

Federal Home Loan Bank Insurance Parity Statute Summary

The Issue

The Federal Home Loan Bank of Cincinnati (FHLB) seeks legislation to improve terms of FHLB lending to Kentucky domiciled member insurance companies.

Under federal law, the 11 regional FHLBanks, including Cincinnati, are exempt from stay and voidable preference requirements in regards to a depository institution in receivership. Consequently, an FHLBank is able (should it become necessary) to promptly apply an appropriate amount of collateral pledged by an insolvent depository institution toward the satisfaction of such member's outstanding obligations to such FHLBank. Because Kentucky law governing FHLB lending to insurance companies differs from federal banking law governing FHLBank (and Federal Reserve Bank) lending to depository institutions, insurance companies may be required to borrow from FHLBanks on less advantageous terms (including collateral requirements) than do similarly rated depository institutions. This lack of parity with federal law has been an area of focus by the FHLBanks' regulator, the Federal Housing Finance Agency (FHFA). The FHFA views lending to insurance companies as a higher risk than lending to depositories, in part due to the potential of a regulatory stay being placed on the FHLB's ability to liquidate pledged collateral. As a result, the FHFA is requiring more stringent collateral requirements to secure FHLB lending in the event, however unlikely, of any insurance company's failure.

Impact

Under regulatory direction, the FHLB phased in adjusted collateral requirements in 2017, commencing with pledged securities. Depending on the type of bonds pledged, Kentucky insurers are currently required to pledge on average just over 2 percent additional collateral relative to Ohio and Tennessee insurance company members for the same class of collateral, having an estimated negative impact of \$6.0 million in borrowing capacity.

Suggested Action

In 2013, the FHLBanks worked with a National Association of Insurance Commissioners (NAIC) subgroup to study the legislation. The report of the subgroup presents a comprehensive range of findings and recommendations for state insurance regulators should this legislation be raised in their states. NAIC recommends that regulation be considered on a state-by-state basis.

There are currently 21 states that have this type of legislation enacted as law: Alabama, Arizona, Colorado, Delaware, Georgia, Illinois, Indiana, Iowa, Kansas, Maryland, Michigan, Missouri, Nebraska, North Carolina, Ohio, Oklahoma, Pennsylvania, South Carolina, Tennessee, West Virginia, and Wisconsin. The states with effective statutes are shielded from required collateral adjustments noted above. Several other states are pursuing similar statutes.

The FHLB's proposed legislation is similar to language adopted by the aforementioned states, and would be functionally identical to language passed in Ohio and Tennessee. The proposed bill would amend and create new sections of the Kentucky Revised Statutes under Title 25, Chapter 304, Subtitle 33, to allow a limited exemption for the FHLB from judicial stays and preference requirements after ten days following the commencement of a delinquency proceeding, and to provide a process for the FHLB, the member, and the receiver to follow.

This solution would allow the FHLB's insurance company members chartered in Kentucky to more efficiently manage their assets and their funding, and will establish a more robust framework for cooperation and coordination between the FHLB and the Department of Insurance.