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Federal Home Loan Banks: Actions Related to the Spring 2023 Bank Failures

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Q&A Report to the Committee on Financial Services, House of Representatives
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Why This Matters

Between March 10 and May 1, 2023, state banking supervisors closed Silicon Valley Bank (SVB), Signature Bank, and First Republic Bank and named the Federal Deposit Insurance Corporation (FDIC) as receiver.

The three failed banks had borrowed substantial secured loans from their respective Federal Home Loan Banks (FHLBank) before their failures. The FHLBanks are government-sponsored enterprises that support liquidity by making loans (known as advances) to member financial institutions and promote housing and community development. The FHLBank System includes 11 separate federally chartered banks. SVB and First Republic Bank were members of the FHLBank of San Francisco (FHLBSF), and Signature Bank was a member of the FHLBank of New York (FHLBNY).

We were asked to review the role of the FHLBanks with regard to the recent bank failures. This report provides information on the FHLBanks' funding to the failed banks, their communication and coordination with FDIC and the Federal Reserve System (the failed banks' primary federal regulators), and repayment of the failed banks' outstanding advances.

This report is one in a series of reports about the bank failures.[1] We plan to follow this report with work on broader issues related to the FHLBanks.

Key Takeaways

- SVB, Signature Bank, and First Republic Bank each held substantially more FHLBank advances (as a proportion of their total assets) than a group of 16 commercial bank peers as of year-end 2022.
- The three banks increased their outstanding FHLBank advances by 37 to 50 percent in the first 2 weeks of March 2023, when SVB and Signature Bank failed. First Republic Bank's outstanding advances then largely stabilized until the bank failed on May 1.
- FHLBNY and FHLBSF reviewed regulators' examination reports for the three failed banks and stated that they met regularly with FDIC, the Federal Reserve Banks, and other regulators before the failures. The two FHLBanks and FDIC communicated about Signature Bank and First Republic Bank as the banks were declining, but SVB failed before FHLBSF requested additional supervisory information from the Federal Reserve Bank of San Francisco.
- The two FHLBanks relied on established policies, procedures, and agreements with the relevant Federal Reserve Banks to help Signature Bank and First Republic Bank transfer pledges of collateral between the FHLBanks and the Federal Reserve Banks. These efforts allowed the banks to access additional funding. FHLBSF and Federal Reserve Bank of San Francisco officials said SVB failed before the bank could coordinate collateral pledges between FHLBSF and the Federal Reserve Bank.

- FHLBNY has received full repayment for Signature Bank's advances, and FHLBSF has received full repayment for SVB's advances and repayment of First Republic Bank's advances that have reached maturity. The bank that assumed First Republic Bank's advances indicated that it intends to repay them according to the advance terms.
- According to FDIC officials, repayment of FHLBank advances for a failed bank does not impose a direct cost to the Deposit Insurance Fund. However, if proceeds of the failed bank's liquidated assets do not cover claims eligible for the fund after repayment of FHLBank advances and any other secured claims, the Deposit Insurance Fund would incur costs.

What are FHLBank advances?

FHLBank advances are secured loans that serve as the primary mechanism by which FHLBanks provide funding to member institutions, including banks.[2] Advances can serve as a low-cost funding source for member institutions to make mortgage loans or to lower their liquidity risk. Although regulations require that advances have certain features, each FHLBank has the flexibility to structure the specific terms of advances within those legal parameters. Advance offerings can vary by certain characteristics:

- **Product type.** FHLBanks offer a variety of advance products, including variable and fixed-rate advances.[3] Fixed-rate advances typically represent more than half of advances.
- **Length.** Maturities of FHLBank advances range from overnight to 30 years, although the majority of advances are for 3 years or less. FHLBank officials stated that large commercial banks (such as the three that failed) often request advances with maturities of less than 6 months. Members choose advances with shorter or longer maturities depending on interest rates and their strategies for using advances as a liquidity source, according to the Federal Housing Finance Agency (FHFA) and FHLBank officials. For example, FHLBSF officials said members may seek overnight advances to manage daily cash flows, or longer-term fixed-rate advances to secure a low interest rate in a rising-rate environment.
- **Eligible collateral.** Members are required to secure FHLBank advances with eligible collateral. Such collateral can include, among other things, certain mortgage loans; agency mortgage-backed securities; other real estate-related collateral; debt obligations or securities issued by the U.S. government, such as U.S. Treasuries; and cash or deposits. For the FHLBank System at year-end 2022, single-family mortgage loans represented approximately 49 percent of all eligible pledged collateral, and commercial real estate loans represented 19 percent.[4]

What does regulators' guidance say about examining FHLBank advances?

The examination guidance of FDIC and the Board of Governors of the Federal Reserve System generally directs bank examiners to consider FHLBank advances as part of their broader assessment of banks' funding and liquidity risk management.[5] This assessment includes reviewing banks' assets and liabilities to identify significant borrowings and potential concentrations of funding sources, including FHLBank advances.

Examiners also are to consider how well a bank is meeting its current and future funding needs. Relevant factors include the bank's prospective sources of liquidity and its plans for raising supplemental funding during a stress event. Examiners consider the efficiency with which a bank can borrow from supplemental funding sources, including FHLBanks.

FDIC and the Federal Reserve also have additional examination practices related to FHLBank advances:

- FDIC's examination instructions state that if a bank holds 10 percent or more of total assets in a specific funding source, such as FHLBank advances, examiners must document how the bank uses that funding and the economic and business conditions surrounding the source.
- Federal Reserve examination guidance directs examiners to analyze FHLBank advance documentation to determine if the advance achieved its stated purpose or whether it reflects liquidity deficiencies.

How do FHLBanks provide advances to member institutions?

FHLBank advances typically involve the following steps:

- **Setting a credit limit.** When an institution applies for FHLBank membership, the FHLBank conducts an initial assessment of the applicant's creditworthiness and assigns it a financing limit—typically a percentage of the applicant's total assets. FHLBanks periodically reassess their members' creditworthiness and generally limit borrowing to 20 to 60 percent of a member's total assets.
- **Pledging collateral.** To obtain an advance, a member must pledge eligible collateral in proportion to its borrowings from the FHLBank. The amount of required collateral incorporates the cost to sell or liquidate the pledged collateral and the risk of a potential decline in its current market value. As a result, the reported market value of a member's pledged collateral generally exceeds the amount owed to the FHLBank.
- **Making the advance.** The FHLBank generally lends the requested amount if it is within the lesser o44f the member's available borrowing capacity or its credit limit, subject to certain market conditions. Advances are not associated with specific collateral; rather, members can borrow against the aggregate borrowing capacity of their pledged collateral.

  FHLBank officials stated that large commercial banks usually pledge more collateral than they plan to use at any one time so that it is available to be borrowed against when needed.[6] According to officials, most members use 20 to 30 percent of the borrowing capacity of their pledged collateral at any one time.

The member must also purchase and maintain stock in its FHLBank, consistent with the capital structure plan of the FHLBank, as part of its membership obligations and as a condition of transacting business with the FHLBank.[7] In turn, the FHLBank has a lien upon and holds the stock of the member as additional collateral for all advances.

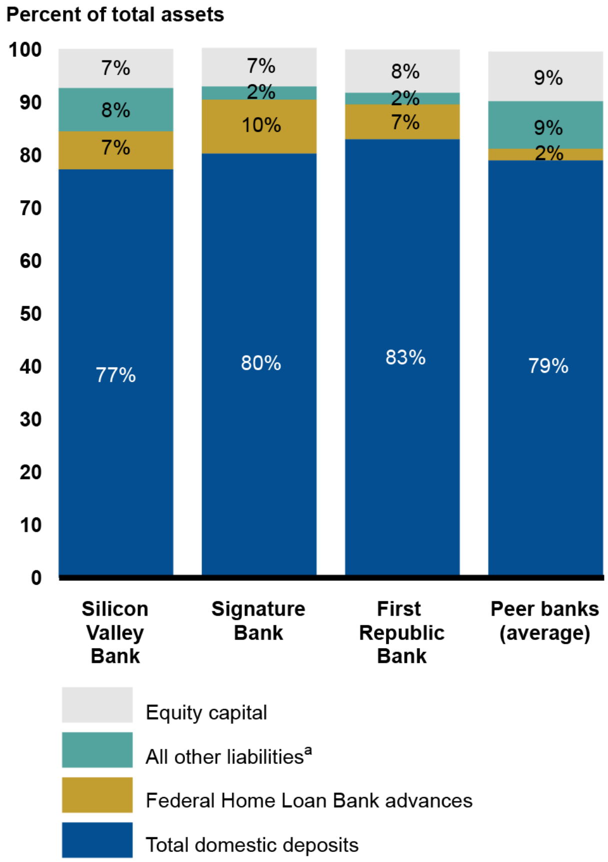
An FHLBank may limit or deny a member's advance request for many reasons, including if it determines, based on supervisory information from the member's primary regulator, that the member is engaging in unsafe or unsound banking practices. Under certain conditions—including if a member's financial condition is deteriorating—the FHLBank also may require a detailed list of loans pledged or take physical possession of collateral as a condition for outstanding or new advances.

