UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

# FORM 10-Q

☒ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the quarterly period ended March 31, 2016**

**OR**

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
**For the transition period from            to**

**Commission File No. 000-51401**

FHLB Chicago

Federal Home Loan Bank of Chicago
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| **Federally chartered corporation** | **36-6001019** |
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |
| **200 East Randolph Drive Chicago, IL** | **60601** |
| (Address of principal executive offices) | (Zip Code) |

Registrant's telephone number, including area code: **(312) 565-5700**

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☒ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one)

| | |
|---|---|
| Large accelerated filer ☐ | Accelerated filer ☐ |
| Non-accelerated filer ☒ (Do not check if a smaller reporting company) | Smaller reporting company ☐ |

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒

As of April 30, 2016, including mandatorily redeemable capital stock, registrant had 20,326,577 total outstanding shares of Class B Capital Stock.

FHLB Chicago

Federal Home Loan Bank of Chicago

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**PART I - FINANCIAL INFORMATION**
**Item 1. Financial Statements.**
**Statements of Condition (unaudited)**
(Dollars in millions, except capital stock par value)

| | March 31, 2016 | December 31, 2015 |
|---|---|---|
| **Assets** | | |
| Cash and due from banks | $ 33 | $ 499 |
| Interest bearing deposits | 650 | 650 |
| Federal Funds sold | 3,610 | 1,702 |
| Securities purchased under agreements to resell | 250 | 1,375 |
| **Investment securities -** | | |
| Trading, $103 and $62 pledged | 1,156 | 1,160 |
| Available-for-sale | 16,742 | 17,470 |
| Held-to-maturity, $5,741 and $6,513 fair value | 5,189 | 5,967 |
| **Investment securities** | 23,087 | 24,597 |
| Advances, $605 and $511 carried at fair value | 38,353 | 36,778 |
| MPF Loans held in portfolio, net of allowance for credit losses of $(2) and $(3) | 4,679 | 4,828 |
| Derivative assets | 3 | 2 |
| Other assets | 248 | 240 |
| **Assets** | $ 70,913 | $ 70,671 |
| | | |
| **Liabilities** | | |
| **Deposits -** | | |
| Noninterest bearing | $ 44 | $ 41 |
| Interest bearing, $17 and $12 from other FHLBs | 454 | 497 |
| **Deposits** | 498 | 538 |
| **Consolidated obligations, net -** | | |
| Discount notes, $2,237 and $9,006 carried at fair value | 40,293 | 41,564 |
| Bonds, $3,811 and $952 carried at fair value | 24,021 | 22,582 |
| **Consolidated obligations, net** | 64,314 | 64,146 |
| Derivative liabilities | 60 | 55 |
| Affordable Housing Program assessment payable | 90 | 89 |
| Mandatorily redeemable capital stock | 302 | 8 |
| Other liabilities | 292 | 239 |
| Subordinated notes | 944 | 944 |
| **Liabilities** | 66,500 | 66,019 |
| Commitments and contingencies - see notes to the financial statements | | |
| **Capital** | | |
| Class B1 activity stock - putable $100 par value - 10 million and 13 million shares issued and outstanding | 1,050 | 1,313 |
| Class B2 membership stock - putable $100 par value - 7 million and 6 million shares issued and outstanding | 683 | 637 |
| **Capital stock** | 1,733 | 1,950 |
| Retained earnings - unrestricted | 2,453 | 2,407 |
| Retained earnings - restricted | 337 | 323 |
| **Retained earnings** | 2,790 | 2,730 |
| Accumulated other comprehensive income (loss) (AOCI) | (110) | (28) |
| **Capital** | 4,413 | 4,652 |
| **Liabilities and capital** | $ 70,913 | $ 70,671 |

The accompanying notes are an integral part of these financial statements (unaudited).

FHLB Chicago

Federal Home Loan Bank of Chicago

**Statements of Income (unaudited)**
(Dollars in millions)

| | Three months ended March 31, | |
|---|---|---|
| | **2016** | 2015 |
| Interest income | **$ 318** | $ 321 |
| Interest expense | **198** | 191 |
| **Net interest income** | **120** | 130 |
| | | |
| **Noninterest gain (loss) on -** | | |
| Trading securities | **1** | (1) |
| Derivatives and hedging activities | **(16)** | (11) |
| Instruments held under fair value option | **5** | 3 |
| Other, net | **7** | 4 |
| **Noninterest gain (loss)** | **(3)** | (5) |
| | | |
| **Noninterest expense -** | | |
| Compensation and benefits | **23** | 19 |
| Other operating expenses | **15** | 11 |
| Other | **2** | 3 |
| **Noninterest expense** | **40** | 33 |
| | | |
| **Income before assessments** | **77** | 92 |
| | | |
| Affordable Housing Program assessment | **8** | 9 |
| | | |
| **Net income** | **$ 69** | $ 83 |

The accompanying notes are an integral part of these financial statements (unaudited).

FHLB Chicago

Federal Home Loan Bank of Chicago

**Statements of Comprehensive Income (unaudited)**
(Dollars in millions)

| | Three months ended March 31, | |
|---|---|---|
| | **2016** | 2015 |
| **Net income** | **$ 69** | $ 83 |
| | | |
| **Other comprehensive income (loss) -** | | |
| Net unrealized gain (loss) available-for-sale securities | **(40)** | (22) |
| Non-credit OTTI held-to-maturity securities | **11** | 13 |
| Net unrealized gain (loss) cash flow hedges | **(53)** | (28) |
| Post-retirement plans | **—** | (8) |
| **Other comprehensive income (loss)** | **(82)** | (45) |
| | | |
| **Comprehensive income** | **$ (13)** | $ 38 |

The accompanying notes are an integral part of these financial statements (unaudited).

**Statements of Capital (unaudited)**
(Dollars and shares in millions)

| | Capital Stock - Putable - B1 Activity | | Capital Stock - Putable - B2 Membership | | Capital Stock | | Retained Earnings | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | Shares | Value | Shares | Value | Shares | Value | Unrestricted | Restricted | Total | AOCI | Capital |
| **December 31, 2015** | **13** | **$1,313** | **6** | **$ 637** | **19** | **$1,950** | **$ 2,407** | **$ 323** | **$2,730** | **$ (28)** | **$ 4,652** |
| Comprehensive income | | | | | | | **55** | **14** | **69** | **(82)** | **(13)** |
| Proceeds from issuance of capital stock | **2** | **183** | **—** | **1** | **2** | **184** | | | | | **184** |
| Repurchases of capital stock | **(1)** | **(104)** | **—** | **(3)** | **(1)** | **(107)** | | | | | **(107)** |
| Capital stock reclassified to mandatorily redeemable capital stock | **(3)** | **(294)** | **—** | **—** | **(3)** | **(294)** | | | | | **(294)** |
| Transfers between classes of capital stock | **(1)** | **(48)** | **1** | **48** | | | | | | | |
| Cash dividends - class B1 (2.60% annualized rate) | | | | | | | **(8)** | | **(8)** | | **(8)** |
| Cash dividends - class B2 (0.60% annualized rate) | | | | | | | **(1)** | | **(1)** | | **(1)** |
| **March 31, 2016** | **10** | **$1,050** | **7** | **$ 683** | **17** | **$1,733** | **$ 2,453** | **$ 337** | **$2,790** | **$(110)** | **$ 4,413** |
| | | | | | | | | | | | |
| December 31, 2014 | 8 | $ 827 | 11 | $1,075 | 19 | $1,902 | $ 2,152 | $ 254 | $2,406 | $ 217 | $ 4,525 |
| Comprehensive income | | | | | | | 67 | 16 | 83 | (45) | 38 |
| Proceeds from issuance of capital stock | — | 32 | — | 6 | — | 38 | | | | | 38 |
| Repurchases of capital stock | — | (1) | — | (16) | — | (17) | | | | | (17) |
| Transfers between classes of capital stock | — | (31) | — | 31 | | | | | | | |
| Cash dividends - class B1 (2.25% annualized rate) | | | | | | | (4) | | (4) | | (4) |
| Cash dividends - class B2 (0.50% annualized rate) | | | | | | | (1) | | (1) | | (1) |
| March 31, 2015 | 8 | $ 827 | 11 | $1,096 | 19 | $1,923 | $ 2,214 | $ 270 | $2,484 | $ 172 | $ 4,579 |

The accompanying notes are an integral part of these financial statements (unaudited).

FHLB Chicago

Federal Home Loan Bank of Chicago

**Condensed Statements of Cash Flows (unaudited)**
(Dollars in millions)

| | Three months ended March 31, | 2016 | 2015 |
|---|---|---|---|
| **Operating** | **Net cash provided by (used in) operating activities** | **$ (9)** | $ 121 |
| **Investing** | Net change Federal Funds sold | **(1,908)** | (1,497) |
| | Net change securities purchased under agreements to resell | **1,125** | 2,000 |
| | **Advances -** | | |
| | Principal collected | **149,976** | 52,328 |
| | Issued | **(151,432)** | (51,723) |
| | **MPF Loans held in portfolio -** | | |
| | Principal collected | **282** | 337 |
| | Purchases | **(132)** | (13) |
| | **Trading securities -** | | |
| | Proceeds from maturities and paydowns | **103** | 3 |
| | Purchases | **(100)** | — |
| | **Held-to-maturity securities -** | | |
| | Short-term held-to-maturity securities, net | **581** [a] | 705 [a] |
| | Proceeds from maturities and paydowns | **232** | 232 |
| | Purchases | **(11)** | (6) |
| | **Available-for-sale securities -** | | |
| | Proceeds from maturities and paydowns | **727** | 517 |
| | Purchases | **(2)** | — |
| | Other investing activities | **6** | 11 |
| | **Net cash provided by (used in) investing activities** | **(553)** | 2,894 |
| **Financing** | Net change deposits | **(40)** | (20) |
| | **Net proceeds from issuance of consolidated obligations -** | | |
| | Discount notes | **42,844** | 149,597 |
| | Bonds | **4,410** | 4,885 |
| | **Payments for maturing and retiring consolidated obligations-** | | |
| | Discount notes | **(44,124)** | (150,180) |
| | Bonds | **(3,050)** | (6,179) |
| | Net proceeds (payments) on derivative contracts with financing element | **(12)** | (18) |
| | Proceeds from issuance of capital stock | **184** | 38 |
| | Repurchase of capital stock | **(107)** | (17) |
| | Cash dividends paid | **(9)** | (5) |
| | **Net cash provided by (used in) financing activities** | **96** | (1,899) |
| | **Net increase (decrease) in cash and due from banks** | **(466)** | 1,116 |
| | Cash and due from banks at beginning of period | **499** | 342 |
| | **Cash and due from banks at end of period** | **$ 33** | $ 1,458 |
| **Noncash** | Capital stock reclassified to mandatorily redeemable capital stock | **$ 294** | $ — |

[a] Short-term held-to-maturity securities, net, consists of investment securities with a maturity of less than 90 days when purchased.

The accompanying notes are an integral part of these financial statements (unaudited).

FHLB Chicago

Federal Home Loan Bank of Chicago
**Notes to Financial Statements - (Unaudited)**
**(Dollars in millions except per share amounts unless otherwise indicated)**

**Note 1 – Background and Basis of Presentation**

The Federal Home Loan Bank of Chicago is a federally chartered corporation and one of 11 Federal Home Loan Banks (the FHLBs) that, with the Office of Finance, comprise the Federal Home Loan Bank System (the System). The FHLBs are government-sponsored enterprises (GSE) of the United States of America and were organized under the Federal Home Loan Bank Act of 1932, as amended (FHLB Act), in order to improve the availability of funds to support home ownership. We are supervised and regulated by the Federal Housing Finance Agency (FHFA), an independent federal agency in the executive branch of the United States (U.S.) government.

Each FHLB is a member-owned cooperative with members from a specifically defined geographic district. Our defined geographic district is Illinois and Wisconsin. All federally-insured depository institutions, insurance companies engaged in residential housing finance, credit unions and community development financial institutions located in our district are eligible to apply for membership with us. All our members are required to purchase our capital stock as a condition of membership. Our capital stock is not publicly traded, and is issued, repurchased or redeemed at par value, $100 per share, subject to certain statutory and regulatory limits. As a cooperative, we do business with our members, and former members (under limited circumstances). Specifically, we provide credit principally in the form of secured loans called advances. We also provide liquidity for home mortgage loans to members approved as Participating Financial Institutions (PFIs) through the Mortgage Partnership Finance® (MPF®) Program.

Our accounting and financial reporting policies conform to generally accepted accounting principles in the United States of America (GAAP). Amounts in prior periods may be reclassified to conform to the current presentation and if material are disclosed in the following notes.

In the opinion of management, all normal recurring adjustments have been included for a fair statement of this interim financial information. These unaudited financial statements and the following footnotes should be read in conjunction with the audited financial statements and footnotes for the year ended December 31, 2015, included in our Annual Report on Form 10-K (2015 Form 10-K) starting on page F-1, as filed with the SEC.

