

Letters of Credit

- Credit Enhancement for Bonds
- Performance Guarantees
- Public Unit Deposits

Benefits to Members

The Federal Home Loan Bank of Chicago (FHLBC) offers irrevocable letters of credit (LOCs) that provide members a low-cost and efficient way to attract and secure agreements with third parties.

Using a letter of credit from the FHLBC allows members to leverage our Aaa/AA+ rating at a competitive price in order to retain and grow their local customer relationships. In addition, LOCs:

- **Provide liquidity by serving as an alternative form of collateral;**
- **Help members manage month-to-month deposit fluctuations;**
- **Improve bond-related transaction costs;**
- **Allow smaller members to compete with larger, rated banks and grow fee income; and**
- **Provide project financing opportunities that support community economic development and affordable housing projects.**

Members use LOCs for a variety of purposes, including:

- Residential housing finance;
- Community lending;
- Asset liability; and
- Liquidity.

Types of Letters of Credit

The FHLBC offers standby/confirming letters of credit that can be used to secure public unit deposits, provide performance guarantees, and credit enhance tax-exempt or taxable bond financings. We also offer direct pay letters of credit in connection with bond financings.

Standby/Confirming: A standby or confirming LOC is a financial instrument issued by the FHLBC that provides recourse in the event a member defaults under its contractual obligations with a third party. The FHLBC will issue a standby LOC directly on behalf of a member's account with a third party or to confirm a member's guarantee of its customer's performance. The member is first to pay under a draw request. The FHLBC letter of credit is drawn on in the event that the member does not perform.

Direct Pay: Under a direct pay LOC, the FHLBC provides the primary payment mechanism. The FHLBC makes the principal and interest payments to satisfy the member's obligations. The member reimburses the FHLBC under the terms of a reimbursement agreement and then seeks reimbursement from the borrower.

Getting Started is Easy

Completing the application is straightforward, and the FHLBC staff is available to guide you through the process. In addition, forms are available on our members-only website, eBanking.

Credit Enhancement for Bond Financings

Your customer may need an LOC from a rated bank to arrange financing for a housing or community economic development project with proceeds from a bond issuance. Members that are unrated, or that have less than an Aaa or AA+ rating, may retain their customer relationships by requesting an FHLBC confirming/standby or direct pay LOC, which will guarantee the principal and interest payments to bondholders and credit enhance the bonds with its Aaa/AA+ rating. Direct pay LOCs issued by the FHLBC also accommodate multi-member participation structures.

The FHLBC offers support for taxable and tax-exempt bond financing for housing projects and for taxable bonds for community economic development activities.

Proceeds from the bond issuance can help finance a range of projects, including:

- **Housing developments;**
- **Healthcare facilities;**
- **Schools and universities; and**
- **Manufacturing plants.**

Members can benefit from discounted pricing on projects eligible under our Community Investment Cash Advance (CICA) Program. All non-housing projects must be CICA-qualified in order to obtain an FHLBC LOC.

How does the FHLBC credit enhancement work?

- The FHLBC member works with the borrower and underwriters to determine project feasibility and terms of bond financing.
- In most cases, the FHLBC issues a confirming LOC in support of a member's LOC, under which the FHLBC promises to make payments for the benefit of the bondholders if the member does not pay under its LOC. Alternatively, the FHLBC also offers direct pay LOCs under which the FHLBC provides the primary payment mechanism on the bonds.
- Bonds are issued with the FHLBC rating, which increases the marketability of the bonds and reduces the financing costs.

Standby LOCs for Performance Guarantees

Does MasterCard, VISA, or American Express require an LOC to guarantee payments on your credit card processing account? Do you need an LOC from a rated bank to stand behind your guarantee of a customer's lease payments or performance under a construction contract?

The FHLBC offers standby LOCs issued directly on behalf of a member's account or to confirm a member's guarantee of its customer's performance.

LOC guarantees may include:

- **Credit card processing accounts;**
- **Construction projects;**
- **Insurance payments;**
- **Workers' compensation and insurance premiums;**
- **Working capital guarantees; and**
- **Lease payments.**

How Insurance Companies Use LOCs

The FHLBC is registered with the National Association of Insurance Commissioners (NAIC). Insurance companies that are members of the FHLBC use standby LOCs in a variety of situations, including:

- As a security deposit for leasing space.
- In court. If an insurance claim is filed in court and a judgment is rendered against the insurance company, the insurance company can post the judgment amount or an appeal bond in the form of an LOC.
- Reinsurance. Insurance companies may syndicate their exposures, which may require tangible collateral to be pledged to the reinsurer. An LOC can be used for this purpose.