FHLBank officials stated that they typically fulfill advance requests within minutes for established members with sufficient pledged collateral and credit availability. However, the timing and size of a request can affect an FHLBank's ability to fund an advance request quickly or fully. Among other things, FHLBanks must weigh a large advance request against other member requests to ensure they can meet all members' needs. To fund member requests, FHLBanks access the capital markets by issuing debt through their joint Office of Finance.[8] FHLBanks set deadlines for same-day requests to ensure the Office of Finance can access the markets during business hours.

What was the funding composition of the failed banks compared with that of peer banks?

The proportion of total domestic deposits to total assets of SVB, Signature Bank, and First Republic Bank was similar to that of a peer group of 16 commercial banks at year-end 2022 (the most recent quarter in which data were available for all three failed banks).[9] However, the three failed banks had substantially higher proportions of FHLBank advances than the peer group average (see fig. 1).

Figure 1: Funding Composition of Failed Banks and Peer Banks as of Dec. 31, 2022



Source: GAO analysis of Federal Financial Institutions Examination Council call report data. | GAO-24-106957

Notes: Our analysis compared Silicon Valley Bank, Signature Bank, and First Republic Bank with a group of 16 commercial banks with reported domestic deposit balances and total assets between $100 and $250 billion at year-end 2022 in their fourth quarter 2022 Federal Financial Institutions Examination Council call reports. The banks were also members of the Federal Home Loan Bank System. Percentages may not add up to 100 percent due to rounding.

[a]All other liabilities may include borrowings from Federal Reserve Banks, federal funds, repurchase agreements, and subordinated notes and debentures, among others.

The three banks' other liabilities (such as borrowings from Federal Reserve Banks, including the discount window; federal funds; and repurchase agreements) as a percentage of their total assets did not show a clear pattern compared with the peer banks.[10] In contrast, the three failed banks and the peer banks had similar proportions of equity capital (which includes retained earnings and stock) to total assets.

Throughout 2022, SVB, Signature Bank, and First Republic Bank all reported decreases in total domestic deposits as a percentage of total assets, while their use of FHLBank advances increased (see table 1). The same trend occurred for the peer group, but to a lesser degree. The Federal Reserve's interest rate increases that began in March 2022 caused volatility in deposit rates. This led commercial banks to seek alternate sources of short-term, liquid funding (such as FHLBank advances), according to the Council of Federal Home Loan Banks—the FHLBank System's trade association—and FHFA, which oversees the FHLBank System.

Table 1: Percentage Point Changes in Selected Funding Categories for Failed Banks and Peer Banks, First Quarter 2022–Fourth Quarter 2022

	Total domestic deposits	Federal Home Loan Bank advances
Silicon Valley Bank	-6.7	7.2
Signature Bank	-9.3	8.2
First Republic Bank	-3.6	4.6
Peer banks (average)	-1.5	1.2

Source: GAO analysis of Federal Financial Institutions Examination Council call report data. | GAO-24-106957

Note: Our analysis compared Silicon Valley Bank, Signature Bank, and First Republic Bank with a group of 16 commercial banks with reported domestic deposit balances and total assets between $100 and $250 billion at year-end 2022 in their fourth quarter 2022 Federal Financial Institutions Examination Council call reports. The banks were also members of the Federal Home Loan Bank System.

SVB, Signature Bank, and First Republic Bank had significantly higher proportions of uninsured domestic deposits than did peer banks.[11] Uninsured deposits can be an unstable source of funding because customers may be more likely to withdraw these funds during times of stress.[12] Between the first quarter and the fourth quarter of 2022, the three failed banks' proportions of uninsured deposits decreased, while their proportions of FHLBank advances increased. The peer banks' use of advances remained relatively stable compared with the three failed banks (see fig. 2).

Figure 2: Funding Composition of Failed Banks and Peer Banks in 2022, by Quarter

Source: GAO analysis of Federal Financial Institutions Examination Council call report data. | GAO-24-106957

Note: Our analysis compared Silicon Valley Bank, Signature Bank, and First Republic Bank with a group of 16 commercial banks with reported domestic deposit balances and total assets between $100 and $250 billion at year-end 2022 in their fourth quarter 2022 Federal Financial Institutions Examination Council call reports. The banks were also members of the Federal Home Loan Bank System.

[a]All other liabilities may include borrowings from Federal Reserve Banks, federal funds, repurchase agreements, and subordinated notes and debentures, among others.

All three banks' FHLBank advances increased in dollar value between the first quarter and fourth quarter of 2022. In contrast, the dollar value of total domestic deposits increased for First Republic Bank during the period (due to an increase in insured deposits) but decreased for the other two banks. According to FDIC officials, the three failed banks had different business models and had different reasons for increasing their FHLBank advance borrowing in 2022.

SVB and Signature Bank did not file call reports (financial reports required by law) for the first quarter of 2023 because they failed before the quarter ended. However, First Republic Bank reported that its FHLBank advances nearly doubled as a percentage of its total assets in the first quarter of 2023, compared with the previous quarter. See appendix I for further analysis of First Republic Bank's funding composition.

Our review of FDIC and Federal Reserve examination reports for the three failed banks since January 2021 found that the regulators did not identify the proportion of FHLBank advances as a specific factor in any concerns about the banks' safety and soundness. In their reports, FDIC and the Federal Reserve identified broader issues, such as inadequate liquidity stress tests or contingency funding plans.[13] FHLBank advances are one of many sources of liquidity and contingency funding that examiners would have considered in developing their findings.

What actions did the FHLBanks take leading up to the three banks' failures in 2023?

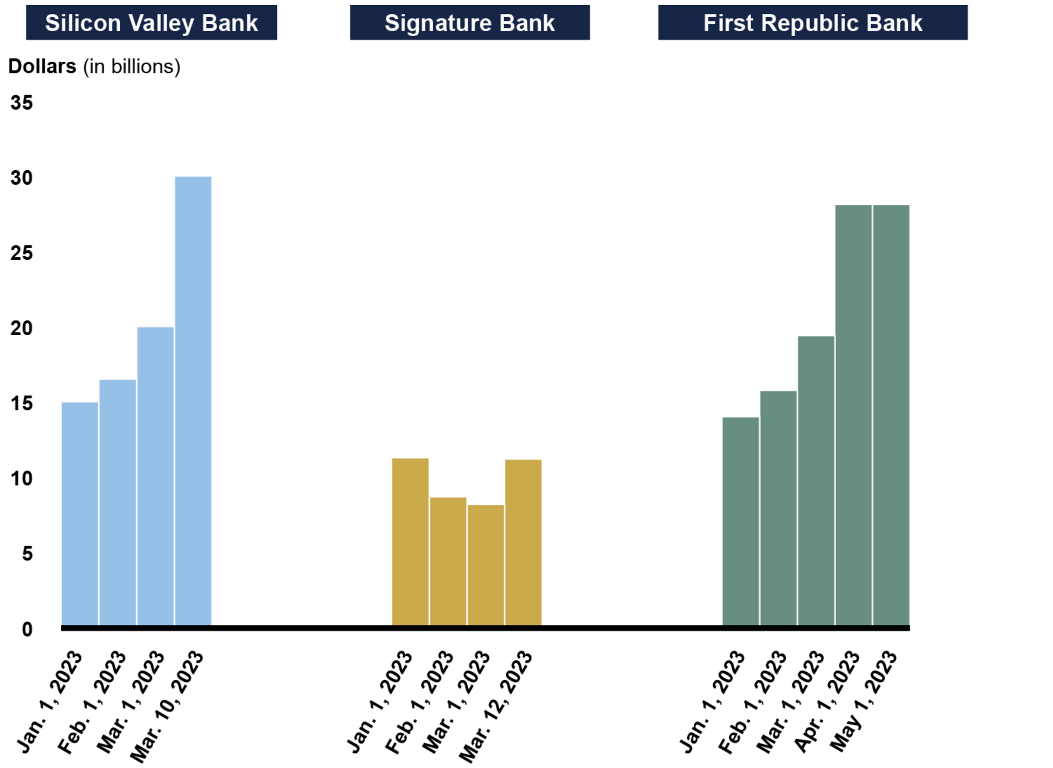
FHLBNY and FHLBSF continued to provide advances to the three failed banks in 2023, while also taking steps to reduce their own exposure to credit risk from these banks.

January and February 2023

At the beginning of 2023, SVB and First Republic were FHLBSF's two largest borrowers, holding 17 percent and 16 percent, respectively, of FHLBSF's total advance balances outstanding. Signature Bank was FHLBNY's fourth largest borrower at the time, holding approximately 10 percent of FHLBNY's total advance balances outstanding.

In January and February 2023, the three failed banks maintained outstanding advance balances from their respective FHLBanks. As shown in figure 3, the amount of outstanding advances increased over the period for SVB and First Republic Bank and decreased for Signature Bank.