Unless otherwise specified, references to we, us, our, and the Bank are to the Federal Home Loan Bank of Chicago.

“Mortgage Partnership Finance”, “MPF”, “MPF Xtra”, and "Community First" are registered trademarks of the Federal Home Loan Bank of Chicago.

**Use of Estimates**

The preparation of financial statements in accordance with GAAP requires us to make assumptions and estimates that may affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported amounts of income and expense. The most significant of these assumptions and estimates applies to fair value measurements and allowance for credit losses. Actual results could differ from these assumptions and estimates.

**Consolidation of Variable Interest Entities**

We would consolidate a variable interest entity if we determine that we are its primary beneficiary, which occurs when both conditions shown below are met.

- We have the power to direct the activities of a variable interest entity that most significantly impact the entity’s economic performance.

- We have the obligation to absorb losses of the entity that could potentially be significant to the variable interest entity or the right to receive benefits from the entity that could potentially be significant to the variable interest entity.

We did not consolidate any of our investments in variable interest entities since we are not the primary beneficiary. We classify variable interest entities as investment securities in our statements of condition. Such investment securities include, but are not limited to, senior interests in private-label mortgage backed securities (MBS) and Federal Family Education Loan Program asset backed securities (FFELP ABS). Our maximum loss exposure for these investment securities is limited to their carrying amounts. We have no liabilities related to these investments in variable interest entities. We have not provided financial or other support (explicitly or implicitly) to these investment securities that we were not previously contractually required to provide, nor do we intend to provide such support in the future.

**Gross versus Net Presentation of Financial Instruments**

We present derivative assets and liabilities on a net basis in our statements of condition on the basis that the Bank's right of setoff with its clearing agents and/or its counterparties is enforceable at law. We include accrued interest receivable/payable and cash collateral, including initial and variation margin, in the carrying amount of a derivative. Derivatives are netted by contract (e.g., master netting agreement) or otherwise, to discharge all or a portion of the debt owed to our counterparty by applying against the debt an amount that our counterparty owes to us. Additionally, we clear certain derivatives transactions with clearinghouses classified as a Derivatives Clearing Organization (DCO) through a Futures Commission Merchant (FCM). If these netted amounts are positive, they are classified as a derivative asset and if negative, they are classified as a derivative liability. Any over-collateralization amount received by us is not offset against another derivative asset counterparty exposure for which there is no legal right of offset, while any over-collateralization delivered by us is not offset against another derivative liability counterparty exposure for which there is no legal right of offset. Refer to **Note 9 - Derivatives and Hedging Activities** for further details.

Our policy is to report securities purchased under agreements to resell and securities sold under agreements to repurchase, if any, and securities borrowing transactions, if any, on a gross basis.

**Note 2 – Summary of Significant Accounting Policies**

Our **Summary of Significant Accounting Policies** through December 31, 2015, can be found in **Note 2 – Summary of Significant Accounting Policies** to the financial statements in our 2015 Form 10-K. We adopted the following policies in 2016:

*Simplifying the Presentation of Debt Issuance Cost (i.e., Concession Fees)*

In April of 2015, the FASB issued new guidance requiring any concession fee to be presented as a direct deduction from the debt it relates to rather than separately presented as a deferred cost in Other Assets. We retrospectively adopted the new guidance January 1, 2016 by reclassifying deferred concession fees from Other Assets to its related debt, which includes our Consolidated obligations discount notes, Consolidated obligation bonds and Subordinated notes. This reclassification did not have a material effect on our financial condition, results of operations, cash flows, or percentage net interest yield on our consolidated obligations at the time of adoption.

*Effect of Derivative Contract Novations on Existing Hedge Accounting Relationships*

In March of 2016, the FASB issued new guidance clarifying that a change in counterparty (novation) to a derivative instrument that has been designated as the hedging instrument in an existing hedging relationship would not, in and of itself, be considered a termination of the derivative instrument or be considered a change in the critical term of the hedging relationship. We early adopted this new guidance on a prospective basis effective January 1, 2016. The new guidance did not have a material effect on our financial condition, results of operations, or cash flows at the time of adoption.

**Note 3 – Recently Issued but Not Yet Adopted Accounting Standards**

*Contingent Put and Call Options in Debt Instruments*

In March of 2016, the FASB issued new guidance clarifying the requirements for assessing whether contingent call (put) options that can accelerate the payment of principal on debt instruments are clearly and closely related to their debt hosts. Specifically, the FASB clarified that the determination as to whether an embedded call (put) option is clearly and closely related to its debt host contract, should be determined solely based on the four-step decision sequence outlined in existing GAAP. Entities no longer will be required to assess whether the event triggering the acceleration of the contingent call (put) option is related to interest rates or credit risk as opposed to some extraneous event or factor in order to determine whether an embedded contingent call (put) option is clearly and closely related to its debt host. We plan to adopt the new guidance on its effective date, which is January 1, 2017. The modified retrospective approach is required when adopting the new guidance. We do not expect the new guidance to have a material effect on our financial condition, results of operations, or cash flows at the time of adoption.

*Leases*

In February of 2016, the FASB issued new guidance pertaining to lease accounting. Outlined below are the key provisions relevant to us. These provisions provide guidance governing lessee accounting for operating leases. Currently, we record operating leases off-balance sheet rather than on-balance sheet in our statements of condition.

- Recognize a right-of-use asset and a lease liability, initially measured at the present value of lease payments, in our statement of condition.
- Recognize a single lease cost, calculated so that the cost of the lease is allocated over the lease term on a generally straight-line basis.
- Classify all cash payments within operating activities in our statement of cash flows.
- For leases with a term of 12 months or less, we would be permitted to make an accounting policy election by class of underlying asset not to recognize lease assets and lease liabilities.

The new guidance becomes effective January 1, 2019. A modified retrospective transition approach is required to be applied to leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. We are in the process of reviewing its expected effect on our financial condition, results of operations, and cash flows.

*Recognition and Measurement of Financial Assets and Financial Liabilities*

In January of 2016, the FASB issued new guidance pertaining to the recognition and measurement of financial assets and financial liabilities. The key provisions applicable to us include, but are not limited to the following:

- The ability to elect the fair value option will continue to be permitted.
- Requires recognizing the portion of the total change in fair value of a liability resulting from a change in the instrument-specific credit risk in other comprehensive income when we elect to carry that liability at fair value under the fair value option.
- Requires separate presentation of financial assets and financial liabilities by measurement category, such as amortized cost, and form, such as securities or loans, on our statements of condition or the accompanying notes to the financial statements.
- Eliminates the requirement to disclose the method(s) and assumptions used to estimate fair value of financial instruments measured at amortized cost on our statements of condition.

The new guidance becomes effective January 1, 2018. We are in the process of reviewing its expected effect on our financial condition, results of operations, and cash flows.

*Revenue from Contracts with Customers*

In May of 2014, the FASB issued new guidance governing revenue recognition from contracts with customers. In August of 2015, the FASB deferred the effective date for the new revenue recognition guidance until January 1, 2018. In March of 2016, the FASB issued additional guidance related to distinguishing when an entity is acting as a principal versus an agent in contracts with customers. The distinction is relevant to reporting revenue gross (as principal) or net (as agent). In April of 2016, the FASB issued additional guidance for identifying performance obligations and licensing agreements for purposes of revenue recognition. Financial instruments and other contractual rights within the scope of other GAAP guidance are excluded from the scope of this new revenue recognition guidance. We have completed our review of the new guidance, including the guidance issued in March and April of 2016 described above. We concluded that since the majority of contracts with our members are excluded from the scope of this new guidance, the new guidance is not expected to have a material effect on our financial condition, results of operations, or cash flows at the time of adoption.

FHLB Chicago

Federal Home Loan Bank of Chicago
**Notes to Financial Statements - (Unaudited)**
**(Dollars in millions except per share amounts unless otherwise indicated)**

**Note 4 – Interest Income and Interest Expense**

The following table presents interest income and interest expense for the periods indicated:

| | Three months ended March 31, | |
|---|---|---|
| | **2016** | 2015 |
| **Interest income -** | | |
| Interest bearing deposits, Federal Funds sold and securities purchased under agreements to resell | **$ 5** | $ 3 |
| **Investment securities -** | | |
| Trading | **2** | 1 |
| Available-for-sale | **132** | 134 |
| Held-to-maturity | **59** | 69 |
| **Investment securities** | **193** | 204 |
| **Advances -** | | |
| Advance interest income | **62** | 39 |
| Advance prepayment fees, including related hedge adjustment gains (losses) of $0 and $1 | **1** | 6 |
| **Advances** | **63** | 45 |
| MPF Loans held in portfolio | **57** | 69 |
| **Interest income** | **318** | 321 |
| **Interest expense -** | | |
| **Consolidated obligations -** | | |
| Discount notes | **82** | 72 |
| Bonds | **102** | 105 |
| **Consolidated obligations** | **184** | 177 |
| Subordinated notes | **14** | 14 |
| **Interest expense** | **198** | 191 |
| **Net interest income** | **$ 120** | $ 130 |

(Dollars in millions except per share amounts unless otherwise indicated)

**Note 5 – Investment Securities**

We classify securities as either trading, held-to-maturity (HTM), or available-for-sale (AFS). Our security disclosures within these classifications are disaggregated by major security types as shown below. Our major security types are based on the nature and risks of the security.

- U.S. Government & other government related may consist of the sovereign debt of the United States; debt issued by government sponsored enterprises (GSE); and non-mortgage-backed securities of the Small Business Administration and Tennessee Valley Authority.
- Federal Family Education Loan Program - asset backed securities (FFELP ABS).
- GSE residential mortgage-backed securities (MBS) issued by Fannie Mae and Freddie Mac.
- Government-guaranteed MBS.
- Private-label residential MBS.
- State or local housing agency obligations.

**Pledged Collateral**

We disclose the amount of investment securities pledged as collateral pertaining to our derivatives activity parenthetically on our statements of condition. See **Note 9 - Derivatives and Hedging Activities** for further details.

**Trading Securities**

The following table presents the fair value of our trading securities. We did not hold a material amount of securities we issued through our MPF Government MBS product as of the dates presented. We had no material unrealized gains or losses on trading securities.

| As of | **March 31, 2016** | December 31, 2015 |
|---|---|---|
| U.S. Government & other government related | **$ 1,106** | $ 1,108 |
| **Residential MBS:** | | |
| GSE | **48** | 50 |
| Government-guaranteed | **2** | 2 |
| **Residential MBS** | **50** | 52 |
| **Trading securities** | **$ 1,156** | $ 1,160 |

(Dollars in millions except per share amounts unless otherwise indicated)

**Amortized Cost Basis and Fair Value – Available-for-Sale Securities (AFS)**

| | Amortized Cost Basis | Gross Unrealized Gains in AOCI | Gross Unrealized (Losses) in AOCI | Carrying Amount and Fair Value |
|---|---|---|---|---|
| **As of March 31, 2016** | | | | |
| U.S. Government & other government related | $ 380 | $ 24 | $ (6) | $ 398 |
| State or local housing agency | 20 | — | — | 20 |
| FFELP ABS | 4,915 | 165 | (27) | 5,053 |
| | | | | |
| **Residential MBS:** | | | | |
| GSE | 9,063 | 414 | (15) | 9,462 |
| Government-guaranteed | 1,687 | 60 | — | 1,747 |
| Private-label | 59 | 3 | — | 62 |
| **Residential MBS** | 10,809 | 477 | (15) | 11,271 |
| **Available-for-sale securities** | $ 16,124 | $ 666 | $ (48) | $ 16,742 |
| | | | | |
| As of December 31, 2015 | | | | |
| U.S. Government & other government related | $ 405 | $ 21 | $ (4) | $ 422 |
| State or local housing agency | 18 | — | — | 18 |
| FFELP ABS | 5,090 | 233 | (24) | 5,299 |
| | | | | |
| **Residential MBS:** | | | | |
| GSE | 9,427 | 383 | (12) | 9,798 |
| Government-guaranteed | 1,811 | 57 | — | 1,868 |
| Private-label | 61 | 4 | — | 65 |
| **Residential MBS** | 11,299 | 444 | (12) | 11,731 |
| **Available-for-sale securities** | $ 16,812 | $ 698 | $ (40) | $ 17,470 |

We had no sales of AFS securities for the periods presented.