Standby LOCs to Secure Public Unit Deposits

Your municipal clients provide a valuable deposit business. To retain your securities for liquidity and other purposes and to attract public unit deposits that exceed the amount covered by FDIC insurance, you can use a low-cost FHLBC standby LOC for public unit deposits (PUD LOC) to collateralize a public entity's deposits.

For public unit deposit accounts that frequently fluctuate, members can now request the Fluctuating Balance PUD LOC for amounts of \$10 million or more. The FHLBC can issue Fluctuating Balance PUD LOCs for the benefit of a single public unit depositor or to a third-party trustee as beneficiary for multiple public unit depositors. Alternatively, the FHLBC can issue PUD LOCs for one-month terms to manage fluctuations.

The PUD LOC is acceptable collateral under both Illinois and Wisconsin law, although the depositor's legal counsel must confirm eligibility. The FHLBC's Law Department has produced a short document called "Information Regarding Using FHLBC Letters of Credit to Back Public Unit Deposits" that members can share with their depositors' legal counsel to make understanding and executing an LOC as easy as possible.

Members can use a standby LOC to collateralize deposits from many public entities, including:

- **Local government: city, county, township;**
- **State government and state agencies;**
- **Transportation authorities;**
- **Housing authorities;**
- **Water reclamation districts; and**
- **Public school districts and community colleges.**

Benefits to the Public Entity

The benefits of a PUD LOC from the Federal Home Loan Bank of Chicago to a public agency include:

- **Immediate payout.** In the unlikely event of a default, the FHLBC pays out under the LOC immediately; there is no delay with selling securities in the market to make payment.
- **Convenient.** The FHLBC can issue a standard PUD within 24 hours and, in many circumstances, within several hours.
- **Secure and irrevocable.** The LOC carries the FHLBC's Aaa/AA+ rating.

For More Information

If you have any questions about the Federal Home Loan Bank of Chicago's LOCs, or if you would like a copy of the document from the FHLBC's Law Department called "Information Regarding Using FHLBC Letters of Credit to Back Public Unit Deposits" to share with your public agency customers, please contact the Member Transaction Desk at 877-230-1610 or your sales coverage team.

Visit our website at www.fhlbc.com.

LOC General Terms and Conditions

All terms and conditions below are subject to review and change. Additional terms and conditions may apply.

Maximum Term: 10 years.

Maximum or Minimum: For most LOCs, there is no maximum or minimum amount requirement. Fluctuating Balance PUD LOCs are available in minimum amounts of \$10 million.

Irrevocable: FHLBC letters of credit are irrevocable.

Collateral: FHLBC letters of credit must be fully collateralized at the time of issuance in the same manner as advances. Refer to the Member Products and Credit Policy.

Stock: There is no capital stock purchase requirement at issuance of a FHLBC letter of credit. In general, the FHLBC does not anticipate its standby letters of credit being drawn upon. In the event that a draw does occur under a standby or direct pay letter of credit and the member does not immediately reimburse the FHLBC for the draw, an advance will be made. Any required capital stock purchases will be calculated at the time an advance is made.

Documentation: The member must complete an application and reimbursement agreement. If applicable, a copy of the member's underlying letter of credit must be provided prior to the issuance of the FHLBC letter of credit. For credit enhancements of bond financings, additional documentation will be required prior to closing.

CICA Eligibility: Discounted pricing is offered for housing and community lending projects eligible under our Community Investment Cash Advance (CICA) program. All community lending (non-housing) projects must be CICA-qualified in order to obtain an FHLBC letter of credit.

Fees: Fees are paid annually in advance, calculated on an actual/360 basis, for most FHLBC LOCs. For Fluctuating Balance PUD LOCs, a minimum fee on 50% of the amount of the LOC is paid annually in advance, calculated on an actual/360 basis, with additional fees based on the average daily balance of the deposit accounts as reported by the member paid quarterly and at the expiration of the LOC.

Additional fees may apply. Fees are assessed for drafts on FHLBC letters of credit. Members incur the associated legal and documentation costs for a FHLBC letter of credit to credit enhance a bond financing and any other non-standard FHLBC letter of credit. Please refer to our Letter of Credit Fee Schedule and the Member Products and Credit Policy for additional information.

Renewal: FHLBC letters of credit must contain a specific expiration date or be for a definite term. Evergreen provisions where FHLBC has the option to renew are permissible as long as there is a stated final maturity date.

Transferable: FHLBC letters of credit are only transferable with prior written consent from the FHLBC.

Cancellation: LOCs may be terminated prior to their stated maturity upon written notification from the Beneficiary and receipt of the cancelled original letter of credit.

Questions? Please contact your Institutional Sales Director or the Member Transaction Desk at 877-230-1610.