Figure 3: Failed Banks' Total Outstanding FHLBank Advances, Jan. 1, 2023, to Failure



Source: GAO analysis of Federal Home Loan Bank (FHLBank) advance data. | GAO-24-106957

A significant amount of new advances and renewals of existing advances to the three banks in January and February had maturities of 30 days or less. According to FHFA, the need for funding caused by interest rate increases led to a general increase in advance borrowing. Members steadily increased borrowing of advances with maturities of 30 days or less throughout 2022 and into 2023. FHLBNY and FHLBSF officials stated they did not deem the failed banks to be significant credit risks until March 2023.

March 1, 2023, through failure

SVB. From March 1 to March 8, 2023, SVB increased the balance of its outstanding advances by 50 percent, from approximately $20 billion to $30 billion. Most of the new and renewed advances SVB requested during this period were for terms of 1 to 3 years. FHLBSF officials said that SVB did not have a particular stated strategy for borrowing advances in that maturity range. However, the officials observed members requesting advances with longer maturities in 2023 compared with 2022 because members were concerned about rising interest rates.

From March 8 through SVB's failure on March 10, 2023, SVB's outstanding advance balance remained at $30 billion—approximately 28 percent of FHLBSF's total outstanding advances as of March 10, according to FHLBSF officials. FHLBSF was unable to fill an advance request from SVB for $20 billion on the afternoon of March 9. This was due to market conditions, the size and late timing of the request, and FHLBSF's need to better understand ongoing events, including SVB's customers withdrawing over $40 billion in deposits that day, according to FHLBSF officials.[14]

FHLBSF took steps to reduce its credit risk exposure starting on March 9, the day before SVB's failure. These included downgrading SVB's internal credit rating, updating SVB's collateral terms, and reducing SVB's credit limit to zero percent of its total assets (down from 25 percent at the start of the year).

Signature Bank. From March 1 through its failure on March 12, 2023, Signature Bank increased its outstanding advances by 37 percent, from approximately $8.2 billion to $11.2 billion. According to FHLBNY officials, Signature Bank's outstanding advances represented 9 percent of FHLBNY's total outstanding advances as of March 12.

FHLBNY officials said that in late 2022, Signature Bank provided a rough schedule of its strategy to temporarily replace crypto-related deposits with advances and indicated that it would slowly reduce its reliance on these advances over the course of 2023.[15] Signature Bank generally followed its schedule until March 2023.

FHLBNY continued to fill new and renewed advance requests with maturities of 30 days or less from Signature Bank during this period. These requests were in line with the bank's borrowing pattern in January and February 2023, but the bank also requested advances with maturities of 31 to 180 days.

FHLBNY officials said they did not update Signature Bank's credit limit or change contractual provisions of existing advances before the bank failed on March 12 because the events leading up to the bank's failure happened quickly. They also stated that they believed Signature Bank's liquidity position was adequate prior to the evening of Friday, March 10, when it experienced significant deposit runs. FHLBNY officials said that although the FHLBanks do not lend on the weekends, FHLBNY was working the weekend of March 11–12 to help Signature Bank access discount window borrowing (as described later in this report). They said they were operating under the expectation that the bank would be open for business on Monday, March 13.

First Republic Bank. From March 1 to March 13, 2023, First Republic Bank increased the balance of its outstanding advances by 45 percent, from approximately $19.4 billion to $28.1 billion. According to FHLBSF officials, First Republic Bank's advance balance represented 24 percent of FHLBSF's outstanding advances as of March 13. Most of the new and renewed advances the bank requested during this period had maturities of 30 days or less.

FHLBSF filled new and renewed advance requests of approximately $8 billion from First Republic Bank on Friday, March 10. However, FHLBSF did not fill additional advance requests for approximately $7 billion later that day. FHLBSF officials stated that they were unable to fill the advance request due to market conditions, the size and late timing of the request, requests for advances from other FHLBSF members, and FHLBSF's need to understand events related to depositor uncertainty at regional banks. These events included deposit runs at First Republic Bank. On Monday, March 13, FHLBSF filled $6 billion of First Republic Bank's $7 billion request from Friday.

From March 14 through First Republic Bank's failure on May 1, 2023, First Republic Bank's outstanding advance balance was largely stable at around $28.1 billion. According to FHLBSF officials, this represented 29 percent of FHLBSF's total outstanding advances as of May 1. However, due to renewals, advances with maturities of 1 to 3 years started making up a greater proportion of the bank's outstanding advance balance compared with advances of 30 days or less. FHLBSF officials stated that First Republic Bank was borrowing advances in this maturity range as part of its strategy to obtain more reliable liquidity.

FHLBSF took steps to reduce its credit risk exposure starting on March 11, 2023. These steps included downgrading First Republic Bank's internal credit rating, updating its collateral terms, and reducing its credit limit to 20 percent of its total assets (from 40 percent at the start of the year). FHFA officials stated that

FHLBSF also consulted with them on whether to continue lending to First Republic Bank on March 17, and they advised FHLBSF against providing the bank with new advances. FHLBSF did not provide any additional advances to First Republic Bank from March 14 up to the bank's failure, but it continued to renew existing advances.

FHLBSF officials said they also requested daily liquidity reports from First Republic Bank to monitor the bank's liquidity positions given the impact of deposit runs. Once First Republic Bank's liquidity situation stabilized, FHLBSF officials stated that they tried repeatedly to obtain a copy of its strategic plan for reestablishing long-term sustainability in April. However, First Republic Bank shared only a summary of the plan the week before its failure because the plan was not yet board-approved.

What additional advances did the FHLBanks provide to the three banks after failure?

After the bank failures, FHLBSF did not provide any new advances to Silicon Valley Bridge Bank, National Association, which took over SVB's banking services after its failure, or to First Republic Bank. FHLBNY continued to renew existing advances with Signature Bridge Bank, National Association, which took over Signature Bank's banking services, and then subsequently with FDIC as receiver (after Signature Bridge Bank was placed into receivership).[16]

SVB. On March 13, 2023, FDIC created Silicon Valley Bridge Bank—a temporary bank to take over and maintain banking services for SVB's customers—and transferred SVB's outstanding advances to the bridge bank. Silicon Valley Bridge Bank maintained outstanding advances with FHLBSF until March 17, 2023, and did not request additional FHLBank advances.

Signature Bank. After Signature Bank failed, FDIC created Signature Bridge Bank and transferred Signature Bank's outstanding advances to it. During the week of March 12 to March 18, 2023, FHLBNY renewed $3 billion of the advances, all of which had maturities of 90 days or less, with Signature Bridge Bank. After the bridge bank was placed in receivership on March 20, 2023, FHLBNY continued to renew the outstanding advances with FDIC as receiver until July 20, 2023.

First Republic Bank. According to FHLBSF officials, FHLBSF did not provide First Republic Bank with advances after its failure. JPMorgan Chase Bank, National Association, acquired the bank on the same day it failed and immediately assumed its outstanding advances. Because JPMorgan Chase is not a member of FHLBSF, these advances cannot be renewed.

What policies govern communication of supervisory and other information between regulators and FHLBanks?

Federal banking regulators are required by law to share supervisory information (including confidential examination findings) with the FHLBanks upon an FHLBank's request.[17] Federal financial regulators and the FHLBanks further outlined this process in a 1990 memorandum on sharing of supervisory information. The FHLBanks may use this information to evaluate credit applications and value collateral, among other purposes.

Per regulation, each FHLBank, upon written request from a member bank's federal regulator, must provide that regulator information on the given member's advances and commitments.[18] Officials from FDIC, the Federal Reserve, and FHLBSF stated that they rely on the member banks to share information on their FHLBank advances with their primary regulators.[19] FHLBNY officials added that they may also provide such information to member banks' primary regulators as part of such regulators' supervisory or resolution authorities.

To what extent did the regulators and FHLBanks share supervisory and other information about the three failed banks?

According to officials and documentation we reviewed, FHLBNY, FHLBSF, FDIC, and the Federal Reserve Banks communicated regularly to share supervisory or other information prior to and during the bank failures.

FHLBNY and FHLBSF requested and received examination reports for the three banks at various points before the failures. FHLBNY officials reviewed Signature Bank's most recent examination report in January 2023. FHLBSF officials said they regularly request any new examination reports for their members from the federal and state regulators' supervisory staff. This ensures they receive the most recent reports as soon as possible.

In addition, FHLBank officials said they meet with FDIC and the Federal Reserve Banks, as well as other regulators, several times a year to discuss trends in the bank sector and other areas of shared interest, such as collateral coordination with the Federal Reserve Banks. An FHLBank official noted that these regular discussions typically do not involve specific member bank information due to member confidentiality considerations.

FHLBNY, FHLBSF, and the federal regulators increased the frequency of their communication beginning in March 2023, when SVB experienced a depository run (see apps. II and III for timelines).