FHLB Chicago

Federal Home Loan Bank of Chicago
**Notes to Financial Statements - (Unaudited)**
**(Dollars in millions except per share amounts unless otherwise indicated)**

**Amortized Cost Basis, Carrying Amount, and Fair Value - Held-to-Maturity Securities (HTM)**

| | Amortized Cost Basis | Non-credit OTTI Recognized in AOCI (Loss) | Carrying Amount | Gross Unrecognized Holding Gains | Gross Unrecognized Holding (Losses) | Fair Value |
|---|---|---|---|---|---|---|
| **As of March 31, 2016** | | | | | | |
| U.S. Government & other government related | **$ 1,307** | **$ —** | **$ 1,307** | **$ 80** | **$ —** | **$ 1,387** |
| State or local housing agency | **15** | **—** | **15** | **—** | **—** | **15** |
| | | | | | | |
| **Residential MBS:** | | | | | | |
| GSE | **2,093** | **—** | **2,093** | **151** | **—** | **2,244** |
| Government-guaranteed | **928** | **—** | **928** | **19** | **—** | **947** |
| Private-label | **1,052** | **(206)** | **846** | **303** | **(1)** | **1,148** |
| **Residential MBS** | **4,073** | **(206)** | **3,867** | **473** | **(1)** | **4,339** |
| **Held-to-maturity securities** | **$ 5,395** | **$ (206)** | **$ 5,189** | **$ 553** | **$ (1)** | **$ 5,741** |
| | | | | | | |
| As of December 31, 2015 | | | | | | |
| U.S. Government & other government related | $ 1,932 | $ — | $ 1,932 | $ 64 | $ (1) | $ 1,995 |
| State or local housing agency | 16 | — | 16 | — | — | 16 |
| | | | | | | |
| **Residential MBS:** | | | | | | |
| GSE | 2,163 | — | 2,163 | 134 | — | 2,297 |
| Government-guaranteed | 969 | — | 969 | 16 | — | 985 |
| Private-label | 1,104 | (217) | 887 | 334 | (1) | 1,220 |
| **Residential MBS** | 4,236 | (217) | 4,019 | 484 | (1) | 4,502 |
| **Held-to-maturity securities** | $ 6,184 | $ (217) | $ 5,967 | $ 548 | $ (2) | $ 6,513 |

We had no sales of HTM securities for the periods presented.

FHLB Chicago

Federal Home Loan Bank of Chicago
**Notes to Financial Statements - (Unaudited)**
**(Dollars in millions except per share amounts unless otherwise indicated)**

**Aging of Unrealized Temporary Losses**

The following tables present unrealized temporary losses on our AFS and HTM portfolio for periods less than 12 months and for 12 months or more. We recognized no OTTI charges on these unrealized loss positions because we expect to recover the entire amortized cost basis, we do not intend to sell these securities, and we believe it is more likely than not that we will not be required to sell them prior to recovering their amortized cost basis. In the tables below, in cases where the gross unrealized losses for an investment category are less than $1 million, the losses are not reported.

**Available-for-Sale Securities**

| | Less than 12 Months | | 12 Months or More | | Total | |
|---|---|---|---|---|---|---|
| | Fair Value | Gross Unrealized (Losses) | Fair Value | Gross Unrealized (Losses) | Fair Value | Gross Unrealized (Losses) |
| **As of March 31, 2016** | | | | | | |
| U.S. Government & other government related | $ 32 | $ (2) | $ 47 | $ (4) | $ 79 | $ (6) |
| FFELP ABS | 60 | (1) | 762 | (26) | 822 | (27) |
| **Residential MBS:** | | | | | | |
| GSE | 1,544 | (5) | 1,014 | (10) | 2,558 | (15) |
| Government-guaranteed | 25 | — | — | — | 25 | — |
| Private-label | — | — | 21 | — | 21 | — |
| **Residential MBS** | 1,569 | (5) | 1,035 | (10) | 2,604 | (15) |
| **Available-for-sale securities** | $ 1,661 | $ (8) | $ 1,844 | $ (40) | $ 3,505 | $ (48) |
| As of December 31, 2015 | | | | | | |
| U.S. Government & other government related | $ 30 | $ (1) | $ 45 | $ (3) | $ 75 | $ (4) |
| State or local housing agency | 4 | — | — | — | 4 | — |
| FFELP ABS | 64 | (1) | 787 | (23) | 851 | (24) |
| **Residential MBS:** | | | | | | |
| GSE | 1,081 | (3) | 1,006 | (9) | 2,087 | (12) |
| Government-guaranteed | 90 | — | — | — | 90 | — |
| Private-label | — | — | 8 | — | 8 | — |
| **Residential MBS** | 1,171 | (3) | 1,014 | (9) | 2,185 | (12) |
| **Available-for-sale securities** | $ 1,269 | $ (5) | $ 1,846 | $ (35) | $ 3,115 | $ (40) |

(Dollars in millions except per share amounts unless otherwise indicated)

**Held-to-Maturity Securities**

| | Less than 12 Months | | 12 Months or More | | Total | |
|---|---|---|---|---|---|---|
| | Fair Value | Gross Unrealized (Losses) | Fair Value | Gross Unrealized (Losses) | Fair Value | Gross Unrealized (Losses) |
| **As of March 31, 2016** | | | | | | |
| U.S. Government & other government related | $ — | $ — | $ 16 | $ — | $ 16 | $ — |
| State or local housing agency | 1 | — | 9 | — | 10 | — |
| | | | | | | |
| **Residential MBS:** | | | | | | |
| GSE | 4 | — | — | — | 4 | — |
| Government-guaranteed | 141 | — | — | — | 141 | — |
| Private-label | 6 | — | 1,098 | (207) | 1,104 | (207) |
| **Residential MBS** | 151 | — | 1,098 | (207) | 1,249 | (207) |
| **Held-to-maturity securities** | $ 152 | $ — | $ 1,123 | $ (207) | $ 1,275 | $ (207) |
| | | | | | | |
| As of December 31, 2015 | | | | | | |
| U.S. Government & other government related | $ 606 | $ — | $ 16 | $ (1) | $ 622 | $ (1) |
| State or local housing agency | 1 | — | 10 | — | 11 | — |
| | | | | | | |
| **Residential MBS:** | | | | | | |
| GSE | 4 | — | — | — | 4 | — |
| Private-label | — | — | 1,167 | (218) | 1,167 | (218) |
| **Residential MBS** | 4 | — | 1,167 | (218) | 1,171 | (218) |
| **Held-to-maturity securities** | $ 611 | $ — | $ 1,193 | $ (219) | $ 1,804 | $ (219) |

**Contractual Maturity Terms**

The following table presents the amortized cost basis and fair value of AFS and HTM securities by contractual maturity, excluding ABS and MBS securities. These securities are excluded because their expected maturities may differ from their contractual maturities if borrowers of the underlying loans elect to prepay their loans.

| | Available-for-Sale | | Held-to-Maturity | |
|---|---|---|---|---|
| **As of March 31, 2016** | Amortized Cost Basis | Carrying Amount and Fair Value | Carrying Amount | Fair Value |
| **Year of Maturity -** | | | | |
| Due in one year or less | $ — | $ — | $ 123 | $ 124 |
| Due after one year through five years | 65 | 68 | 314 | 329 |
| Due after five years through ten years | 28 | 29 | 76 | 78 |
| Due after ten years | 307 | 321 | 809 | 871 |
| ABS and MBS without a single maturity date | 15,724 | 16,324 | 3,867 | 4,339 |
| **Total securities** | $ 16,124 | $ 16,742 | $ 5,189 | $ 5,741 |

**(Dollars in millions except per share amounts unless otherwise indicated)**

**Other-Than-Temporary Impairment Analysis**

*Significant Inputs Used to Determine OTTI*

We assess an HTM or AFS private-label MBS security for OTTI whenever its fair value is less than its amortized cost basis as of the reporting date. Specifically, we generate cash flow projections utilizing key modeling assumptions, significant inputs, and methodologies provided by an FHLB System OTTI Committee, which was formed by the FHLBs to achieve consistency among the FHLBs in their OTTI analyses for private-label MBS. We then utilize these cash flow projections to determine OTTI on our private-label MBS; however, we are still responsible for making our own OTTI determination, which includes determining the reasonableness of assumptions, significant inputs, and methodologies used, and performing the required present value calculations using appropriate historical cost bases and yields.

*Cash Flow Analysis*

We perform a cash flow analysis for substantially all of these private-label securities utilizing two models provided by independent third parties as described below,

- First model. This model considers borrower characteristics and the particular attributes of the loans underlying the securities, in conjunction with assumptions about future changes in home prices and interest rates, prepayment rates, default rates, and loss severities. A significant input to the first model is the forecast of future housing price changes for the relevant states and core based statistical areas (CBSAs), which are based upon an assessment of the individual housing markets. Outputs from this first model are then used as inputs by the second model as follows.

- Second model. This model uses the month-by-month projections of future loan performance derived from the first model and allocates the projected loan level cash flows and losses to the various security classes in the securitization structure in accordance with its prescribed cash flow and loss allocation rules.

At March 31, 2016, we had a short-term housing price forecast with projected changes ranging from -1.0% to +8.0% over the twelve month period beginning January 1, 2016 over all markets. For the vast majority of markets, the short-term forecast has changes ranging from +3.0% to +5.0%.

Based on these inputs and assumptions, we had no OTTI for the periods presented.

The following table presents the changes in the cumulative amount of previously recorded OTTI credit losses (recognized into earnings) on investment securities for the reporting periods indicated.

| | Three months ended March 31, | |
|---|---|---|
| | **2016** | 2015 |
| **Beginning Balance** | **$ 568** | $ 620 |
| **Reductions:** | | |
| Increases in expected future cash flows recorded as accretion into interest income | **(13)** | (15) |
| **Ending Balance** | **$ 555** | $ 605 |

On October 15, 2010, we instituted litigation relating to 64 private-label MBS bonds we purchased in an aggregate original principal amount of $4.29 billion. In April 2016, we received a payment of $37.5 million (partially offset by $5.0 million of related legal fees and other expenses) resulting from a settlement with some of the defendants. As of April 30, 2016, the remaining litigation covers four private-label MBS bonds in the aggregate original principal amount of $77.5 million.

(Dollars in millions except per share amounts unless otherwise indicated)

**Note 6 – Advances**

We offer a wide range of fixed- and variable-rate advance products with different maturities, interest rates, payment characteristics and optionality.

The following table presents our advances by redemption terms. Actual maturities may differ from contractual maturities because some borrowers have the right to call or prepay advances with or without penalties.

| As of March 31, 2016 | Weighted Average Interest Rate | | Amount |
|---|---|---|---|
| Due in one year or less | 0.74% | $ | 9,603 |
| One to two years | 0.84% | | 7,851 |
| Two to three years | 0.70% [a] | | 5,515 |
| Three to four years | 0.59% [a] | | 7,037 |
| Four to five years | 0.77% [a] | | 4,119 |
| More than five years | 1.71% | | 3,935 |
| **Par value** | 0.83% | $ | 38,060 |

[a] The weighted average interest rate is relatively lower when compared to other categories due to a majority of advances in this category consisting of variable rate advances which reset periodically at current interest rates.

See **Note 8 - Allowance for Credit Losses** for information related to our credit risk on advances and allowance methodology for credit losses.

The following table reconciles the par value of our advances to the carrying amount on our statements of condition as of the dates indicated.

| As of | | March 31, 2016 | | December 31, 2015 |
|---|---|---|---|---|
| **Par value** | $ | 38,060 | $ | 36,605 |
| Hedging adjustments | | 268 | | 159 |
| Other adjustments | | 25 | | 14 |
| **Advances** | $ | 38,353 | $ | 36,778 |

The following advance borrowers exceeded 10% of our total advances outstanding:

| As of March 31, 2016 | | Par Value | % of Total Outstanding |
|---|---|---|---|
| One Mortgage Partners Corp | $ | 11,000 [a] | 29% |
| The Northern Trust Company | | 4,000 | 11% |

[a] One Mortgage Partners Corp. is a subsidiary of JPMorgan Chase Bank NA.

(Dollars in millions except per share amounts unless otherwise indicated)

**Note 7 – MPF Loans Held in Portfolio**

We acquire MPF Loans from PFIs to hold in our portfolio, and in some cases we purchased participations in pools of eligible mortgage loans from other FHLBs (MPF Banks). MPF Loans are defined as fixed-rate conventional and government mortgage loans secured by one-to-four family residential properties with maturities ranging from 5 years to 30 years or participations in pools of eligible mortgage loans from other MPF Banks.

The following table presents information on MPF Loans held in portfolio by contractual maturity at the time of purchase.

| As of | March 31, 2016 | December 31, 2015 |
|---|---|---|
| Medium term (15 years or less) | $ 580 | $ 662 |
| Long term (greater than 15 years) | 4,046 | 4,112 |
| **Unpaid principal balance** | 4,626 | 4,774 |
| Net premiums, credit enhancement and deferred loan fees | 21 | 20 |
| Hedging adjustments | 34 | 37 |
| **MPF Loans held in portfolio, before allowance for credit losses** | 4,681 | 4,831 |
| Allowance for credit losses on MPF Loans | (2) | (3) |
| **MPF Loans held in portfolio, net** | $ 4,679 | $ 4,828 |
| | | |
| Conventional mortgage loans | $ 3,453 | $ 3,568 |
| Government Loans | 1,173 | 1,206 |
| **Unpaid principal balance** | $ 4,626 | $ 4,774 |

See the **MPF Risk Sharing Structure** on page F-14 in our 2015 Form 10-K for information related to our credit losses on MPF Loans held in portfolio

In addition to our portfolio MPF Products, PFIs sell eligible MPF Loans to us through the MPF Program infrastructure and we concurrently sell them to third party investors or hold MPF Loans in our held for sale portfolio in other assets for a short period of time until such loans are pooled into MBS.

