arising from the Banks’ relative lack of familiarity with the regulatory regimes that apply to credit unions that are supervised only at the state level and that would be liquidated by a private insurance company continue to exist and logically should apply with equal validity to both CDFI credit unions and NFICUs.

Given the Banks’ scant experience with state-chartered credit unions that do not have federal share insurance, it remains prudent to require all such applicants—that is, both CDFI credit unions and NFICUs—to meet the performance trend criteria as part of satisfying the “financial condition” eligibility requirement. Moreover, assessing compliance with the performance trend criteria is a relatively straightforward exercise,

¹⁹ See 75 FR 678, 684-85 (Jan. 5, 2010)

²⁰ The Bank membership regulation effectively treats federally insured credit unions certified as CDFIs as insured depository institutions for Bank membership purposes, while subjecting a “CDFI credit union” (defined to refer only to a CDFI that is a state-chartered credit union without Federal share insurance) to the same standards that apply to non-depository CDFIs, with the exception of those that must be met in order for an applicant to be deemed in compliance with the financial condition eligibility requirement.

requiring only that a Bank confirm that an applicant has positive net income and that its nonperforming assets and its allowance for loan and lease losses meet certain specified ratios. As the Banks gain more experience with admitting these types of members, FHFA could reconsider this requirement.

4. Reports and Examinations—§ 1263.31

Existing § 1263.31 sets forth a number of stipulations to which each Bank member is deemed to have agreed as a condition precedent to becoming a Bank member. The final rule adopts without change the revisions to paragraphs (b) and (e) of that section that appeared in the proposed rule. Existing § 1263.31(b) deems each Bank member to have agreed that the appropriate local, state, or Federal agencies or institutions may furnish the member's reports of examination to the Bank or to FHFA upon request. The final rule revises that provision to stipulate that each member that is an NFICU or a CDFI credit union is also deemed to have agreed that a private entity providing the member with share insurance may furnish such reports. Existing § 1263.31(e) deems each Bank member to have agreed to provide the Bank, within 20 days of filing, with copies of reports of condition and operations filed with its appropriate Federal banking agency. The final rule revises that provision to stipulate that each member is also deemed to have agreed to furnish copies of any reports of condition and operations it may be required to file with its appropriate state regulator and that each NFICU or CDFI credit union member is deemed to have agreed to provide copies of any such reports required to be filed with a private entity providing it with share insurance.

III. Consideration of Differences Between the Banks and the Enterprises

Section 1313(f) of the Safety and Soundness Act requires the Director of FHFA, when promulgating regulations relating to the Banks, to consider the differences between the Banks and the Enterprises (Fannie Mae and Freddie Mac) as they relate to: the Banks' cooperative ownership structure; the mission of providing liquidity to members; the affordable housing and community development mission; their capital structure; and their joint and several liability on consolidated obligations.²¹ The Director also may consider any other differences that are deemed appropriate. In preparing this final rule, the Director considered the differences between the Banks and the Enterprises as they relate to the above factors, and determined that the rule is appropriate.

IV. Paperwork Reduction Act

The Paperwork Reduction Act of 1995 (PRA) requires that FHFA consider the impact of paperwork and other information collection burdens imposed on the public.²² Under the PRA and the implementing regulations of the Office of Management and Budget (OMB), an agency may not collect or sponsor the collection of information, nor may it impose an information collection requirement unless it displays a currently valid control number assigned by OMB.²³ FHFA's regulation "Members of the Federal Home Loan Banks," located at 12 CFR part 1263, contains several collections of information that OMB has approved under control number 2590-0003, which expires on March 31, 2020. The final rule does not make any revisions that affect the burden estimates for those collections of information. Therefore, FHFA has not submitted any materials to OMB for review.

²¹ 12 U.S.C. 4513(f).

²² See 44 U.S.C. 3507(a) and (d).

²³ See 44 U.S.C. 3512(a); 5 CFR 1320.8(b)(3)(vi).

V. Regulatory Flexibility Act

The Regulatory Flexibility Act²⁴ (RFA) requires that a regulation that has a significant economic impact on a substantial number of small entities, small businesses, or small organizations must include an initial regulatory flexibility analysis describing the regulation's impact on small entities. Such an analysis need not be undertaken if the agency has certified that the regulation will not have a significant economic impact on a substantial number of small entities.²⁵ FHFA has considered the impact of the final rule under the RFA. The General Counsel of FHFA certifies that the final rule is not likely to have a significant economic impact on a substantial number of small entities because the regulation applies only to the Banks, which are not small entities for purposes of the RFA.

List of Subjects in 12 CFR Part 1263

Federal home loan banks, Reporting and recordkeeping requirements.

Authority and Issuance

For the reasons stated in the **SUPPLEMENTARY INFORMATION**, and under the authority of 12 U.S.C. 4511, 4513, and 4526, FHFA amends part 1263 of subchapter D of chapter XII of title 12 of the Code of Federal Regulations as follows:

PART 1263—MEMBERS OF THE BANKS

1. The authority citation for part 1263 continues to read as follows:

Authority: 12 U.S.C. 1422, 1423, 1424, 1426, 1430, 1442, 4511, 4513.

2. Amend § 1263.1 as follows:

a. Revise the definitions of “CDFI credit union” and “Community development

²⁴ 5 U.S.C. 601, *et seq.*

²⁵ See 5 U.S.C. 605(b).

financial institution or CDFI”;

b. Add, in alphabetical order, a definition for “Federal share insurance”;

c. Revise the definition of “Insured depository institution”;

d. Add, in alphabetical order, a definition for “Non-federally-insured credit union”; and

e. Revise the definition of “Regulatory financial report”.