SVB. FHLBSF officials contacted staff in the Federal Reserve Bank of San Francisco's Supervision + Credit Group by email and phone on March 9, 2023, after SVB announced a significant loss from sales of its securities on March 8. However, by that point, SVB had experienced a large volume of withdrawals and closed within 48 hours of announcing losses. FHLBSF officials stated that, as a result of SVB's quick decline, they did not have time to formally request information about SVB's creditworthiness before its failure.

Signature Bank. FHLBNY officials stated that on March 10, 2023, they met with FDIC to discuss Signature Bank's overall liquidity position and borrowing capacity. Their goal was to keep FDIC apprised of advances to Signature Bank and to moderate potential receivership losses should the bank fail.

Email communications we reviewed between FHLBNY and FDIC from March 11 and 12 discussed Signature Bank's total outstanding advances and borrowing capacity and FHLBNY's subordination of its interest in certain of Signature Bank's pledged collateral to the Federal Reserve Bank of New York. FDIC did not advise FHLBNY officials as to whether they should lend to the bank. FDIC officials stated that they generally do not have a role in the credit decisions of FHLBanks.[20]

First Republic Bank. After SVB failed, FHLBSF requested information from federal and state regulators that could affect First Republic Bank's creditworthiness and financing limit. FDIC and First Republic Bank's state regulator shared two joint downgrade letters (from March 31 and April 28, 2023), as well as high-level supervisory information.

FHLBSF officials said that beginning the day before First Republic Bank's failure, FDIC reached out to FHLBSF and provided regular telephone updates about its auction and bid process for the bank. The calls included discussion of how the various bids could have affected FHLBSF's credit and collateral position.

When the banks had been or were about to be placed into receivership, discussions (including emails we reviewed) between the FHLBanks and FDIC turned to the status of and plans for resolving any outstanding FHLBank advances.

What policies and procedures govern pledging of collateral between the FHLBanks and Federal Reserve Banks?

FHLBNY and FHLBSF have policies, procedures, and agreements with the Federal Reserve Banks of New York and San Francisco, respectively, to facilitate pledging and depledging of collateral between the entities.[21]

Members may wish to pledge excess FHLBank collateral to a Federal Reserve Bank to access the discount window, which generally provides advances for short-term liquidity and accepts a wide variety of collateral, including much of the collateral eligible for FHLBank advances.[22] Banks can also move collateral pledges from the discount window to an FHLBank, depending on their liquidity strategies and other factors.

FHLBNY and FHLBSF routinely coordinate with the Federal Reserve Banks of New York and San Francisco, respectively, to ensure that their respective rights to collateral are clear. For example, FHLBNY and the Federal Reserve Bank of New York have a collateral administration agreement in place, which serves to enhance certainty between them regarding their respective rights to collateral that may be subject to security interests of both entities.

FHLBSF and the Federal Reserve Bank of San Francisco have templates of intercreditor agreements that specify the types of collateral that could be pledged to both institutions and which institution has a priority lien on which collateral. If a member needs to pledge collateral to the Federal Reserve Bank, the three parties enter into an intercreditor agreement and FHLBSF can subordinate its interest in such collateral to the Federal Reserve Bank, and vice versa.

To what extent did the Federal Reserve Banks and the FHLBanks coordinate on pledged collateral before the failures?

Starting on March 9, 2023, the FHLBanks and the Federal Reserve Banks of New York and San Francisco made several efforts, in accordance with their policies and procedures, to help the failing banks pledge collateral to obtain liquidity from the Federal Reserve Banks (see apps. II and III for timelines).

SVB. FHLBSF officials said they attempted to help SVB depledge certain of its excess collateral (i.e., collateral not needed to support outstanding advances) at FHLBSF and pledge it to the Federal Reserve Bank of San Francisco on March 9. However, the bank failed the next morning, before FHLBSF could work with the Federal Reserve Bank to move the collateral. According to Federal Reserve Bank officials, although SVB was able to borrow up to its existing lendable value at the discount window, the bank was not prepared to quickly reposition collateral from FHLBSF to access additional discount window funding.

FDIC, the Federal Reserve Banks, and other federal regulators issued updated guidance in July 2023 to encourage depository institutions to incorporate the discount window as part of their contingency funding plans. The guidance also reinforces the importance of operational readiness to use the discount window, including conducting periodic small-value transactions.[23]

Signature Bank. On March 10, FHLBNY subordinated its interest in a total of approximately $7.1 billion in excess pledged securities collateral of Signature Bank to the Federal Reserve Bank of New York via a subordination agreement to allow the bank to access discount window funding. This approach was necessary because Signature Bank missed the cutoff time to directly transfer securities held by a custodian bank to the Federal Reserve Bank of New York.

At Signature Bank's request, FHLBNY initiated a second subordination agreement for additional loan and securities collateral the weekend of Signature Bank's failure. The loan collateral consisted of commercial real estate loans, for which FHLBNY and the Federal Reserve Bank of New York use a subordination agreement. The subordination agreement was also necessary for the securities collateral because the Federal Reserve Banks' system for transferring securities is closed over the weekend, which made a direct transfer of the securities impossible. However, Signature Bank was closed and placed into receivership before the bank and FHLBNY finalized the collateral schedule for the agreement.[24]

First Republic Bank. During the weekend of March 11–12, FHLBSF, the Federal Reserve Bank of San Francisco, and First Republic Bank executed an intercreditor agreement that established the two lenders' respective lien positions and priorities regarding certain First Republic Bank loan collateral. This agreement gave First Republic Bank flexibility to pledge collateral to the institutions in a manner that would maximize its liquidity options.

According to our analysis of transaction records, from March 12 through April 28, First Republic Bank pledged and de-pledged collateral to FHLBSF and the Federal Reserve Bank of San Francisco multiple times. During this period, at First Republic Bank's request and pursuant to the March intercreditor agreement, FHLBSF subordinated its interest in up to approximately $121 billion of collateral to the Federal Reserve Bank of San Francisco.

What happens to outstanding FHLBank advances when a member bank fails?

The disposition of a failed bank's outstanding FHLBank advances varies depending on how FDIC, as receiver, resolves the bank.[25] Because FHLBanks are typically secured creditors that have perfected their security interests in pledged collateral, the receiver generally pays off secured FHLBank advances before it pays other creditors, including those holding unsecured collateral.[26]

As receiver for a failed bank, FDIC is responsible for settling claims against the failed bank, liquidating the bank, and selling its assets. FDIC has options in terms of how it executes these responsibilities in the resolution process. However, it must do so in a way that imposes the least cost to the Deposit Insurance Fund unless the systemic risk exception is invoked.[27]

The law allows for several resolution methods. The resolution method chosen by FDIC can affect how FHLBank advances are resolved. Specifically:

- **Purchase and assumption.** FDIC may find a purchaser financial institution to purchase some or all of the failed bank's assets and assume some or all of the failed bank's liabilities. This may include all or a portion of the outstanding FHLBank advances and the collateral securing those advances (which can be purchased or assumed separately or together). These transactions are executed via a purchase and assumption agreement.

  According to FHLBank officials, FDIC typically informs the FHLBank of the pending purchase upon execution of the purchase and assumption agreement. FHLBSF officials stated that they then conduct a credit and financial assessment of the purchaser to determine whether the advances can remain with the purchaser until the stated maturity dates.

- **FDIC pays as receiver.** FDIC as receiver may retain and repay the outstanding advances. Consistent with FDIC resolution and receivership rules, FDIC and the FHLBank must develop a mutually agreeable plan for the payment of advances or the servicing of, foreclosure upon, and liquidation of collateral securing the advances.[28]

  Because FHLBank advances are secured by collateral, FDIC as receiver must pay off a failed bank's outstanding FHLBank advances before it can access that collateral (the assets the failed bank pledged to the FHLBank). If FDIC fully pays off the outstanding advances, it can access the collateral and liquidate those assets, which enables FDIC to use the proceeds to pay other receivership obligations, such as depositors and other creditor claims.

As a receiver, FDIC also may organize a bridge depository institution that could assume outstanding advances or transfer such advances to a third-party assuming institution.

In addition to advances, elements that may need to be resolved following bank failure include the following:

- **Prepayment fees.** FHLBanks charge prepayment fees in most circumstances. These fees, as provided in an advance agreement and required by FHFA regulation for certain advance products, are established by formula to ensure that the FHLBank is financially indifferent if the advance is repaid early.[29]
- **Waiver fees.** Some FHLBanks may charge waiver fees to a member bank or FDIC in exchange for the ability to make voluntary prepayments exceeding established limits. For example, per the terms of FHLBSF's Confirmation of Advance agreement with its members, a member may only make voluntary prepayments that conform to established prepayment requirements, including daily and monthly limits. The FHLBank may waive these limits and charge the member or FDIC as receiver a waiver fee that will compensate the FHLBank for risks associated with allowing a prepayment exceeding the daily or monthly limits.
- **FHLBank stock.** FHLBank members must purchase and maintain FHLBank stock as part of their membership obligations and as a condition of transacting business with the FHLBank. When a member bank fails, the FHLBank repurchases the failed member's stock once all outstanding obligations are repaid. If the failed institution is acquired by another FHLBank member institution, the assuming institution may also keep the advances outstanding until the scheduled maturity dates and maintain the stock levels required to support those outstanding advances.

