



CDFA Lends Support to Federal Home Loan Bank (FHLB) Letter of Credit Legislation for Tax-exempt Bonds

As part of CDFA's legislative agenda, the Council routinely monitors legislative activity on Capitol Hill. CDFA has been following two bills, H.R. 2091 (introduced by Rep Levin, D-MI and Rep. English, R-PA) and S. 1963 (introduced by Sen. Rockefeller, D-WV, and Sen. Crapo, R-ID). CDFA has agreed to sign-on as supporters of this important legislation. This bill will:

- Help local communities raise funds for water treatment facilities, bridges and other infrastructure improvements, industrial development, healthcare facilities, fire stations, parking facilities, long-term care for the elderly, schools and other important activities.
- Allow FHLBank member banks to assist these issuers by offering FHLBank LOCs without triggering the loss of the bonds' tax-exempt status. Obtaining a performance guarantee from a Triple A rated entity, such as the FHLBanks, further lowers costs for communities.
- Not transfer risk to the federal government nor provide a double subsidy of tax-exempt bonds. FHLBanks are privately owned financial institutions whose obligations are explicitly not guaranteed by the United States. The credit markets independently rate the obligations of the FHLBank letters of credit on objective criteria assessing the financial strength of each FHLBank.
- Amend Section 149 of the Internal Revenue Code (IRC) to add FHLBanks to the list of GSEs that can credit enhance tax-exempt municipal, industrial development and other private activity bonds. Fannie Mae, Freddie Mac, Ginnie Mae, FHA, and VA have been permitted since 1984 under the IRC to provide credit support. At that time, FHLBanks did not offer letters of Credit (LOCs) for tax-exempt bonds. Now they do – for tax-exempt housing bonds (in addition to taxable bonds).

This legislation change should not significantly reduce Federal budget receipts. It was scored by staff of the Joint Committee on Taxation in 1997 at \$6 million over 5 years and \$20 million over 10 years. The provision was in the Senate-passed version of H.R. 2014, the Revenue Reconciliation Act of 1997 and dropped in conference.

- FHLBank LOCs give local banks the opportunity to compete for this business and serve their communities. FHLBank LOCs will increase competition, helping to ensure the best cost for municipal governments and their taxpayers. Community banks within the FHLB System are well suited to underwrite the credit for such projects since this is an essential aspect of the business of community banking.
- The legislation is needed to support communities and small issuers that are currently underserved by bond insurers. This will increase competition, helping to ensure the best cost for municipal governments and their taxpayers.
- If this legislation passes, the standby letters of credit issued by community banks and supported by FHLBanks would go primarily towards modest projects such as small local colleges, health care facilities, small manufacturers and other private activity bonds issued by small local governments.