The revisions and additions read as follows:

§ 1263.1 Definitions.

* * * * *

CDFI credit union means a State-chartered credit union that does not have Federal share insurance and that has been certified as a CDFI by the CDFI Fund.

* * * * *

Community development financial institution or CDFI means an institution that is certified as a community development financial institution by the CDFI Fund under the Community Development Banking and Financial Institutions Act of 1994 (12 U.S.C. 4701 et seq.), other than a bank or savings association insured under the Federal Deposit Insurance Act (12 U.S.C. 1811 et seq.), a holding company for such a bank or savings association, or a credit union that has Federal share insurance.

* * * * *

Federal share insurance means insurance coverage of credit union member accounts provided by the National Credit Union Share Insurance Fund under subchapter II of the Federal Credit Union Act (12 U.S.C. 1781 et seq.).

* * * * *

Insured depository institution means:

(1) An insured depository institution as defined in section 2(9) of the Bank Act, as amended (12 U.S.C. 1422(9)); and

(2) To the extent provided under § 1263.19, a non-federally-insured credit union.

* * * * *

Non-federally-insured credit union means a State-chartered credit union that does not have Federal share insurance and that has not been certified as a CDFI by the CDFI Fund.

* * * * *

Regulatory financial report means a financial report that an institution is required to file with its appropriate regulator on a specific periodic basis, including the quarterly call report for commercial banks and savings associations, quarterly or semi-annual call report for credit unions, NAIC's annual or quarterly statement for insurance companies, or other similar report, including such report maintained by the appropriate regulator in an electronic database.

* * * * *

§ 1263.2 [Amended]

3. Amend § 1263.2:

a. By removing “to 1263.18” wherever it appears and, in its place, adding “through 1263.19”; and

b. In paragraph (b), by adding at the end of the paragraph the sentence “In preparing a digest for a non-federally-insured credit union applicant, the Bank shall summarize the manner in which the applicant has complied with the requirements of §

1263.19(a).”

§ 1263.3 [Amended]

4. Amend § 1263.3, in paragraph (c), by removing from the second sentence the words “a Bank” and adding in their place the words “the Bank”.

§ 1263.11 [Amended]

5. Amend § 1263.11, in paragraph (b)(3)(iii), by removing the words “A CDFI credit union applicant” and adding in their place the words “An applicant that is a CDFI credit union or a non-federally-insured credit union”.

§ 1263.19 [Transferred to Subpart C]

6. Transfer reserved § 1263.19 to subpart C.

Subpart C—Eligibility Requirements

7. Add § 1263.19 to read as follows:

§ 1263.19 Non-federally-insured credit unions.

(a) Applicants. Except where otherwise provided, a non-federally-insured credit union applying to become a member of a Bank shall be treated as an insured depository institution for purposes of determining its eligibility for membership under this part, provided that all of the following requirements have been met:

(1) Notice. Upon receiving from a non-federally-insured credit union an application for membership, a Bank shall promptly notify the applicant in writing that its application will not be deemed complete or be acted upon by the Bank until the applicant has, in addition to satisfying all other generally applicable requirements, complied with paragraph (a)(2) of this section and subsequently provided one of the items listed in paragraph (a)(3) of this section.

(2) Request to regulator. After receiving the notice required under paragraph (a)(1) of this section, a non-federally-insured credit union applicant shall send to its appropriate State regulator a written request for a determination that the applicant met all of the eligibility requirements for Federal share insurance as of the date of the request. The applicant shall provide to the Bank a copy of that request simultaneously with its transmittal to the regulator.

(3) Completion of application. A Bank may deem the application of a non-federally-insured credit union to be complete and may act upon the application, as provided under § 1263.3(c), only if it has received from the applicant one of the following items:

(i) A written statement from the applicant's appropriate State regulator that the applicant met all of the eligibility requirements for Federal share insurance as of the date of the request sent pursuant to paragraph (a)(2) of this section;

(ii) A written statement from the applicant's appropriate State regulator that it cannot or will not make a determination regarding the applicant's eligibility for Federal share insurance; or

(iii) A written statement from the applicant, prepared no earlier than the end of the six-month period beginning on the date of the request sent pursuant to paragraph (a)(2) of this section, certifying that the applicant did not receive from its appropriate State regulator within that six-month period either a response as described in paragraph (a)(3)(i) or (ii) of this section or a response stating that the applicant did not meet all of the eligibility requirements for Federal share insurance as of the date of the request sent pursuant to paragraph (a)(2) of this section.

(b) Members canceling Federal share insurance. A Bank member that is a federally insured credit union and that subsequently cancels its Federal share insurance may remain a member of the Bank, subject to all regulatory provisions applicable to insured depository institution members, provided that the Bank has determined that the institution has canceled its Federal share insurance voluntarily.

8. Amend § 1263.31 by revising paragraphs (b) and (e) to read as follows:

§ 1263.31 Reports and examinations.

* * * * *

(b) Agrees that reports of examination by local, State, or Federal agencies or institutions, or by any private entity providing share insurance to a member that is a non-federally-insured credit union or a CDFI credit union, may be furnished by such authorities or entities to the Bank or FHFA upon request;

* * * * *

(e) To the extent applicable, agrees to provide to the Bank, within 20 days of filing, copies of reports of condition and operations required to be filed with:

(1) The member's appropriate Federal banking agency;

(2) The member's appropriate State regulator; or

(3) Any private entity providing share insurance to a member that is a non-federally-insured credit union or a CDFI credit union.

_____ Dated: May 24, 2017.
Melvin L. Watt,
Director, Federal Housing Finance Agency.

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