What are the potential costs of FHLBank advances to the Deposit Insurance Fund?

Repayment of FHLBank advances (in cases where FDIC as receiver retains them) does not have a direct cost to the Deposit Insurance Fund, according to FDIC officials. The receivership repays the FHLBank advances and is made whole through liquidation of the failed bank's assets. In a depositor payoff, the Deposit Insurance Fund would cover disbursements to protect insured deposits not covered by proceeds from the sale of the failed bank's assets, along with FDIC's costs in winding down the failed bank.[30]

However, FHLBank secured advance repayments are obligations of the receivership and are prioritized for repayment, consistent with 12 C.F.R. § 360.2, along with payments to other secured creditors. After these secured claims, the highest priorities for repayment are FDIC's administrative expenses as receiver and insured deposit liabilities. If proceeds of the failed bank's liquidated assets do not cover these claims, the Deposit Insurance Fund would incur a loss for the difference. However, FDIC officials noted that FHLBank advances typically represent a small portion of payments due during receivership.[31]

Research findings vary regarding the risks that failed banks' FHLBank advances pose to the Deposit Insurance Fund. For example, in 2000 and 2005, respectively, Federal Reserve Bank and FDIC studies noted that FHLBanks' priority position in receivership could subsidize member bank risk-taking, which could imply greater losses for the Deposit Insurance Fund.[32] A 2023 FHFA review of academic literature found that FHLBanks' regulatory policies and practices mitigate moral hazard concerns.[33] In addition, a 2023 Urban Institute study found that an increase in a bank's use of FHLBank advances reduces its odds of failure, particularly for smaller banks.[34]

What is the status of FHLBank advance claims for the three failed banks?

FHLBNY has received full repayment for Signature Bank's advances, and FHLBSF has received full repayment for SVB's advances and repayment of First Republic Bank's advances that have reached maturity (see table 2).

Table 2: Status of Repayment of Failed Banks' Advances to FHLBanks, as of Feb. 26, 2024

Dollars in millions

	Silicon Valley Bank	Signature Bank	First Republic Bank
Total outstanding advances at the time of failure	$30,000	$11,184	$28,100
Advances repaid	30,000	11,184	5,825
Prepayment fees paid	266.5	0.26	—
Waiver fees paid	18.8	—	—
Outstanding advances	0	0	22,275[a]

Legend: — = not applicable

Source: GAO analysis of Federal Deposit Insurance Corporation and Federal Home Loan Bank (FHLBank) data. | GAO-24-106957

[a]First Republic Bank's outstanding advances were assumed by JPMorgan Chase Bank, National Association, which has indicated that it will repay the advances according to the advance terms, according to FHLBank officials.

SVB. After SVB failed, FDIC transferred its deposits and nearly all of its assets to Silicon Valley Bridge Bank, which paid all outstanding FHLBank advances by March 17, 2023. Silicon Valley Bridge Bank also paid approximately $19 million in waiver fees for SVB. The institution that ultimately assumed SVB's FHLBank advances received $810 million from FHLBSF's repurchase of SVB's FHLBank stock. As of March 17, the total collateral released to FDIC as receiver for Silicon Valley Bridge Bank had a market value of approximately $50.3 billion, according to FHLBSF officials.

Signature Bank. After Signature Bank failed, FDIC transferred its deposits and nearly all of its assets to Signature Bridge Bank. Signature Bridge Bank retained its FHLBank advances when Flagstar Bank, National Association acquired many of Signature Bridge Bank's assets. Signature Bridge Bank and FDIC, as receiver to Signature Bridge Bank, paid all outstanding FHLBank advances by July 20, 2023.

Through July 21, the collateral released to FDIC as receiver for Signature Bank and Signature Bridge Bank had a market value of approximately $20.9 billion, according to FHLBNY officials. FDIC as receiver also received $556 million when FHLBNY repurchased Signature Bank's FHLBank stock.

First Republic Bank. First Republic Bank's outstanding FHLBank advances were assumed by JPMorgan Chase, which has indicated to FHLBSF that it plans to repay those advances according to the advance terms. JPMorgan Chase is not a member of FHLBSF, so these advances cannot be renewed. As of February 26, 2024, JPMorgan Chase had repaid approximately $5.83 billion in advances that had reached maturity.

Agency Comments and Third Party Views

We provided a draft of this report to FDIC, the Federal Reserve, FHFA, FHLBNY, FHLBSF, and the Council of FHLBanks for review and comment. FHFA and the Council of FHLBanks provided written comments that are reprinted in appendixes IV and V, respectively. FDIC, FHFA, FHLBNY, and FHLBSF provided technical comments, which we incorporated as appropriate.

How GAO Did This Study

To describe advances and how FHLBanks provide them to member banks, we reviewed FHFA's regulations for the FHLBank System. We also reviewed FHLBank System publications and FHLBNY and FHLBSF policies on advances and credit risk management.

To describe regulators' examination guidance on FHLBank advances, we reviewed relevant sections of FDIC's *Risk Management Manual of Examination Policies* and the Federal Reserve Board's *Commercial Bank Examination Manual*. We also reviewed other guidance applicable to FHLBank advances, including an addendum to an interagency policy statement on funding and liquidity risk management, an FDIC memorandum on advances, and FDIC procedures for analyzing liquidity. We also reviewed the regulators' relevant examination reports and supervisory letters for SVB, Signature Bank, and First Republic Bank for examinations conducted from January 2021 through the banks' failures. We selected this time frame because it allowed us to capture any differences in how the regulators assessed advance use as the banks' use increased over time.

To compare the failed banks' funding with that of peer banks, we identified banks that, as of year-end 2022, were members of the FHLBank System and reported assets between $100 billion to $250 billion and domestic deposits greater than $0 in their Federal Financial Institutions Examination Council call reports (publicly available regulatory reports). The peer bank group we identified consisted of 16 banks.

We reviewed the failed and peer banks' Federal Financial Institutions Examination Council call report data on key funding sources, including insured and uninsured domestic deposits, FHLBank advances, other liabilities, and equity capital for all four quarters of 2022 and the first quarter of 2023.[35] We began our analysis with the first quarter of 2022 to capture any changes in FHLBank borrowing in response to the Federal Reserve's interest rate increases that began in March 2022. We assessed the reliability of the call report data by reviewing relevant documentation and tracing selections of downloaded data back to the individual banks' call reports. We determined that the data were reliable for the purpose of reporting the banks' funding sources.

To describe the FHLBanks' actions regarding the three banks, we analyzed data from FHLBNY and FHLBSF on the dates, amounts, and maturities of advances they provided to the three banks in 2023. We limited our analysis to advances with maturities of 3 years or less because FHFA officials told us most advances fit within this duration. We also analyzed data on outstanding advance balances for the three banks for selected dates in 2023.

We assessed the reliability of the advance data by reviewing relevant documentation and interviewing FHLBNY and FHLBSF officials. We determined that the data were reliable for the purpose of reporting the three banks' received and outstanding advances from January 2023 through their failures. In addition, we reviewed FHLBNY's and FHLBSF's 2022 10-K reports filed with the Securities and Exchange Commission to obtain information on their largest borrowers.

To assess communication of supervisory information between the FHLBanks and the regulators, we reviewed laws, regulations, agreements, and associated policies related to sharing supervisory information. We also reviewed agreements, policies, procedures, and templates from FHLBNY, FHLBSF, and the Federal Reserve Banks of New York and San Francisco related to pledging collateral between the FHLBanks and the Federal Reserve Banks. In addition, we reviewed subordination agreements FHLBNY completed with the Federal Reserve Bank of New York and intercreditor agreements FHLBSF completed with the Federal Reserve Bank of San Francisco and analyzed data on the amounts and types of collateral pledged between the entities.

We assessed the reliability of the First Republic Bank collateral pledge data by reviewing relevant documentation and interviewing FHLBSF officials. We determined that the data were reliable for our purpose of reporting the value of collateral that First Republic Bank pledged between FHLBSF and the Federal Reserve Bank of San Francisco from March 12 until its failure. We also reviewed other documentation on communication and coordination among the entities, including emails and timelines. We compared these entities' efforts against their policies and procedures and federal internal control standards on external communication.[36]

To describe what happens to outstanding FHLBank advances for failed banks, we reviewed applicable statutes, FDIC resolution and receivership regulations, and FHLBNY's additional policies and procedures for failed banks. To describe the potential risks that failed banks' FHLBank advances pose to the Deposit Insurance Fund, we reviewed FHFA's 2023 literature review findings and existing studies identified through structured internet searches.[37] To describe the status of the failed banks' outstanding advances, we obtained and corroborated data from FDIC, FHLBNY, and FHLBSF.

To inform all our work, we interviewed officials from the Council of FHLBanks, FHLBNY, FHLBSF, FDIC, the Federal Reserve System (including staff from the Board of Governors and the Federal Reserve Banks of New York and San Francisco), and FHFA.