(Dollars in millions except per share amounts unless otherwise indicated)

**Note 8 – Allowance for Credit Losses**

See **Note 2 - Summary of Significant Accounting Policies** to the financial statements in our 2015 Form 10-K for further details pertaining to the methodologies and factors we consider when determining the amount to recognize as an allowance for credit losses, if any, for each portfolio segment identified below.

We have identified our portfolio segments as shown below.

- Member credit products (advances, letters of credit and other extensions of credit to borrowers);
- Conventional MPF Loans held in portfolio;
- Government Loans held in portfolio; and
- Federal Funds Sold and Securities Purchased Under Agreements to Resell.

**Member Credit Products**

We have not recorded any allowance for credit losses for our member credit products portfolio segment based upon our credit analysis and the repayment history on member credit products. We had no member credit products that were past due, on nonaccrual status, involved in a troubled debt restructuring or otherwise considered impaired. We have not recorded a liability to reflect an allowance for credit losses for our member credit products with off-balance sheet credit exposures.

**Conventional MPF Loans Held in Portfolio**

For further detail of our **MPF Risk Sharing Structure** see page F-14 in our 2015 Form 10-K.

The following table presents the changes in the allowance for credit losses attributable to our portfolio segment for conventional MPF Loans held in portfolio.

| | Three months ended March 31, | |
|---|---|---|
| | **2016** | 2015 |
| Balance, beginning of period | **$ 3** | $ 15 |
| Losses charged to the allowance | **(1)** | (11) |
| Balance, end of period | **$ 2** | $ 4 |

The following table presents the recorded investment in conventional MPF Loans by impairment methodology. Recorded investment in a conventional MPF Loan is its amortized cost basis plus related accrued interest receivable, if any. Recorded investment is not net of its allowance for credit losses but is net of any direct charge-off on the conventional MPF Loan.

| As of | **March 31, 2016** | December 31, 2015 |
|---|---|---|
| **Allowance for credit losses on conventional MPF Loans -** | | |
| Homogeneous pools of loans collectively evaluated for impairment | **$ 2** | $ 3 |
| | | |
| **Recorded investment in conventional MPF Loans -** | | |
| Individually evaluated for impairment | **$ 96** | $ 107 |
| Collectively evaluated for impairment | **3,415** | 3,519 |
| **Recorded investment** | **$ 3,511** | $ 3,626 |

**Government Loans Held in Portfolio**

Any losses incurred on Government Loans that are not recovered from the government insurer or guarantor are absorbed by the servicing PFI. We did not establish an allowance for credit losses of our portfolio segment for Government Loans included in our MPF Loan held in portfolio for the reporting periods presented based on our assessment of our servicing PFIs' ability to absorb such losses. Further, Government Loans were not placed on nonaccrual status or disclosed as troubled debt restructurings for the same reason.

(Dollars in millions except per share amounts unless otherwise indicated)

**Credit Quality Indicators - MPF Loans**

The following table summarizes our recorded investment in MPF Loans by our key credit quality indicators, which include:

- "Serious delinquency rate" consists of MPF Loans that are 90 days or more past due or in the process of foreclosure, as a percentage of the total recorded investment.
- "Past due 90 days or more still accruing interest" consists of MPF Loans that are either government guaranteed or conventional mortgage loans that are well secured (by collateral that have a realizable value sufficient to discharge the debt or by the guarantee or insurance, such as PMI, of a financially responsible party) and in the process of collection.

| | **March 31, 2016** | | | December 31, 2015 | | |
|---|---|---|---|---|---|---|
| As of | **Conventional** | **Government** | **Total** | Conventional | Government | Total |
| Past due 30-59 days | **$ 92** | **$ 52** | **$ 144** | $ 99 | $ 63 | $ 162 |
| Past due 60-89 days | **28** | **16** | **44** | 32 | 21 | 53 |
| Past due 90 days or more | **91** | **16** | **107** | 100 | 15 | 115 |
| Past due | **211** | **84** | **295** | 231 | 99 | 330 |
| Current | **3,300** | **1,111** | **4,411** | 3,395 | 1,130 | 4,525 |
| **Recorded investment** | **$ 3,511** | **$ 1,195** | **$ 4,706** | $ 3,626 | $ 1,229 | $ 4,855 |
| Also in process of foreclosure | **$ 49** | **$ 3** | **$ 52** | $ 51 | $ 3 | $ 54 |
| Serious delinquency rate | **2.59%** | **1.36%** | **2.28%** | 2.77% | 1.23% | 2.38% |
| Past due 90 days or more still accruing interest | **$ 8** | **$ 16** | **$ 24** | $ 10 | $ 15 | $ 25 |
| On nonaccrual status | **$ 96** | **$ —** | **$ 96** | $ 107 | $ — | $ 107 |

*Individually Evaluated Impaired MPF Loans*

The following table summarizes the recorded investment, unpaid principal balance, and related allowance for credit losses attributable to individually evaluated impaired conventional MPF Loans. Conventional MPF Loans are individually evaluated for impairment when they are adversely classified. There is no allowance for credit losses attributable to conventional MPF Loans that are individually evaluated for impairment, since the related allowance for credit losses have been charged off.

| As of | **March 31, 2016** | December 31, 2015 |
|---|---|---|
| Recorded investment without an allowance for credit losses | **$ 96** | $ 107 |
| Unpaid principal balance without an allowance for credit losses | **105** | 117 |

The following table summarizes the average recorded investment of impaired conventional MPF Loans. We do not recognize interest income on impaired loans.

| | Three months ended March 31, | |
|---|---|---|
| | **2016** | 2015 |
| Average recorded investment without an allowance for credit losses | **$ 99** | $ 148 |

**Term Federal Funds Sold and Term Securities Purchased Under Agreements to Resell**

We only had credit risk exposure to overnight Federal Funds sold and Securities Purchased Under Agreements to Resell as of March 31, 2016 and December 31, 2015. We did not have any term Federal Funds sold and Securities Purchased Under Agreements to Resell arrangements. We did not establish an allowance for credit losses for our overnight Federal Funds sold since all Federal Funds sold were repaid according to their contractual terms. We also did not establish an allowance for credit losses for overnight Securities Purchased Under Agreements to Resell since all payments due under the contractual terms have been received and we hold sufficient underlying collateral.

**Note 9 – Derivatives and Hedging Activities**

Refer to **Note 2 - Summary of Significant Accounting Policies** in our 2015 Form 10-K for our accounting policies for derivatives.

We transact most of our derivatives with large banks and major broker-dealers. Some of these banks and broker-dealers or their affiliates buy, sell, and distribute consolidated obligations. Derivative transactions may be entered into through an over-the-counter bilateral agreement with an individual counterparty. Additionally, we clear some derivatives transactions with clearinghouses classified as a Derivatives Clearing Organization (DCO) through a Futures Commission Merchant (FCM). We are not a derivatives dealer and do not trade derivatives for speculative purposes.

*Managing Credit Risk on Derivative Agreements*

We are subject to credit risk due to the risk of nonperformance by counterparties to our derivative agreements. For bilateral derivative agreements, the degree of counterparty risk depends on the extent to which master netting arrangements, collateral requirements and other credit enhancements are included in such contracts to mitigate the risk. We manage counterparty credit risk through credit analysis, collateral requirements and adherence to the requirements set forth in our policies and FHFA regulations. We require collateral agreements on all derivatives that establish collateral delivery thresholds. Additionally, collateral related to derivatives with member institutions includes collateral assigned to us, as evidenced by a written security agreement, and held by the member institution for our benefit. Based on credit analyses and collateral requirements, we do not anticipate any credit losses on our derivative agreements. See **Note 16 - Fair Value** to the financial statements in our 2015 Form 10-K for discussion regarding our fair value methodology for derivative assets and liabilities, including an evaluation of the potential for the fair value of these instruments to be affected by counterparty credit risk.

Our over-the-counter bilateral derivative agreements may contain provisions that require us to post additional collateral with our counterparties if there is deterioration in our credit rating, except for those derivative agreements with a zero unsecured collateral threshold for both parties, in which case positions are required to be fully collateralized regardless of credit rating. If our credit rating is lowered by a major credit rating agency, such as Standard and Poor's or Moody’s, we would be required to deliver additional collateral on derivatives in net liability positions. If our credit rating had been lowered from its current rating to the next lower rating, we would have been required to deliver up to an additional $42 million of collateral at fair value to our derivatives counterparties at March 31, 2016.

Cleared swaps are subject to initial and variation margin requirements established by the DCO and its clearing members. We post initial and variation margin through the clearing member, on behalf of the DCO, which could expose us to institutional credit risk in the event that a clearing member or the DCO fail to meet their obligations. Clearing derivatives through a DCO mitigates counterparty credit risk exposure because a central DCO counterparty is substituted for individual counterparties and collateral is posted daily for changes in the value of cleared derivatives through an FCM. The DCO determines initial margin requirements for cleared derivatives. In this regard, clearing agents may require additional initial margin to be posted based on credit considerations, including but not limited to, credit rating downgrades. We had no requirement to post additional initial margin by our clearing agents at March 31, 2016.

We present our derivative assets and liabilities on a net basis in our statements of condition. Refer to **Note 1 - Background and Basis of Presentation** for further discussion. In addition to the cash collateral as noted in the following table, we also pledged $103 million of investment securities that can be sold or repledged, as part of our initial margin related to cleared derivative transactions at March 31, 2016.

(Dollars in millions except per share amounts unless otherwise indicated)

The following table presents our gross and net derivative assets and liabilities by contract type and amount for our derivative agreements.

| | March 31, 2016 | | | December 31, 2015 | | |
|---|---|---|---|---|---|---|
| As of | Notional Amount | Derivative Assets | Derivative Liabilities | Notional Amount | Derivative Assets | Derivative Liabilities |
| **Derivatives in hedge accounting relationships-** | | | | | | |
| Interest rate swaps | **$ 24,177** | **$ 67** | **$ 1,264** | $ 25,140 | $ 30 | $ 1,082 |
| **Derivatives not in hedge accounting relationships-** | | | | | | |
| Interest rate swaps | **23,211** | **556** | **459** | 28,866 | 456 | 341 |
| Interest rate swaptions | **860** | **51** | **—** | 1,270 | 40 | — |
| Interest rate caps or floors | **1,129** | **73** | **—** | 1,131 | 76 | — |
| Interest rate futures | **17** | **—** | **—** | 7 | — | — |
| Mortgage delivery commitments | **717** | **1** | **1** | 479 | 1 | 1 |
| TBAs Ginnie Mae securitizations | **111** | **—** | **1** | 114 | — | — |
| **Derivatives not in hedge accounting relationships** | **26,045** | **681** | **461** | 31,867 | 573 | 342 |
| **Gross derivative amount before adjustments** | **$ 50,222** | **748** | **1,725** | $ 57,007 | 603 | 1,424 |
| Netting adjustments and cash collateral | | **(745)** [a] | **(1,665)** [a] | | (601) [a] | (1,369) [a] |
| **Derivatives on statements of condition** | | **$ 3** | **$ 60** | | $ 2 | $ 55 |

[a] Amounts represent the application of the netting requirements that allow us to settle positive and negative positions and also cash collateral and related accrued interest held or placed by us with the same clearing agent and/or counterparty. Cash collateral posted was $947 million and $793 million at March 31, 2016, and December 31, 2015, and cash collateral received was $28 million and $25 million.

The following table presents our gross recognized amount of offsetting derivative assets and liabilities for derivatives with legal right of offset as well as derivatives without the legal right of offset.

| | Derivative Assets | | | Derivative Liabilities | | |
|---|---|---|---|---|---|---|
| **As of March 31, 2016** | **Bilateral** | **Cleared** | **Total** | **Bilateral** | **Cleared** | **Total** |
| **Derivatives with legal right of offset -** | | | | | | |
| Gross recognized amount | **$ 602** | **$ 145** | **$ 747** | **$ 1,167** | **$ 557** | **$ 1,724** |
| Netting adjustments and cash collateral | **(600)** | **(145)** | **(745)** | **(1,122)** | **(543)** | **(1,665)** |
| **Derivatives with legal right of offset - net** | **2** | **—** | **2** | **45** | **14** | **59** |
| Derivatives without legal right of offset | **1** | **—** | **1** | **1** | **—** | **1** |
| **Derivatives on statements of condition** | **3** | **—** | **3** | **46** | **14** | **60** |
| Noncash collateral received (pledged) and cannot be sold or repledged | **1** | **—** | **1** | **—** | **14** | **14** |
| **Net amount** | **$ 2** | **$ —** | **$ 2** | **$ 46** | **$ —** | **$ 46** |
| | | | | | | |
| As of December 31, 2015 | | | | | | |
| **Derivatives with legal right of offset -** | | | | | | |
| Gross recognized amount | $ 509 | $ 93 | $ 602 | $ 1,182 | $ 241 | $ 1,423 |
| Netting adjustments and cash collateral | (508) | (93) | (601) | (1,140) | (229) | (1,369) |
| **Derivatives with legal right of offset - net** | 1 | — | 1 | 42 | 12 | 54 |
| Derivatives without legal right of offset | 1 | — | 1 | 1 | — | 1 |
| **Derivatives on statements of condition** | 2 | — | 2 | 43 | 12 | 55 |
| Noncash collateral received (pledged) and cannot be sold or repledged | — | — | — | — | 12 | 12 |
| **Net amount** | $ 2 | $ — | $ 2 | $ 43 | $ — | $ 43 |

At March 31, 2016, we had $88 million of additional net credit exposure on cleared derivatives due to our pledging of non-cash collateral to a DCO for initial margin, which exceeded our net derivative liability position. We had $50 million comparable exposure at December 31, 2015.

