Leveraging Letters of Credit for Public Unit Deposits

Your state and local agency clients provide you with a valuable source of 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 low-cost Federal Home Loan Bank of Chicago (FHLBC) standby letters of credit for public unit deposits (PUD LOCs) to collateralize a public entity’s deposits.

For public unit deposit accounts that frequently fluctuate, members can now opt to use Fluctuating Balance PUD LOCs 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, some members may prefer to use one-month term PUD LOCs to manage such fluctuations.

Benefits of Using PUD LOCs

- **Enhance your liquidity position** by keeping securities unencumbered
- **Improve net interest margins** by using deposits to fund loans or higher-yielding investments
- **Collateralize** deposits using current loan assets pledged to FHLBC
- **Reduce costs** associated with pledging and releasing pledges that collateralize deposits
- **Eliminate** the need to monitor margin calls with a more efficient collateralization process
- **Preference**: A public agency may prefer a PUD LOC versus pledged securities.
- **Immediate payout**: In the unlikely event of a default, the FHLBC pays out under the PUD LOC immediately; there is no delay from selling securities in the market to receive payment.
- **Convenience**: The FHLBC can typically issue a standard PUD LOC within 24 hours.
- **Secure**: PUD LOCs from the FHLBC are rated Aaa/AA+, the same rating as the U.S. government.

Collaboration Pays Off

PUD LOCs are the result of a collaboration among the FHLBC, its members, and public agency depositors. Your depositor can request a PUD LOC in which they are named as beneficiary. By using the FHLBC letter of credit, you guarantee your customers’ deposits and support our cooperative which contributes both directly and indirectly to the communities you serve – through the competitively priced funding you employ as well as backing for the affordable housing and community development in the district.
Members can use a standby LOC to collateralize deposits from various public entities, including:

- Municipalities
- State Treasurers
- Regional Transportation Authorities
- Water Reclamation Districts
- Housing Authorities
- Community Colleges
- Public School Districts
- Hospitals
- Public Libraries

How to Get Started

Securing PUD LOCs from the FHLBC is as easy as filling out an application on eBanking, our members-only website.

We can work with you to provide materials and participate in presentations and other efforts with your customers to help them understand the benefits of working with FHLBC letters of credit.

Should you need more information about PUD LOCs or have questions regarding pricing, please contact the Member Transaction Desk at 855-FHLB-CHI (855-345-2244) or your sales coverage. Additional information is available at our website: www.fhlbc.com.

Alternatively, you can contact LOC Product Manager Carol Dimitrakopoulos at 312-565-5843 or cdimitrak@fhlbc.com.

PUD LOCs Under Illinois and Wisconsin Statutes

The question of whether a particular public agency may accept an FHLBC letter of credit to secure its deposits is generally considered to be a matter of state law.

Illinois Law

In Illinois, the Public Funds Investment Act provides that: "Whenever a public agency deposits any public funds in a financial institution, the public agency may enter into an agreement with the financial institution requiring any funds not insured by the Federal Deposit Insurance Corporation...to be collateralized by any of the following classes of securities * * * letters of credit issued by a Federal Home Loan Bank..."  

The same statute defines “public agency” to mean: “...the State of Illinois, the various counties, townships, cities, towns, villages, school districts, educational service regions, special road districts, public water supply districts, fire protection districts, drainage districts, levee districts, sewer districts, housing authorities, the Illinois Bank Examiners’ Education Foundation, the Chicago Park District, and all other political corporations or subdivisions of the State of Illinois, now or hereafter created, whether herein specifically mentioned or not.”

Wisconsin Law

In Wisconsin, the state statute addressing public deposits provides that: [a] surety bond or other security may be required of or given by any public depository for any public deposits that exceed the amount of deposit insurance provided by an agency of the United States and the coverage provided under s. 34.08(2).  

“Public deposits” is defined as “public moneys deposited by a public depository in a public depository, including private moneys held in trust by a public officer.” “Public depository” means “any state or county, city, village, town, drainage district, power district, school district, cooperative educational services agency, sewer district, or any commission, committee, board or any governmental subdivision of the state or any court of this state...”

While the Public Deposits chapter does not define what constitutes a security for purposes of Section 34.07, several other unrelated sections of the Wisconsin state statutes identify letters of credit as an acceptable form of security and may provide some guidance.

1 30 ILCS 235/1 et seq.  
2 30 ILCS 235/6(d)(9)(iii)  
3 30 ILCS 235/1  
4 Wis. Stats. 34.01 et seq.  
5 Wis. Stats. 34.07  
6 Wis. Stats. §34.01(3)  
7 Wis. Stats. §34.01(4)  
8 See, Wis. Stats. 126.16 (“form of security...an irrevocable bank letter of credit”); Wis. Stats. 99.03 (“form of security...an irrevocable bank letter of credit”)  

* This information has been provided as a courtesy by the Federal Home Loan Bank of Chicago and is believed to be accurate. It does not constitute legal advice. Please consult your own legal advisor regarding the information presented here.