We conducted this performance audit from July 2023 to March 2024 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

List of Addressees

The Honorable Patrick McHenry
Chairman
The Honorable Maxine Waters
Ranking Member
Committee on Financial Services
House of Representatives

As agreed with your offices, unless you publicly announce the contents of this report earlier, we plan no further distribution until 30 days from the report date. At that time, we will send copies to the House Financial Services Committee, the Chairman of the Federal Deposit Insurance Corporation, the Chairman of the Board of Governors of the Federal Reserve System, the Director of the Federal Housing Finance Agency, and other interested parties. In addition, the report will be available at no charge on the GAO website at https://www.gao.gov.

GAO Contact Information

For more information, contact: Jill Naamane, Director, Financial Markets and Community Investment, NaamaneJ@gao.gov, (202) 512-8678.

Chuck Young, Managing Director, Public Affairs, YoungC1@gao.gov, (202) 512-4800.

A. Nicole Clowers, Managing Director, Congressional Relations, ClowersA@gao.gov, (202) 512-4400.

Staff Acknowledgments: Patricia MacWilliams (Assistant Director), Lisa Reynolds (Analyst-in-Charge), Abigail Brown, Lauren Capitini, M'Baye Diagne, Jill Lacey, Fritz Manzano, Catherine Paxton, David Raymond, Jennifer Schwartz, and Jena Sinkfield.

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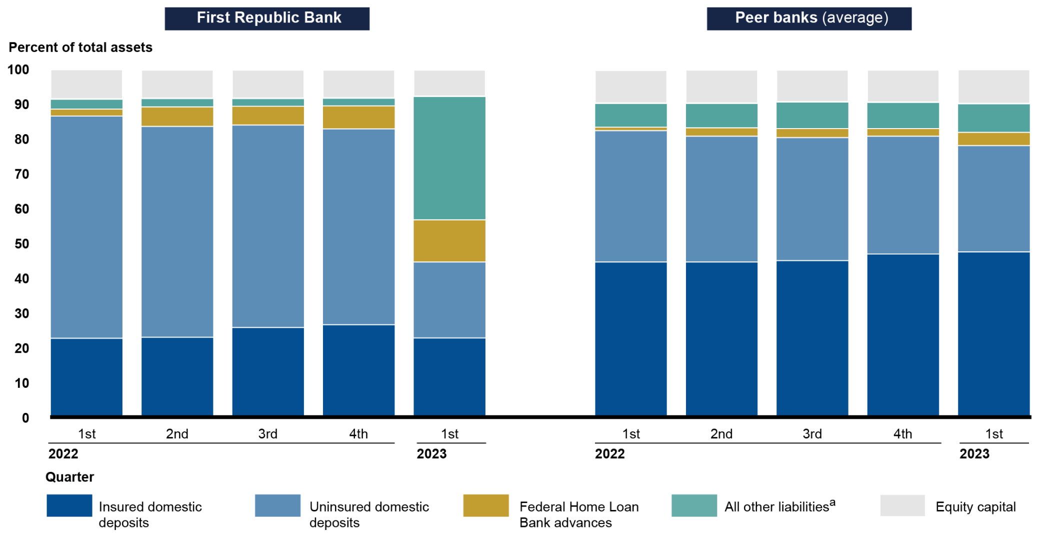
Appendix I

In mid-March 2023, First Republic Bank experienced significant deposit outflows. As a result, the bank turned to other liability sources to meet its funding needs (see fig. 4). These sources included Federal Home Loan Bank (FHLBank) advances and the Federal Reserve's discount window. At the end of the first quarter of 2023, First Republic Bank had doubled the amount of its outstanding FHLBank advances and substantially increased borrowing in all other liability sources compared to the previous quarter.

Figure 4: Funding Composition of First Republic Bank and Peer Banks, Jan. 2022–Mar. 2023, by Quarter



Source: GAO analysis of Federal Financial Institutions Examination Council call report data. | GAO-24-106957

Note: Our analysis compared First Republic Bank with a group of 16 commercial banks (all Federal Home Loan Bank members) with reported domestic deposit balances and total assets between $100 and $250 billion at year-end 2022 in their fourth quarter 2022 Federal Financial Institutions Examination Council call reports.

[a]All other liabilities may include borrowings from Federal Reserve Banks, federal funds, repurchase agreements, and subordinated notes and debentures, among others.

Table 3: Communication and Coordination among FDIC, Federal Reserve Banks, and FHLBanks Surrounding Failures of Silicon Valley Bank, Signature Bank, and First Republic Bank, Mar. 9–12, 2023

Date	Silicon Valley Bank	Signature Bank	First Republic Bank
Thursday, Mar. 9	FHLBSF requested supervisory information from the Federal Reserve Bank of San Francisco, which provided it with high-level information.	No reported activity.	No reported activity.
Friday, Mar. 10	The California Department of Financial Protection and Innovation closed Silicon Valley Bank and appointed FDIC as receiver.	FDIC asked FHLBNY about Signature Bank's FHLBank advances and discussed Signature Bank's overall liquidity position with FHLBNY. FHLBNY, FDIC, and the Federal Reserve Bank of New York met throughout the evening to discuss Signature Bank. In the evening, Signature Bank's custodian bank attempted to transfer securities collateral pledged to FHLBNY to the Federal Reserve discount window, but it was unable to do so. FHLBNY and the Federal Reserve Bank of New York subordinated FHLBNY's interest in certain Signature Bank collateral to the Federal Reserve Bank of New York. FDIC monitored these discussions but did not direct transfers of pledged collateral.	FHLBSF and the Federal Reserve Bank of San Francisco spoke with FDIC about First Republic Bank's deposit and funding needs. FHLBSF and the Federal Reserve Bank of San Francisco scheduled a meeting for March 11 to discuss First Republic Bank's pledged collateral and a potential pledge transfer from FHLBSF to the Federal Reserve Bank. FDIC and FHLBSF held a call to discuss the Silicon Valley Bank failure and potential contagion impact on First Republic Bank.

Date	Silicon Valley Bank	Signature Bank	First Republic Bank
Saturday, Mar. 11	—	FHLBNY and FDIC discussed FHLBNY's actions to support Signature Bank, including collateral available to pledge to the discount window. FHLBNY and the Federal Reserve Bank of New York discussed Signature Bank's status, and FHLBNY instructed its staff to coordinate with the Federal Reserve Bank of New York on their collateral positions. FHLBNY, the Federal Reserve Bank of New York, FDIC, and the New York State Department of Financial Services met throughout the day to assess Signature Bank's liquidity position.	FHLBSF began daily contact with the Federal Reserve Bank of San Francisco and First Republic Bank about their respective interests in loan collateral that First Republic Bank wished to pledge to FHLBSF and the Federal Reserve Bank.
Sunday, Mar. 12	—	FHLBNY and FDIC discussed collateral transfers from FHLBNY to the Federal Reserve Bank of New York to provide additional liquidity to Signature Bank on Monday, March 13. The New York State Department of Financial Services closed Signature Bank and appointed FDIC as receiver.	FHLBSF and the Federal Reserve Bank of San Francisco executed an intercreditor agreement to subordinate FHLBSF's interest in certain First Republic Bank loan collateral to the Federal Reserve Bank. First Republic Bank depledged certain collateral pledged to FHLBSF and pledged the collateral to the Federal Reserve Bank of San Francisco.

Legend: FDIC = Federal Deposit Insurance Corporation; FHLBank = Federal Home Loan Bank; FHLBSF = Federal Home Loan Bank of San Francisco; FHLBNY = Federal Home Loan Bank of New York; — = after failure

Source: GAO analysis of testimonial information and FDIC, Federal Reserve, and FHLBank documentation. | GAO-24-106957

Table 4: Communication and Coordination between FDIC, Federal Reserve Bank of San Francisco, and FHLBSF Surrounding Failure of First Republic Bank, Mar. 17–May 1, 2023