(Dollars in millions except per share amounts unless otherwise indicated)

The following table presents the gains (losses) of derivatives and hedging activities as presented in the statements of income.

| | Three months ended March 31, | |
|---|---|---|
| For the periods ending | **2016** | 2015 |
| **Fair value hedges -** | | |
| Interest rate swaps | **$ (9)** | $ (19) |
| **Economic hedges -** | | |
| Interest rate swaps | **(27)** | (23) |
| Interest rate swaptions | **11** | 8 |
| Interest rate caps or floors | **(3)** | (1) |
| Net interest settlements | **12** | 24 |
| Mortgage delivery commitments | **2** | — |
| TBAs Ginnie Mae securitizations | **(2)** | — |
| **Economic hedges** | **(7)** | 8 |
| **Gains (losses) on derivatives and hedging activities** | **$ (16)** | $ (11) |

*Fair Value Hedges*

The following table presents, by type of hedged item, the gains (losses) on derivatives and the related hedged items in fair value hedging relationships and the effect of those derivatives on our net interest income. **Net Interest Settlements Recorded in Net Interest Income** represents the effect of net interest settlements attributable to open derivative hedging instruments on net interest income. The effect of derivatives on net interest income is included in the interest income/expense line item of the respective hedged item type. **Closed Hedge Adjustments Amortized into Net Interest Income** represents the amortization of hedge adjustments included in the interest income/expense line item of the respective hedged item type. We had no gain (loss) for hedged firm commitments on forward-starting advances that no longer qualified as a fair value hedge.

| | **On Derivative** | **On Hedged Item** | **Total Ineffectiveness Recognized in Derivatives and Hedging Activities** | **Net Interest Settlements Recorded in Net Interest Income** | **Closed Hedge Adjustments Amortized into Net Interest Income** |
|---|---|---|---|---|---|
| **Three months ended March 31, 2016** | | | | | |
| Available-for-sale securities | **$ (51)** | **$ 48** | **$ (3)** | **$ (30)** | **$ (4)** |
| Advances | **(110)** | **109** | **(1)** | **(20)** | **—** |
| MPF Loans held for portfolio | **—** | **—** | **—** | **—** | **(2)** |
| Consolidated obligation bonds | **68** | **(73)** | **(5)** | **25** | **(3)** |
| **Total** | **$ (93)** | **$ 84** | **$ (9)** | **$ (25)** | **$ (9)** |
| Three months ended March 31, 2015 | | | | | |
| Available-for-sale securities | $ (36) | $ 31 | $ (5) | $ (34) | $ (10) |
| Advances | (61) | 57 | (4) | (20) | 1 |
| MPF Loans held for portfolio | — | — | — | — | (4) |
| Consolidated obligation bonds | 74 | (84) | (10) | 58 | — |
| **Total** | $ (23) | $ 4 | $ (19) | $ 4 | $ (13) |

(Dollars in millions except per share amounts unless otherwise indicated)

*Cash Flow Hedges*

The following table presents our gains (losses) on our cash-flow hedging relationships recorded in income and other comprehensive income (loss). In cases where amounts are insignificant in the aggregate, we do not report a balance. We reclassify amounts in AOCI into our statements of income in the same period or periods during which the hedged forecasted transaction affects our earnings. We had no discontinued hedges. The deferred net gains (losses) on derivative instruments in AOCI that are expected to be reclassified to earnings during the next twelve months were $(3) million as of March 31, 2016. The maximum length of time over which we are hedging our exposure to the variability in future cash flows for forecasted transactions is 5 years. **Net Interest Settlements Recorded in Net Interest Income** represents the effect of net interest settlements attributable to open derivative hedging instruments on net interest income. The effect of derivatives on net interest income is included in the interest income/expense line item of the respective hedged item type. We had no hedge ineffectiveness reclassified from AOCI to derivatives and hedging activities for the periods presented in the below table.

| | | Amortization of Effective Portion Reclassified From AOCI to Interest | Total Reclassified From AOCI to Statements of Income | Net Change in Other Comprehensive Income | Effective Portion Recorded in AOCI | Net Interest Settlements Recorded in Net Interest Income |
|---|---|---|---|---|---|---|
| **Three months ended March 31, 2016** | | | | | | |
| Advances | Interest rate floors | **$ 2** | **$ 2** | **$ (2)** | **$ —** | **$ —** |
| Discount notes | Interest rate swaps | **—** | **—** | **(52)** | **(52)** | **(47)** |
| Bonds | Interest rate swaps | **(1)** | **(1)** | **1** | **—** | **—** |
| **Total** | | **$ 1** | **$ 1** | **$ (53)** | **$ (52)** | **$ (47)** |
| Three months ended March 31, 2015 | | | | | | |
| Advances | Interest rate floors | $ 3 | $ 3 | $ (3) | $ — | $ — |
| Discount notes | Interest rate swaps | (1) | (1) | (26) | (27) | (62) |
| Bonds | Interest rate swaps | (1) | (1) | 1 | — | — |
| **Total** | | $ 1 | $ 1 | $ (28) | $ (27) | $ (62) |

(Dollars in millions except per share amounts unless otherwise indicated)

**Note 10 – Consolidated Obligations**

The FHLBs issue consolidated obligations through the Office of Finance as their agent. Consolidated obligations consist of discount notes and consolidated obligation bonds. Consolidated discount notes are issued to raise short-term funds, are issued at less than their face amount and redeemed at par value when they mature. The maturity of consolidated bonds may range from less than one year to over 20 years, but they are not subject to any statutory or regulatory limits on maturity.

The following table presents our consolidated obligation bonds, for which we are the primary obligor, including callable bonds that are redeemable in whole, or in part, at our discretion on predetermined call dates.

| **As of March 31, 2016** | **Contractual Maturity** | **Weighted Average Interest Rate** | **By Next Maturity or Call Date** |
|---|---|---|---|
| Due in one year or less | $ 5,528 | 1.81% | $ 16,188 |
| One to two years | 5,148 | 2.19% | 3,973 |
| Two to three years | 3,342 | 1.27% | 1,120 |
| Three to four years | 3,694 | 1.49% | 1,516 |
| Four to five years | 2,655 | 1.68% | 101 |
| Thereafter | 3,677 | 3.43% | 1,146 |
| **Par value** | $ 24,044 | 2.00% | $ 24,044 |

The following table presents our consolidated obligation discount notes for which we are the primary obligor. All are due in one year or less.

| As of | **March 31, 2016** | December 31, 2015 |
|---|---|---|
| Carrying Amount | **$ 40,293** | $ 41,564 |
| Par Value | **40,313** | 41,584 |
| Weighted Average Interest Rate | **0.38%** | 0.22% |

The following table presents consolidated obligation bonds outstanding by call feature:

| As of | **March 31, 2016** | December 31, 2015 |
|---|---|---|
| Noncallable | **$ 12,690** | $ 10,148 |
| Callable | **11,354** | 12,536 |
| **Par value** | **24,044** | 22,684 |
| Hedging adjustments | **(26)** | (101) |
| Other adjustments | **3** | (1) |
| **Consolidated obligation bonds** | **$ 24,021** | $ 22,582 |

The following table summarizes the consolidated obligations of the FHLBs and those for which we are the primary obligor. We did not accrue a liability for our joint and several liability related to the other FHLBs' share of the consolidated obligations as of March 31, 2016, and December 31, 2015. Refer to **Note 17 - Commitments and Contingencies** to the financial statements in our 2015 Form 10-K for further details.

| | **March 31, 2016** | | | December 31, 2015 | | |
|---|---|---|---|---|---|---|
| Par values as of | **Bonds** | **Discount Notes** | **Total** | Bonds | Discount Notes | Total |
| FHLB System total consolidated obligations | **$ 459,139** | **$ 437,689** | **$ 896,828** | $ 410,859 | $ 494,343 | $ 905,202 |
| FHLB Chicago as primary obligor | **24,044** | **40,313** | **64,357** | 22,684 | 41,584 | 64,268 |
| As a percent of the FHLB System | **5%** | **9%** | **7%** | 6% | 8% | 7% |

FHLB Chicago

Federal Home Loan Bank of Chicago
**Notes to Financial Statements - (Unaudited)**
**(Dollars in millions except per share amounts unless otherwise indicated)**

**Note 11 – Capital and Mandatorily Redeemable Capital Stock (MRCS)**

Under our Capital Plan our stock consists of two sub-classes of stock, Class B1 activity stock and Class B2 membership stock (together, Class B stock), both with a par value of $100 and redeemable on five years' written notice, subject to certain conditions. Under the Capital Plan, each member is required to own capital stock in an amount equal to the greater of a membership stock requirement or an activity stock requirement. Class B1 activity stock is available for purchase only to support a member's activity stock requirement. Class B2 membership stock is available to be purchased to support a member's membership stock requirement and any activity stock requirement.

**Minimum Capital Requirements**

For details on our minimum capital requirements, including how the ratios below were calculated, see **Minimum Capital Requirements** on page F-42 of our 2015 Form 10-K. We complied with our minimum regulatory capital requirements as shown below.

| | **March 31, 2016** | | December 31, 2015 | |
|---|---|---|---|---|
| | **Requirement** | **Actual** | Requirement | Actual |
| Risk-based capital | **$ 988** | **$ 4,825** | $ 1,027 | $ 4,688 |
| Total regulatory capital | **$ 2,837** | **$ 4,825** | $ 2,827 | $ 4,688 |
| Total regulatory capital ratio | **4.00%** | **6.81%** | 4.00% | 6.63% |
| Leverage capital | **$ 3,546** | **$ 7,238** | $ 3,534 | $ 7,032 |
| Leverage capital ratio | **5.00%** | **10.21%** | 5.00% | 9.95% |

Total regulatory capital and leverage capital includes mandatorily redeemable capital stock (MRCS) but does not include AOCI. Under the FHFA regulation on capital classifications and critical capital levels for the FHLBs, we are adequately capitalized.

The following members' regulatory capital stock exceeded 10% of our total regulatory capital stock outstanding:

| **As of March 31, 2016** | **Regulatory Capital Stock Outstanding** | **% of Total Outstanding** |
|---|---|---|
| One Mortgage Partners Corp | **$ 250** [a] | **12%** |

[a] One Mortgage Partners Corp. is a subsidiary of JPMorgan Chase Bank NA.

*Transfer of Capital Stock to Mandatorily Redeemable Capital Stock (MRCS)*

During the first quarter of 2016, we transferred $294 million of our captive insurance company members' capital stock from equity to MRCS in liabilities on our statement of condition. The transfer was triggered by the issuance of the final FHFA rule on FHLB membership making captive insurance companies ineligible for FHLB membership, which was issued on January 20, 2016 and became effective February 19, 2016. Under this rule, our three captive insurance company members will have their memberships terminated by February 2021. The transfer from equity to MRCS in liabilities was required because the new rule creates an unconditional obligation requiring us to redeem our capital stock from our captive insurance company members after their membership terminates. We reclassify our capital stock from equity to MRCS in liabilities at fair value, which is its par value plus any dividends related to the capital stock. Par value represents fair value since our capital stock can only be acquired and redeemed or repurchased at par value. Further, our capital stock is not traded and no market mechanism exists for the exchange of stock outside our cooperative structure. Upon reclassification to MRCS, subsequent dividends are accrued at the expected dividend rate and reported as a component of interest expense in our statements of income.

*Excess Capital Stock*

In February 2016, we announced significant reductions in our membership stock and activity stock requirements, which went into effect on April 1, 2016. As a result of these changes, we held $593 million of excess capital stock on April 1, 2016. As of April 30, 2016, we held excess capital stock of $422 million. The reduction was a result of members requesting repurchase of their excess stock and members utilizing excess stock to support new advance borrowing activities.