Date	Communication and coordination activities
Friday, Mar. 17	FHLBSF met with FDIC to discuss potential FHLBSF actions to ensure the continued viability of First Republic Bank and FDIC's onsite monitoring. Because the results were not yet published, FDIC could not share additional information about its targeted review of First Republic's retail lending.
Monday, Mar. 20	FHLBSF met with the Federal Reserve Bank of San Francisco to discuss a potential transfer of certain pledged collateral from the Federal Reserve Bank to FHLBSF. FHLBSF and the Federal Reserve Bank discussed potential effects of FHLBSF taking possession of First Republic Bank's loan collateral (a risk mitigation step) on the Federal Reserve Bank's pledging process.
Friday, Mar. 24	First Republic Bank depledged certain collateral from the Federal Reserve Bank and pledged it to FHLBSF.
Thursday, Mar. 30	FHLBSF sent letters requesting that FDIC and the state regulator share information that could affect First Republic Bank's creditworthiness.
Friday, Mar. 31	FHLBSF sent a letter requesting that the Federal Reserve Bank share information that could affect First Republic Bank's creditworthiness.
Monday, Apr. 3	First Republic Bank pledged and depledged certain collateral between FHLBSF and the Federal Reserve Bank.
Thursday, Apr. 6	In response to FHLBSF's March 30 request, FDIC shared its March 31 interim examination letter downgrading First Republic Bank's rating.
Wednesday, Apr. 12	The Federal Reserve Bank responded to FHLBSF's request from March 31 that it had no information to share about the bank's creditworthiness because First Republic Bank was a nonmember.
Friday, Apr. 14	First Republic Bank pledged and depledged certain collateral between FHLBSF and the Federal Reserve Bank.
Thursday, Apr. 20	First Republic Bank depledged certain collateral from FHLBSF and pledged it to the Federal Reserve Bank.
Friday, Apr. 21	First Republic Bank pledged and depledged certain collateral between FHLBSF and the Federal Reserve Bank.
Wednesday, Apr. 26	FDIC and FHLBSF discussed concerns related to First Republic Bank's liquidity position and resolution actions.
Thursday, Apr. 27	First Republic Bank pledged and depledged certain collateral between FHLBSF and the Federal Reserve Bank.
Friday, Apr. 28	First Republic Bank depledged certain collateral from the Federal Reserve Bank and pledged it to FHLBSF.
Saturday, Apr. 29	FDIC informed FHLBSF of its April 28 interim examination letter downgrading First Republic Bank's rating.
Sunday, Apr. 30	FDIC shared with FHLBSF its April 28 interim examination letter downgrading First Republic Bank's rating. Throughout the day, FDIC regularly updated FHLBSF about FDIC's anticipated receivership, the receipt of bids to purchase First Republic Bank, and the bids' potential effects on FHLBSF's credit and collateral position.
Monday, May 1	The California Department of Financial Protection and Innovation closed First Republic Bank and appointed FDIC as receiver, and FDIC announced sale to JPMorgan Chase Bank, National Association.

Legend: FDIC = Federal Deposit Insurance Corporation; FHLBSF = Federal Home Loan Bank of San Francisco

Source: GAO analysis of testimonial information and FDIC, Federal Reserve Bank of San Francisco, and FHLBSF documentation. | GAO-24-106957

Appendix IV: Comments from the Federal Housing Finance Agency

Federal Housing Finance Agency

MEMORANDUM

TO: Jill Naamane, Director, Financial Markets and Community Investment, Government Accountability Office

FROM: Joshua Stallings, Deputy Director, Division of Federal Home Loan Bank Regulation

JOSHUA STALLINGS
Digitally signed by JOSHUA STALLINGS
Date: 2024.02.15 11:04:48 -05'00'

SUBJECT: Draft Report *Federal Home Loan Banks, Actions Related to the Spring 2023 Bank Failures*

DATE: February 15, 2024

Thank you for the opportunity to review and provide technical comments on your draft report, *Federal Home Loan Banks, Actions Related to the Spring 2023 Bank Failures* (Report). The Report discusses the role of the Federal Home Loan Banks (FHLBanks) during the recent bank failures. The Report also provides information on FHLBank advances to member institutions and the pertinent guidance governing their administration should a member institution fail. As the prudential federal regulator of the FHLBanks, the Federal Housing Finance Agency (FHFA) is a critical stakeholder in their operations.

As cited in your Report, FHFA recently published its report on the *FHLBank System at 100: Focusing on the Future* initiative, the Agency's comprehensive review of the FHLBank System in anticipation of the FHLBank System's centennial in 2032. Our report discusses the recent bank failures and a range of other policy issues facing the FHLBank System.

We appreciate the engagement and professionalism of the GAO staff who conducted the review. Please feel free to contact us if you have any questions.

cc: Edward Stolle
John Major

Appendix V: Comments from the Council of Federal Home Loan Banks

FHLBANKS
A NATION OF LOCAL LENDERS

February 14, 2024

Jill Naamane
Director, Financial Markets and Community Investment
U.S. Government Accountability Office
441 G St. N.W. Washington, DC 20548

Dear Director Naamane:

The Council of Federal Home Loan Banks ("Council") welcomes the opportunity to comment on the U.S. Government Accountability Office's ("GAO") draft report GAO-24-106957 "FEDERAL HOME LOAN BANK: Actions Related to the Spring 2023 Bank Failures" dated February 2024 ("GAO Report"). The Council is the trade association for the Federal Home Loan Bank System ("FHLBank System"), which is composed of the eleven Federal Home Loan Banks ("FHLBanks") and the Office of Finance. The Council represents the public policy views of the FHLBank System in Washington.

The Council has reviewed the GAO Report and believes it provides a fact-based account of the role of the FHLBanks in the period up to and during the failures of Silicon Valley Bank ("SVB"), Signature Bank ("Signature"), and First Republic Bank ("First Republic") in March 2023. The GAO Report shows how the FHLBanks provide critical advances to their members during times of financial duress but also carefully manage their exposures and coordinate with the Federal Reserve System ("Federal Reserve") and the Federal Deposit Insurance Corporation ("FDIC") with respect to troubled banks. The GAO Report highlights how the FHLBank of San Francisco managed its exposures to two of the banks in the run up to their failures as part of their risk management protocols, although in light of the very quick failure of SVB, the FHLB of San Francisco could not fully implement its risk management protocols for SVB. Since the Signature Bank run occurred so quickly on the afternoon of March 10th, there was no time for the FHLBank of New York credit escalation standards to be applied. The GAO Report noted this and correctly reported that post failure, as requested by the FDIC, the FHLBank of New York continued to reliably renew advances to assist the FDIC Signature receiver in meeting its liquidity needs to help facilitate a low-cost resolution through July 2023. Finally, as the GAO Report notes, federal banking agencies have not identified the proportion of FHLBank advances to total assets as being a specific concern about the safety and soundness for SVB, Signature, or First Republic.

The GAO Report correctly describes how the FHLBanks of San Francisco and New York worked closely with the Federal Reserve, the FDIC and the state banking regulators of SVB, Signature, and First Republic, as well with the Federal Housing Finance Agency (which regulates the FHLBank System), as the three banks' conditions deteriorated. In particular, the FHLBanks of New York and San Francisco sought to facilitate efforts (ultimately unsuccessful) by the Federal Reserve Banks of

1800 M Street, NW, Suite 400S
Washington, DC 20036

www.fhlbanks.com
202-955-0002

New York and San Francisco to provide discount window lending. At the same time, the FHLBanks increased their overall provision of liquidity to FHLBank members as markets tightened in reaction to the failure of the three banks. The FHLBank System and federal banking agencies have important, but distinct, statutory roles and the GAO Report underscores how important it is for them to maintain and strengthen their working relationship.

The GAO Report also shows how the FHLBanks serve their members by providing liquidity quickly and efficiently and without putting U.S. taxpayers at risk. At the end of the first quarter of 2023, more than 3,600 FHLBank members had advances outstanding helping them through the tightening of market liquidity. Importantly, the GAO Report points out that FHLBank members include not only commercial banks and savings institutions, but also credit unions, insurance companies, and community development financial institution. The advances the FHLBanks provided these financial institutions in exchange for mortgage-backed collateral during the financial stress of early 2023 demonstrated the continued reliability of the FHLBank System. It is the FHLBank System's statutory mission to be the reliable source of mortgage liquidity for FHLBank members. Since its establishment by Congress, the FHLBank System has consistently upheld this statutory mission. In doing so, the FHLBank System has not only enhanced the liquidity of the mortgage market, but also reduced the costs of housing finance for American households and strengthen the resilience of the U.S. financial system.

The Council appreciates the GAO's careful review of the actions of the FHLBanks in the period up to and during the failure of the three banks in March 2023 and its engagement with the Council as it produced its report. If we can be of additional help as the GAO finalizes the report, we would welcome the opportunity.

Sincerely,

Ryan Donovan
President and CEO

Endnotes

[1]GAO, *Bank Regulation: Preliminary Review of Agency Actions Related to March 2023 Bank Failures*, GAO-23-106736 (Washington, D.C.: Apr. 28, 2023). GAO is also conducting work on other topics related to the bank failures.

[2]Each FHLBank is cooperatively owned by its members, which may include banks, thrifts, credit unions, insurance companies, and community development financial institutions.

[3]Other advance types include hybrid advances, convertible advances, and overnight advances. Advances may have callable, convertible, or putable features, meaning, respectively, that the member may repay an advance ahead of schedule on specific dates without prepayment penalties, the member may convert the advance from floating-to fixed-rate or vice versa, or the FHLBank may require the member to repay the outstanding advance.

[4]Federal Housing Finance Agency, *Report on Collateral Pledged to Federal Home Loan Banks* (Washington, D.C.: Dec. 15, 2023).

[5]The scope for our review with respect to bank regulation and supervision was the federal banking regulators. We generally excluded the actions of state regulators, which also had regulatory and supervisory responsibilities over the failed banks.

[6]Members may also obtain letters of credit from FHLBanks—the notional amount of which must also be secured with pledged collateral—that allow them to attract lending from third parties at a lower cost.