**(Dollars in millions except per share amounts unless otherwise indicated)**

**Note 12 - Accumulated Other Comprehensive Income (Loss)**

The following table summarizes the income (loss) in AOCI for the reporting periods indicated.

| | Net Unrealized Gain (Loss) Available-for-sale Securities | Non-credit OTTI Held-to-maturity Securities | Net Unrealized on Cash Flow Hedges | Post-Retirement Plans | AOCI |
|---|---|---|---|---|---|
| **Three months ended March 31, 2016** | | | | | |
| **Beginning balance** | **$ 658** | **$ (217)** | **$ (463)** | **$ (6)** | **$ (28)** |
| Change in the period recorded to the statements of condition, before reclassifications to statements of income | **(40)** | **11** | **(52)** | **—** | **(81)** |
| **Amounts reclassified in period to statements of income:** | | | | | |
| Net interest income | **—** | **—** | **(1)** | **—** | **(1)** |
| **Other comprehensive income in the period** | **(40)** | **11** | **(53)** | **—** | **(82)** |
| **Ending balance** | **$ 618** | **$ (206)** | **$ (516)** | **$ (6)** | **$ (110)** |
| Three months ended March 31, 2015 | | | | | |
| **Beginning balance** | $ 1,060 | $ (264) | $ (580) | $ 1 | $ 217 |
| Change in the period recorded to the statements of condition, before reclassifications to statements of income | (22) | 13 | (27) | (8) | (44) |
| **Amounts reclassified in period to statements of income:** | | | | | |
| Net interest income | — | — | (1) | — | (1) |
| **Other comprehensive income in the period** | (22) | 13 | (28) | (8) | (45) |
| **Ending balance** | $ 1,038 | $ (251) | $ (608) | $ (7) | $ 172 |

**(Dollars in millions except per share amounts unless otherwise indicated)**

**Note 13 - Fair Value**

Fair value represents the exit price that we would receive to sell an asset or pay to transfer a liability in an orderly transaction with a market participant at the measurement date. Refer to **Note 2 - Summary of Significant Accounting Policies** to the financial statements in our 2015 Form 10-K for our fair value measurement policies. For a description of the valuation techniques and significant inputs see **Note 16 - Fair Value** to the financial statements in our 2015 Form 10-K.

The following tables are a summary of the fair value estimates and related levels in the fair value hierarchy. The carrying amounts are as recorded in the statements of condition. These tables do not represent an estimate of our overall market value as a going concern; as they do not take into account future business opportunities and future net profitability of assets and liabilities. We had no transfers between levels in the fair value hierarchy for the periods shown.

The following table shows the fair values of financial instruments that are measured at amortized cost on our statements of condition, except where we elected the fair value option. Financial instruments for which we elected the fair value option are measured at fair value on a recurring basis on our statements of condition and are parenthetically shown in the following table.

| | Carrying Amount | Fair Value | Fair Value Hierarchy Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|---|
| **March 31, 2016** | | | | | |
| **Financial Assets -** | | | | | |
| Cash and due from banks | $ 33 | $ 33 | $ 33 | $ — | $ — |
| Interest bearing deposits | 650 | 650 | 650 | — | — |
| Federal Funds sold | 3,610 | 3,610 | — | 3,610 | — |
| Securities purchased under agreements to resell | 250 | 250 | — | 250 | — |
| Held-to-maturity securities | 5,189 | 5,741 | — | 4,593 | 1,148 |
| Advances | 38,353 | 38,311 | — | 38,311 | — |
| MPF Loans held in portfolio, net | 4,679 | 4,999 | — | 4,965 | 34 |
| **Financial Liabilities -** | | | | | |
| Deposits | (498) | (498) | — | (498) | — |
| Consolidated obligation discount notes | (40,293) | (40,299) | — | (40,299) | — |
| Consolidated obligation bonds | (24,021) | (24,500) | — | (24,500) | — |
| Mandatorily redeemable capital stock | (302) | (302) | (302) | — | — |
| Subordinated notes | (944) | (954) | — | (954) | — |
| December 31, 2015 | | | | | |
| **Financial Assets -** | | | | | |
| Cash and due from banks | $ 499 | $ 499 | $ 499 | $ — | $ — |
| Interest bearing deposits | 650 | 650 | 650 | — | — |
| Federal Funds sold | 1,702 | 1,702 | — | 1,702 | — |
| Securities purchased under agreements to resell | 1,375 | 1,375 | — | 1,375 | — |
| Held-to-maturity securities | 5,967 | 6,513 | — | 5,293 | 1,220 |
| Advances | 36,778 | 36,736 | — | 36,736 | — |
| MPF Loans held in portfolio, net | 4,828 | 5,190 | — | 5,155 | 35 |
| **Financial Liabilities -** | | | | | |
| Deposits | (538) | (538) | — | (538) | — |
| Consolidated obligation discount notes | (41,564) | (41,563) | — | (41,563) | — |
| Consolidated obligation bonds | (22,582) | (22,986) | — | (22,931) | (55) [a] |
| Mandatorily redeemable capital stock | (8) | (8) | (8) | — | — |
| Subordinated notes | (944) | (966) | — | (966) | — |

[a] Amount represents debt carried at fair value under a full fair value hedge strategy, not at fair value under the fair value option.

**(Dollars in millions except per share amounts unless otherwise indicated)**

The following table presents financial instruments measured at fair value on a recurring basis on our statements of condition. The **Netting** adjustment amount includes cash collateral (either received or paid by us) and related accrued interest in cases where we have a legal right of setoff, by contract (e.g., master netting agreement) or otherwise, to discharge all or a portion of the debt owed to our counterparty by applying against the debt an amount that our counterparty owes to us. See **Note 9 - Derivatives and Hedging Activities**.

| **March 31, 2016** | **Level 2** | **Level 3** | **Netting** | **Fair Value** |
|---|---|---|---|---|
| **Financial assets -** | | | | |
| U.S. Government & other government related non-MBS | **$ 1,106** | **$ —** | | **$ 1,106** |
| GSE residential MBS | **48** | **—** | | **48** |
| U.S. Governmental-guaranteed residential MBS | **2** | **—** | | **2** |
| **Trading securities** | **1,156** | **—** | | **1,156** |
| U.S. Government & other government related non-MBS | **398** | **—** | | **398** |
| State or local housing agency non-MBS | **20** | **—** | | **20** |
| FFELP ABS | **5,053** | **—** | | **5,053** |
| GSE residential MBS | **9,462** | **—** | | **9,462** |
| U.S. Government-guaranteed residential MBS | **1,747** | **—** | | **1,747** |
| Private-label residential MBS | **—** | **62** | | **62** |
| **Available-for-sale securities** | **16,680** | **62** | | **16,742** |
| Advances | **605** | **—** | | **605** |
| Derivative assets | **748** | **—** | **$ (745)** | **3** |
| Other assets - Mortgage loans held for sale | **62** | **—** | | **62** |
| **Financial assets at fair value** | **$ 19,251** | **$ 62** | **$ (745)** | **$ 18,568** |
| Level 3 as a percent of total assets at fair value | | **0.3%** | | |
| **Financial liabilities -** | | | | |
| Consolidated obligation discount notes | **$ (2,237)** | **$ —** | | **$ (2,237)** |
| Consolidated obligation bonds | **(3,811)** | **—** | | **(3,811)** |
| Derivative liabilities | **(1,725)** | **—** | **$ 1,665** | **(60)** |
| **Financial liabilities at fair value** | **$ (7,773)** | **$ —** | **$ 1,665** | **$ (6,108)** |
| Level 3 as a percent of total liabilities at fair value | | **—%** | | |
| December 31, 2015 | | | | |
| **Financial assets -** | | | | |
| U.S. Government & other government related non-MBS | $ 1,108 | $ — | | $ 1,108 |
| GSE residential MBS | 50 | — | | 50 |
| U.S. Governmental-guaranteed residential MBS | 2 | — | | 2 |
| **Trading securities** | 1,160 | — | | 1,160 |
| U.S. Government & other government related non-MBS | 422 | — | | 422 |
| State or local housing agency non-MBS | 18 | — | | 18 |
| FFELP ABS | 5,299 | — | | 5,299 |
| GSE residential MBS | 9,798 | — | | 9,798 |
| U.S. Government-guaranteed residential MBS | 1,868 | — | | 1,868 |
| Private-label residential MBS | — | 65 | | 65 |
| **Available-for-sale securities** | 17,405 | 65 | | 17,470 |
| Advances | 511 | — | | 511 |
| Derivative assets | 598 | 5 | $ (601) | 2 |
| Other assets - Mortgage loans held for sale | 54 | — | | 54 |
| **Financial assets at fair value** | $ 19,728 | $ 70 | $ (601) | $ 19,197 |
| Level 3 as a percent of total assets at fair value | | 0.4% | | |
| **Financial liabilities -** | | | | |
| Consolidated obligation discount notes | $ (9,006) | $ — | | $ (9,006) |
| Consolidated obligation bonds | (952) | (55) [a] | | (1,007) |
| Derivative liabilities | (1,424) | — | $ 1,369 | (55) |
| **Financial liabilities at fair value** | $ (11,382) | $ (55) | $ 1,369 | $ (10,068) |
| Level 3 as a percent of total liabilities at fair value | | 0.5% | | |

[a] Amount represents debt carried at fair value under a full fair value hedge strategy, not at fair value under the fair value option.

(Dollars in millions except per share amounts unless otherwise indicated)

**Fair Value Option**

We elect the fair value option for financial instruments, such as advances, MPF Loans held for sale, discount notes, and consolidated obligation bonds, in cases where hedge accounting treatment may not be achieved. Specifically, hedge accounting may not be achieved in cases where it may be difficult to pass prospective or retrospective effectiveness testing under derivative hedge accounting guidance even though the derivatives used to hedge these financial instruments have matching terms. Accordingly, electing the fair value option allows us to better match the change in fair value of these financial instruments with the derivative economically hedging them. We made no adjustments to the fair values of these financial instruments for credit risk as of the reporting periods presented.

The following table summarizes the net gain (loss) related to financial assets and liabilities for which we elected the fair value option.

| | Three months ended March 31, | |
|---|---|---|
| | **2016** | 2015 |
| Advances | **$ 11** | $ 1 |
| Bonds | **(3)** | 2 |
| Discount Notes | **(3)** | — |
| **Net gain (loss) instruments held under fair value option** | **$ 5** | $ 3 |

The following table reflects the difference between the aggregate unpaid principal balance (UPB) outstanding and the aggregate fair value for our long term financial instruments for which the fair value option has been elected. None of the advances were 90 days or more past due and none were on nonaccrual status.

| | **March 31, 2016** | | December 31, 2015 | |
|---|---|---|---|---|
| As of | **Advances** | **Bonds** | Advances | Bonds |
| Unpaid Principal Balance | **$ 592** | **$ 3,808** | $ 509 | $ 953 |
| Fair Value Over (Under) UPB | **13** | **3** | 2 | (1) |
| Fair Value | **$ 605** | **$ 3,811** | $ 511 | $ 952 |

**(Dollars in millions except per share amounts unless otherwise indicated)**

**Note 14 – Commitments and Contingencies**

The following table shows our commitments outstanding, which represent off-balance sheet obligations.

| | **March 31, 2016** | | | December 31, 2015 | | |
|---|---|---|---|---|---|---|
| As of | **Expire within one year** | **Expire after one year** | **Total** | Expire within one year | Expire after one year | Total |
| Unsettled consolidated obligation bonds | **$ 1,075** | **$ —** | **$ 1,075** | $ 105 | $ — | $ 105 |
| Unsettled consolidated obligation discount notes | **599** | **—** | **599** | — | — | — |
| Member standby letters of credit | **5,039** | **2,173** [a] | **7,212** | 5,063 | 1,615 [a] | 6,678 |
| Housing authority standby bond purchase agreements | **35** | **344** | **379** | 49 | 362 | 411 |
| Advance commitments | **151** | **1** | **152** | 163 | 5 | 168 |
| MPF delivery commitments | **399** | **—** | **399** | 279 | — | 279 |
| Other commitments | **61** | **1** | **62** | 48 | 3 | 51 |
| **Commitments** | **$ 7,359** | **$ 2,519** | **$ 9,878** | $ 5,707 | $ 1,985 | $ 7,692 |

[a] Contains $576 million and $637 million of member standby letters of credit at March 31, 2016, and December 31, 2015, which were renewable annually.

For a description of previously defined terms see **Note 17 - Commitments and Contingencies** to the financial statements in our 2015 Form 10-K.

**Note 15 – Transactions with Related Parties and Other FHLBs**

We define related parties as members that own 10% or more of our capital stock or members whose officers or directors also serve on our Board of Directors. Capital stock ownership is a prerequisite to transacting any member business with us. Members and former members own all of our capital stock.

In the normal course of business, we extend credit to or enter into other transactions with these related parties. All transactions are done at market terms that are no more favorable than the terms of comparable transactions with other members who are not considered related parties.