[7]This stock is not publicly traded and is issued, redeemed, and repurchased at par value by each FHLBank.

[8]The Office of Finance is a joint office of the FHLBanks that facilitates the issuance and servicing of the FHLBanks' consolidated obligations (debt instruments that serve as the FHLBanks' primary source of funds and allow them to provide advances). Consolidated obligations are the joint and several liability of the FHLBanks collectively.

[9]Our analysis compared SVB, Signature Bank, and First Republic Bank with a group of 16 commercial banks. All of these banks were FHLBank members and reported domestic deposit balances and total assets between $100 and $250 billion at year-end 2022 in their fourth quarter 2022 Federal Financial Institutions Examination Council (FFIEC) call reports. We began our analysis in January 2022 to capture increases in FHLBank advance borrowing related to Federal Reserve interest rate increases that began in March 2022. In the 2 prior years, commercial banks had excess liquidity due to pandemic assistance programs and relied less on loans, including FHLBank advances. At the end of both 2020 and 2021, the FHLBank System recorded lower year-end outstanding advance balances than in the prior year.

[10]The discount window allows eligible institutions to borrow money, usually on a short-term basis, at an above-market rate to meet temporary liquidity shortages. The repurchase agreement, or repo, market is a short-term market that provides financing for securitization activities and financial institutions.

[11]Uninsured deposits reported on FFIEC call reports are the estimated amount of the bank's deposits (in domestic offices and in insured branches in Puerto Rico and U.S. territories and possessions) that is not covered by federal deposit insurance. The standard maximum deposit insurance amount is $250,000. 12 U.S.C. § 1821(a)(1)(E). Deposit insurance is administered by FDIC consistent with 12 C.F.R. part 330.

[12]GAO-23-106736.

[13]Liquidity stress tests identify and quantify potential risks and analyze the possible effects on the institution's liquidity, such as the ability of the bank to access FHLBank advances. Contingency funding plans identify alternate funding sources if a bank's financial condition or the economy deteriorates.

[14]Demand for FHLBank advances increased across the system in March 2023 in response to banking sector volatility caused by the SVB and Signature Bank failures. The elevated advance demand that month exceeded previous financial market disruptions, with total advances outstanding rising to about $1 trillion. See Federal Housing Finance Agency, *2022 Report to Congress* (Washington, D.C.: June 15, 2023).

[15]FHLBNY officials said they heightened their review of Signature Bank's portfolio starting in November 2022 after FTX, a digital asset exchange, went bankrupt. Silvergate Bank, which served FTX and other cryptocurrency companies, experienced significant deposit outflows after FTX's collapse. Signature Bank similarly had a significant volume of crypto-related deposits (although it did not hold cryptocurrency assets). Following FTX's collapse, Signature Bank increased its FHLBank advance usage to help cover short-term liquidity gaps and indicated it would slowly reduce its reliance on these advances over the course of 2023, according to FHLBNY officials.

[16]FHFA has interpreted its regulations to permit an FHLBank to consider a bridge bank as continuing the membership of a failed member. FHFA Regulatory Interpretation 2010-RI-04.

[17]12 U.S.C. § 1442(a).

[18]12 C.F.R. § 1266.4(e)(2).

[19]The banking regulators receive quarterly FFIEC call report information on banks' FHLBank advance borrowing. In addition, certain banking organizations under Federal Reserve supervision—including domestic bank holding companies with $100 billion or more in assets—must submit a Complex Institution Liquidity Monitoring Report (Form FR2052a) on at least a monthly basis. The report collects quantitative information on selected assets, liabilities, funding activities, and contingent liabilities. Such information would include details on the amounts and maturity categories of any outstanding FHLBank loans and on available FHLBank borrowing capacity.

[20]12 C.F.R. § 1266.4 provides for cases in which a federal banking regulator can intervene in FHLBanks' credit decisions. For example, a regulator can request in writing that an FHLBank make a new advance to a member without positive tangible capital, and it can prohibit advances to a capital-deficient member with positive tangible capital by notifying the FHLBank in writing.

[21]In a November 2023 review of the FHLBank System's response to the broad liquidity needs of spring 2023, FHFA found that some of the 11 FHLBanks did not have agreements to facilitate collateral pledges and transfers between the FHLBanks and the Federal Reserve Banks. In its report, FHFA reported that the FHLBanks had taken steps to draft such agreements. See Federal Housing Finance Agency, *FHLBank System at 100: Focusing on the Future* (Washington, D.C.: Nov. 7, 2023).

[22]FHLBank members are typically overcollateralized, meaning they have more collateral pledged to the FHLBank than is needed to secure their existing advances. They then have this collateral available to transfer to their district Federal Reserve Bank for discount window borrowing.

[23]Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, National Credit Union Administration, and Office of the Comptroller of the Currency, *Addendum to the Interagency Policy Statement on Funding and Liquidity Risk Management: Importance of Contingency Funding Plans* (July 28, 2023).

[24]On March 13 (the day after Signature Bank's failure), FHLBNY subordinated its interest in nearly $11.5 billion in securities collateral and approximately $6.9 billion in loan collateral to the Federal Reserve Bank of New York on behalf of Signature Bridge Bank. It did so to facilitate the bridge bank's access to the discount window.

[25]FDIC is required to be appointed as receiver for any institution chartered under federal law, is permitted to be appointed as a receiver of state-chartered institutions when appointed under state law, and is required to be appointed as receiver where the appointment is made pursuant to federal law. FDIC may also appoint itself as a receiver of a state-chartered insured institution in certain circumstances. 12 U.S.C. § 1821(c).

[26]A perfected security interest provides a lender or other secured party with rights in the collateral that are superior to certain other creditors. FHLBanks are entitled to priority over the claims and rights of any party (including any receiver, conservator, trustee, or similar party having rights of a lien creditor) other than claims and rights that (i) would be entitled to priority under otherwise applicable law, and (ii) are held by actual bona fide purchasers for value or by actual secured parties that are secured by actual perfected security interests. 12 U.S.C. § 1430(e), 12 C.F.R. § 360.2(a).

[27]12 U.S.C. § 1823(c)(4). If the systemic risk exception is invoked, the "least cost" method does not need to be followed. 12 U.S.C. § 1823(c)(4)(G). The Secretary of the Treasury (in consultation with the President), on the recommendation of FDIC and the Federal Reserve Board, invoked the systemic risk exception for SVB and Signature Bank, which authorized FDIC to guarantee all deposits—both insured and uninsured—of the two banks. This exception was not invoked for First Republic Bank. FDIC is required to collect one or more special assessments to recover the loss to the Deposit Insurance Fund arising from the use of a systemic risk exception from insured depository institutions, depository institution holding companies, or both, as FDIC determines appropriate. 12 U.S.C. § 1823(c)(4)(G)(ii)(I). The Deposit Insurance Fund insures deposits and protects depositors of FDIC-insured banks and helps fund resolution activities of FDIC when banks fail. The fund is primarily funded by assessments paid by FDIC-insured institutions and interest earned on the investment funds.

[28]12 C.F.R. § 360.2(c).

[29]12 C.F.R. § 1266.6(b). *See also* 12 C.F.R. § 360.2(e) (allowing FHLBank's collection of prepayment fees if certain conditions are met).

[30]As described above, if the systemic risk exception is invoked, FDIC is authorized to guarantee all deposits, both insured and uninsured. However, one or more special assessments will be collected by FDIC to recover the loss to the Deposit Insurance Fund. 12 U.S.C. § 1823(c)(4)(G)(ii)(I).

[31]The FHLBanks in our review stated that by providing liquidity, FHLBanks may help FDIC achieve an orderly resolution and minimize the effects of bank failures on the Deposit Insurance Fund.

[32]Dusan Stojanovic, Mark D. Vaughan, and Timothy J. Yeager, “Is Federal Home Loan Bank Funding a Risky Business for the FDIC?” *Federal Reserve Bank of St. Louis Regional Economist* (Oct. 1, 2000); Rosalind L. Bennett, Mark D. Vaughan, and Timothy J. Yeager, “Should the FDIC Worry about the FHLB? The Impact of Federal Home Loan Bank Advances on the Bank Insurance Fund” (Federal Deposit Insurance Corporation Center for Financial Research Working Paper No. 2005-10, July 2005).

[33]See Federal Housing Finance Agency, *FHLBank System at 100*. Moral hazard, in this case, is the risk that certain protections afforded to the FHLBank System might create incentives for the FHLBanks to extend more credit than is financially prudent, or to extend credit in a manner that presents risks to the broader financial system.

[34]Damien Moore et al., *The Federal Home Loan Banks Support Systemic Stability* (Urban Institute, Nov. 3, 2023).

[35]The 2023 data did not include SVB and Signature Bank because they failed before the end of the first quarter and did not submit call reports.

[36]GAO, *Standards for Internal Control in the Federal Government*, GAO-14-704G (Washington, D.C.: Sept. 10, 2014).

[37]Federal Housing Finance Agency, *FHLBank System at 100*.