*Members*

The following table summarizes balances we had with our members as defined above as related parties (including their affiliates). Members represented in these tables may change between periods presented, to the extent that our related parties change, based on changes in the composition of our Board membership or percentage of capital stock ownership over 10% as noted in **Note 11 - Capital and Mandatorily Redeemable Capital Stock (MRCS).**

| As of | **March 31, 2016** | December 31, 2015 |
|---|---|---|
| Assets - Interest bearing deposits | **$ 650** | $ 650 |
| Assets - Advances | **11,158** | 15,168 |
| Liabilities - Deposits | **18** | 20 |
| Equity - Capital Stock | **267** | 467 |

*Other FHLBs*

From time to time, we may loan to, or borrow from, other FHLBs. All transactions are done at market terms that are no more favorable than the terms of comparable transactions with other counterparties. These transactions are overnight, maturing the following business day. These transactions with other FHLBs, if any, are identified on the face of our **Financial Statements**.

(Dollars in millions except per share amounts unless otherwise indicated)

**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.**
**Selected Financial Data**

| As of or for the three months ended | March 31, 2016 | December 31, 2015 | September 30, 2015 | June 30, 2015 | March 31, 2015 |
|---|---|---|---|---|---|
| **Selected statements of condition data** | | | | | |
| Total investments [a] | **$ 27,597** | $ 28,324 | $ 28,883 | $ 28,080 | $ 30,816 |
| Advances | **38,353** | 36,778 | 35,044 | 34,553 | 31,941 |
| MPF Loans held in portfolio, gross | **4,681** | 4,831 | 5,082 | 5,377 | 5,732 |
| Less: allowance for credit losses | **(2)** | (3) | (3) | (3) | (4) |
| Total assets | **70,913** | 70,671 | 69,824 | 69,760 | 70,147 |
| Consolidated obligation discount notes, net | **40,293** | 41,564 | 37,290 | 34,552 | 30,474 |
| Consolidated obligation bonds, net | **24,021** | 22,582 | 26,062 | 28,672 | 33,043 |
| Total capital stock | **1,733** | 1,950 | 1,892 | 1,835 | 1,923 |
| Total retained earnings | **2,790** | 2,730 | 2,640 | 2,575 | 2,484 |
| Total capital | **4,413** | 4,652 | 4,573 | 4,549 | 4,579 |
| **Other selected data at period end** | | | | | |
| MPF off-balance sheet loans outstanding FHLB System [b] | **$ 15,664** | $ 15,399 | $ 15,083 | $ 14,840 | $ 14,662 |
| MPF off-balance sheet loans outstanding FHLB Chicago PFIs [b] | **7,827** | 7,785 | 7,765 | 7,725 | 7,681 |
| FHLB systemwide consolidated obligations (par) | **896,828** | 905,202 | 856,511 | 852,783 | 812,196 |
| Number of members | **737** | 740 | 742 | 748 | 745 |
| Total employees (full and part time) | **425** | 422 | 410 | 413 | 408 |
| **Selected statements of income data** | | | | | |
| Net interest income after provision for credit losses | **$ 120** | $ 135 | $ 121 | $ 117 | $ 130 |
| Non-interest gain (loss) | **(3)** | 10 | (6) | 24 | (5) |
| Non-interest expense | **40** | 37 | 35 | 33 | 33 |
| Net income | **69** | 97 | 72 | 97 | 83 |
| **Other selected data during the periods** | | | | | |
| MPF off-balance sheet loan volume funded FHLB System [b] | **$ 703** | $ 849 | $ 807 | $ 800 | $ 698 |
| MPF off-balance sheet loan volume funded FHLB Chicago PFIs [b] | **277** | 329 | 363 | 388 | 357 |
| **Selected ratios (rates annualized)** | | | | | |
| Total regulatory capital to assets ratio | **6.81%** | 6.63% | 6.50% | 6.33% | 6.29% |
| Market value of equity to book value of equity | **107%** | 108% | 108% | 110% | 112% |
| Total investments - % of total assets | **39%** | 40% | 41% | 40% | 44% |
| Advances - % of total assets | **54%** | 52% | 50% | 50% | 46% |
| MPF Loans held in portfolio, net - % of total assets | **7%** | 7% | 7% | 8% | 8% |
| Dividend rate class B1 activity stock-period paid | **2.60%** | 2.50% | 2.25% | 2.25% | 2.25% |
| Dividend rate class B2 membership stock-period paid | **0.60%** | 0.50% | 0.50% | 0.50% | 0.50% |
| Return on average assets | **0.38%** | 0.53% | 0.42% | 0.56% | 0.44% |
| Return on average equity | **5.87%** | 8.44% | 6.31% | 8.51% | 7.34% |
| Average equity to average assets | **6.47%** | 6.28% | 6.66% | 6.58% | 5.99% |
| Net yield on average interest-earning assets | **0.66%** | 0.75% | 0.72% | 0.71% | 0.70% |
| Return on average Regulatory Capital spread to three month LIBOR index | **5.17%** | 7.94% | 6.15% | 8.59% | 7.51% |
| Cash dividends | **$ 9** | $ 7 | $ 7 | $ 6 | $ 5 |
| Dividend payout ratio | **13%** | 7% | 10% | 6% | 6% |

[a] Total investments includes investment securities, interest bearing deposits, Federal Funds sold, and securities purchased under agreements to resell.

[b] MPF off-balance sheet loans are MPF Loans purchased from PFIs and concurrently resold to Fannie Mae or other third party investors under the MPF Xtra and MPF Direct products or pooled and securitized in Ginnie Mae MBS under the MPF Government MBS product. See **Mortgage Partnership Finance Program** beginning on page 7 in our 2015 Form 10-K.

**Forward-Looking Information**

Statements contained in this report, including statements describing the objectives, projections, estimates, or future predictions of management, may be “forward-looking statements.” These statements may use forward-looking terminology, such as “anticipates,” “believes,” “expects,” “could,” “estimates,” “may,” “should,” “will,” their negatives, or other variations of these terms. We caution that, by their nature, forward-looking statements involve risks and uncertainties related to our operations and business environment, all of which are difficult to predict and many of which are beyond our control. These risks and uncertainties could cause actual results to differ materially from those expressed or implied in these forward-looking statements and could affect the extent to which a particular objective, projection, estimate, or prediction is realized. As a result, undue reliance should not be placed on such statements.

These forward-looking statements involve risks and uncertainties including, but not limited to, the following:

- changes in the demand by our members for advances, including the impact of the availability of other sources of funding for our members, such as deposits;
- limits on our investments in long-term assets;
- the impact of new business strategies, including our ability to develop and implement business strategies focused on maintaining net interest income; the impact of our efforts to simplify our balance sheet on our market risk profile and future hedging costs; our ability to execute our business model, implement business process improvements and scale our size to our members' borrowing needs; the extent to which our members use our advances as part of their core financing rather than just as a back-up source of liquidity; and our ability to implement product enhancements and new products and generate enough volume in new products to cover our costs related to developing such products;
- the extent to which amendments to our Capital Plan, including our ability to reduce capital stock requirements for certain future advance borrowings, and our ability to continue to pay enhanced dividends on our activity stock, impact borrowing by our members;
- our ability to meet required conditions to repurchase and redeem capital stock from our members (including maintaining compliance with our minimum regulatory capital requirements and determining that our financial condition is sound enough to support such repurchases), and the amount and timing of such repurchases or redemptions;
- general economic and market conditions, including the timing and volume of market activity, inflation/deflation, unemployment rates, housing prices, the condition of the mortgage and housing markets, increased delinquencies and/or loss rates on mortgages, prolonged or delayed foreclosure processes, and the effects on, among other things, mortgage-backed securities; volatility resulting from the effects of, and changes in, various monetary or fiscal policies and regulations, such as those determined by the Federal Reserve Board and Federal Deposit Insurance Corporation; impacts from various measures to stimulate the economy and help borrowers refinance home mortgages and student loans; disruptions in the credit and debt markets and the effect on future funding costs, sources, and availability;
- volatility of market prices, rates, and indices, or other factors, such as natural disasters, that could affect the value of our investments or collateral; changes in the value or liquidity of collateral securing advances to our members;
- changes in the value of and risks associated with our investments in mortgage loans, mortgage-backed securities, and FFELP ABS and the related credit enhancement protections;
- changes in our ability or intent to hold mortgage-backed securities to maturity;
- changes in mortgage interest rates and prepayment speeds on mortgage assets;

- membership changes, including the withdrawal of members due to restrictions on our dividends or the loss of members through mergers and consolidations; changes in the financial health of our members, including the resolution of some members; risks related to expanding our membership to include more institutions with regulators and resolution processes with which we have less experience;

- increased reliance on short-term funding and changes in investor demand and capacity for consolidated obligations and/or the terms of interest rate derivatives and similar agreements, including changes in the relative attractiveness of consolidated obligations as compared to other investment opportunities; changes in our cost of funds due to concerns over U.S. fiscal policy, and any related rating agency actions impacting FHLB consolidated obligations;

- political events, including legislative, regulatory, judicial, or other developments that affect us, our members, our counterparties and/or investors in consolidated obligations, including, among other things, the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) and related regulations and proposals and legislation related to housing finance and GSE reform; changes by our regulator and changes in the FHLB Act or applicable regulations as a result of the Housing and Economic Recovery Act of 2008 (Housing Act) or as may otherwise be issued by our regulator, including regulatory changes to FHLB membership requirements proposed by the FHFA; the potential designation of us as a nonbank financial company for supervision by the Federal Reserve;

- the ability of each of the other FHLBs to repay the principal and interest on consolidated obligations for which it is the primary obligor and with respect to which we have joint and several liability;

- the pace of technological change and our ability to develop and support technology and information systems, including our ability to protect the security of our information systems and manage any failures, interruptions or breaches in our information systems or technology services provided to us through third-party vendors;

- our ability to attract and retain skilled employees;

- the impact of new accounting standards and the application of accounting rules, including the impact of regulatory guidance on our application of such standards and rules;

- the volatility of reported results due to changes in the fair value of certain assets and liabilities; and

- our ability to identify, manage, mitigate, and/or remedy internal control weaknesses and other operational risks.

For a more detailed discussion of the risk factors applicable to us, see **Risk Factors** in our 2015 Form 10-K on page 19.

These forward-looking statements are representative only as of the date they are made, and we undertake no obligation to update any forward-looking statement as a result of new information, future events, changed circumstances, or any other reason.

## Executive Summary

### First Quarter 2016 Financial Highlights

- We recorded net income of $69 million in the first quarter of 2016, down from $83 million in the first quarter of 2015.
- Net interest income for the first quarter of 2016 was $120 million, down from $130 million for the first quarter of 2015 as our higher earning investment and MPF Loan portfolios continued to pay down, while our costs of funding rose slightly.
- Total investment securities decreased 6% to $23.1 billion at March 31, 2016, down from $24.6 billion at December 31, 2015 as our investment portfolio continued to pay down.
- Advances outstanding increased $1.6 billion to $38.4 billion at March 31, 2016, up from $36.8 billion at December 31, 2015, as members support investment activities and loan growth in their communities.
- Total assets remained relatively unchanged at $70.9 billion as of March 31, 2016, compared to $70.7 billion as of December 31, 2015.
- We reached nearly $2.8 billion in retained earnings at March 31, 2016.
- We remained in compliance with all of our regulatory capital requirements as of March 31, 2016.

### Summary and Outlook

*First Quarter 2016 Dividend*

On April 26, 2016, the Bank's Board of Directors increased the dividend declared per share of Class B1 activity capital stock by 20 basis points to again recognize our members that borrow from the Bank, which supports the health of the entire cooperative. The higher dividend, in effect, lowers members' cost of doing business with the Bank. The Board maintained the dividend declared for Class B2 membership capital stock. Based on the Bank's preliminary financial results for the first quarter of 2016, the Board declared a dividend of 2.80% (annualized) for Class B1 activity capital stock and a dividend of 0.60% (annualized) for Class B2 membership capital stock.

*Enhancing the Value of Membership*

We remain focused on serving our members and committed to using our financial strength to enhance the value of their membership. To that end, in February we announced significant reductions in membership stock and activity stock requirements, which went into effect on April 1, 2016. The changes reflect our vision to lower members' cost of membership and increase their return on activity-all while maintaining their access to the same level of funding and liquidity. As a result of these changes, most institutions own excess stock that is eligible to be repurchased so that they can invest those funds in their business and their communities. We held $593 million of excess capital stock on April 1, 2016. As of April 30, 2016, we held excess capital stock of $422 million. The reduction was a result of members requesting repurchase of their excess stock and members utilizing excess stock to support new advance borrowing activities.

(Dollars in millions except per share amounts unless otherwise indicated)

## Results of Operations

### Net Interest Income

Net interest income is the difference between the amount we recognize into interest income on our interest earning assets and the amount we recognize into interest expense on our interest bearing liabilities. These amounts were determined in accordance with GAAP and were based on the underlying contractual interest rate terms of our interest earning assets and interest bearing liabilities as well as the following items:

- Net interest paid or received on interest rate swaps that are accounted for as fair value or cash flow hedges;
- Amortization of premiums;
- Accretion of discounts;
- Amortization of hedge adjustments;
- Advance prepayment fees; and
- MPF credit enhancement fees.

The tables below present the increase or decrease in interest income and expense due to volume or rate variances. The calculation of these components includes the following considerations:

- Average daily balances are computed using historical amortized cost balances except for trading securities and items carried under the fair value option, which both immediately recognize changes in fair value into our statements of income.
- MPF Loans held in portfolio that are on nonaccrual status are included in average daily balances used to determine the effective yield/rate. Amounts included in interest income on MPF Loans held in portfolio are presented as detailed in **MPF Loans Held in Portfolio, Net of Allowance for Credit Losses** on page 45.
- Interest and effective yield/rate includes all components of net interest income as discussed above. Yields/rates are calculated on an annualized basis.
- Any changes due to the combined volume/rate variance have been allocated ratably to volume and rate.

| | **March 31, 2016** | | | March 31, 2015 | | | **Increase (decrease) due to** | | |
|---|---|---|---|---|---|---|---|---|---|
| For the three months ended | **Average Balance** | **Total Interest** | **Yield/ Rate** | Average Balance | Total Interest | Yield/ Rate | **Volume** | **Rate** | **Net Change** |
| Federal Funds sold, securities purchased under agreements to resell, and interest bearing deposits | **$ 5,777** | **$ 5** | **0.35%** | $ 11,187 | $ 3 | 0.11% | **$ (1)** | **$ 3** | **$ 2** |
| Investment securities | **23,339** | **193** | **3.31%** | 25,676 | 204 | 3.18% | **(19)** | **8** | **(11)** |
| Advances | **38,340** | **63** | **0.66%** | 31,704 | 45 | 0.57% | **9** | **9** | **18** |
| MPF Loans held in portfolio | **4,729** | **57** | **4.82%** | 5,788 | 69 | 4.77% | **(13)** | **1** | **(12)** |
| **Interest Income on Assets** | **72,185** | **318** | **1.76%** | 74,355 | 321 | 1.73% | **(24)** | **21** | **(3)** |
| Consolidated obligation discount notes | **43,283** | **82** | **0.76%** | 36,273 | 72 | 0.79% | **14** | **(4)** | **10** |
| Consolidated obligation bonds | **22,838** | **102** | **1.79%** | 32,706 | 105 | 1.28% | **(32)** | **29** | **(3)** |
| Subordinated notes | **944** | **14** | **5.93%** | 944 | 14 | 5.93% | **—** | **—** | **—** |
| **Interest Expense on Liabilities** | **67,065** | **198** | **1.18%** | 69,923 | 191 | 1.09% | **(18)** | **25** | **7** |
| **Net yield on interest-earning assets** | **$ 72,185** | **$ 120** | **0.66%** | $ 74,355 | $ 130 | 0.70% | **$ (6)** | **$ (4)** | **$ (10)** |

Net interest income changed mainly due to the following:

- Interest income from investment securities declined primarily due to the decline in average investment balances as securities matured or paid down. Our ability to make new investments that have a term to maturity in excess of 270 days is restricted. For further information, see **Investments** on page 12 in our 2015 Form 10-K. This decline was partially offset by accretion into interest income of expected improvements in the present value of cash flows on securities that were previously charged with credit related OTTI. For the year to date through March 31, 2016, we recorded additional interest income of $13 million due to such accretion. For the same period in 2015, accretion was $15 million. Accretion is dependent upon how estimated market conditions impact future projected cash flows, and may vary from past experience.

- Interest income from advances increased due to higher member demand for advances and also due to increases in interest rates, primarily as a result of the Federal Reserve Bank's actions at year end 2015. The following were key factors resulting in the increased demand by members for advances.

    - The funding needs of our members in Illinois and Wisconsin have increased as the economic activity in our district continues to improve.

    - The benefits we offer our members through our continuing Reduced Capitalization Advance Program (RCAP), which is designed to make the net cost of borrowing through advances more attractive to members.

- Interest income from MPF Loans held in portfolio continued to decline as expected due to the net decrease in our outstanding MPF Loans held in portfolio. Though we had a net decrease in our outstanding MPF Loans, we resumed purchasing a material amount of MPF Loans in 2016 compared to 2015, as noted in our **Condensed Statements of Cash Flows** on page 7. However, we do not expect our purchases of new MPF Loans to be large enough to offset our current loan paydown activity in the near-term, but may do so in the future.

- Interest expense increased, primarily due to higher rates on our consolidated obligation bonds, partially offset by a slight decline in overall debt outstanding. Rates on our bonds outstanding increased primarily in bonds due in less than one year.

- Our hedging activities also contributed a net reduction to net interest income. The low interest rate environment resulted in negative net interest settlements on derivative contracts in active hedge accounting relationships. For further details see **Trading Securities, Derivatives and Hedging Activities, and Instruments Held at Fair Value Option** on page 41.

**(Dollars in millions except per share amounts unless otherwise indicated)**

**Non-Interest Gain (Loss)**

| | Three months ended March 31, | |
|---|---|---|
| | **2016** | 2015 |
| Trading securities | **$ 1** | $ (1) |
| Derivatives and hedging activities | **(16)** | (11) |
| Instruments held under fair value option | **5** | 3 |
| **Trading Securities, Derivatives and Hedging Activities, and Instruments Held Under Fair Value Option** | **(10)** | (9) |
| Other, net | **7** | 4 |
| **Noninterest gain (loss)** | **$ (3)** | $ (5) |

*Trading Securities, Derivatives and Hedging Activities, and Instruments Held Under Fair Value Option*

Gains (losses) on these activities have generally stabilized in recent years primarily as a result of less volatile hedging costs, which is consistent with the hedging strategies for our more simplified balance sheet, along with a more stable economy. However, most of our total net effect from hedging activities was recorded as a component of net interest income, not included in the above line items. The low interest rate environment resulted in negative net interest settlements on derivative contracts in active hedge accounting relationships. Details of these activities as well as all hedging activities are in the table on the following page.

*Other, net*

Other, net, consists primarily of income from the sale of MPF Loans to third party investors and fees other FHLBs pay us to support their participation in the MPF Program, which offsets a portion of the expenses we incur.

*Litigation settlement awards*

On October 15, 2010, we instituted litigation relating to 64 private-label MBS bonds we purchased in an aggregate original principal amount of $4.29 billion. In April 2016, we received a payment of $37.5 million (partially offset by $5.0 million of related legal fees and other expenses) resulting from a settlement with some of the defendants. We continue to pursue litigation related to these matters. As of April 30, 2016, the remaining litigation covers four private-label MBS bonds in the aggregate original principal amount of $77.5 million. We cannot predict to what extent we will be successful in this remaining litigation. See **Legal Proceedings** on page 58 for further details.

(Dollars in millions except per share amounts unless otherwise indicated)

The following table shows the impact of Trading Securities, Derivatives and Hedging Activities, and Instruments Held Under Fair Value Option on our results of operations. The largest contributor to the total net effect gain (loss) of hedging activities is net interest settlements, which represents interest income or interest expense on derivatives included in net interest income of the underlying hedged item.

| | Advances | Investments | MPF Loans | Discount Notes | Bonds | Total |
|---|---|---|---|---|---|---|
| **Three months ended March 31, 2016** | | | | | | |
| Amortization/accretion | $ 2 | $ (4) | $ (2) | $ — | $ (4) | $ (8) |
| Net interest settlements | (20) | (30) | — | (47) | 25 | (72) |
| **Total recorded in net interest income** | (18) | (34) | (2) | (47) | 21 | (80) |
| Fair value hedges - ineffectiveness net gain (loss) | (1) | (3) | — | — | (5) | (9) |
| Economic hedges - net gain (loss) | (13) | — | 4 | (1) | 3 | (7) |
| **Total recorded derivatives & hedging activities** | (14) | (3) | 4 | (1) | (2) | (16) |
| Trading securities - hedged | — | 1 | — | — | — | 1 |
| Instruments held under fair value option | 11 | — | — | (3) | (3) | 5 |
| **Total net effect gain (loss) of hedging activities** | $ (21) | $ (36) | $ 2 | $ (51) | $ 16 | $ (90) |
| | | | | | | |
| Three months ended March 31, 2015 | | | | | | |
| Amortization/accretion | $ 4 | $ (10) | $ (4) | $ (1) | $ (1) | $ (12) |
| Net interest settlements | (20) | (34) | — | (62) | 58 | (58) |
| **Total recorded in net interest income** | (16) | (44) | (4) | (63) | 57 | (70) |
| Fair value hedges - ineffectiveness net gain (loss) | (4) | (5) | — | — | (10) | (19) |
| Economic hedges - net gain (loss) | (2) | — | 2 | 2 | 6 | 8 |
| **Total recorded derivatives & hedging activities** | (6) | (5) | 2 | 2 | (4) | (11) |
| Instruments held under fair value option | 1 | — | — | — | 2 | 3 |
| **Total net effect gain (loss) of hedging activities** | $ (21) | $ (49) | $ (2) | $ (61) | $ 55 | $ (78) |

(Dollars in millions except per share amounts unless otherwise indicated)

**Noninterest Expense**

| | Three months ended March 31, | |
|---|---|---|
| | **2016** | 2015 |
| Compensation and benefits | **$ 23** | $ 19 |
| Other operating expenses | **15** | 11 |
| Other | **2** | 3 |
| **Noninterest expense** | **$ 40** | $ 33 |

Compensation and benefits increased primarily due to defined benefit pension costs and other post retirement benefit related expenses, driven in part by the continued low interest rate environment and a change in the mortality tables used to calculate the estimated pension liability. We had 425 employees as of March 31, 2016, compared to 422 as of December 31, 2015.

Other operating expenses increased mostly due to our continued investment in information technology, which was primarily general infrastructure maintenance, security, and investment in systems related to the MPF Program.

**Assessments**

We fund the Affordable Housing Program (AHP) program at a calculated rate of 10% of income before assessments.

(Dollars in millions except per share amounts unless otherwise indicated)

**Other Comprehensive Income (Loss)**

| | Three months ended March 31, | |
|---|---|---|
| | **2016** | 2015 |
| Net unrealized gain (loss) available-for-sale securities | **$ (40)** | $ (22) |
| Non-credit OTTI held-to-maturity securities | **11** | 13 |
| Net unrealized gain (loss) cash flow hedges | **(53)** | (28) |
| Post-retirement plans | **—** | (8) |
| **Other comprehensive income (loss)** | **$ (82)** | $ (45) |

*Net unrealized gain (loss) on available-for-sale securities*

The increase in net unrealized losses on available-for-sale securities was due to general market-related declines and the reversal of previous unrealized gain positions in AOCI related to available-for-sale portfolio securities. We continued to have an unrealized net gain position related to our available-for-sale securities portfolio in AOCI as of March 31, 2016. If we do not sell these securities prior to their maturity, this remaining unrealized net gain position in AOCI will eventually reverse to zero.

*Non-credit OTTI on held-to-maturity securities*

The decrease in gains on our non-credit OTTI held-to-maturity securities during the first quarter of 2016 compared to the first quarter of 2015 was due to a decrease in the rate of accretion reversing previously recorded non-credit OTTI losses for held-to-maturity securities. As these securities approach maturity, we expect the accretion to continue as principal and interest are received from the securities, unless there are additional OTTI credit losses.

*Net unrealized gain (loss) on cash flow hedges*

The increase in unrealized losses on our cash flow hedges during the first quarter of 2016 compared to the OCI (loss) in the first quarter of 2015 was due to shorter-term market interest rates remaining stable while longer-term rates rose over the last three years. Our cash flow hedges are more sensitive to changes in longer-term market interest rates than to changes in shorter-term market interest rates. We had a net unrealized (loss) position in AOCI related to our cash flow hedges as of March 31, 2016. We reclassify amounts in AOCI into our statements of income in the same period or periods during which the hedged forecasted transaction affects our earnings.

*Post-retirement plans*

The OCI (loss) in 2015 was due to a revision to the mortality tables we use for our post-retirement healthcare and supplemental defined benefit equalization plan and is being amortized into compensation and benefits expense over the average number of years employment remaining before retirement. The annual amount of amortization is expected to be less than $1 million.

For further information on the activity in Other Comprehensive Income (Loss) see **Note 12 - Accumulated Other Comprehensive Income (Loss)** to the financial statements.

(Dollars in millions except per share amounts unless otherwise indicated)

**Statements of Condition**

| | March 31, 2016 | December 31, 2015 |
|---|---|---|
| Cash and due from banks, interest bearing deposits, Federal Funds sold, and securities purchased under agreement to resell | $ 4,543 | $ 4,226 |
| Investment securities | 23,087 | 24,597 |
| Advances | 38,353 | 36,778 |
| MPF Loans held in portfolio, net of allowance for credit losses | 4,679 | 4,828 |
| Other | 251 | 242 |
| **Assets** | $ 70,913 | $ 70,671 |
| | | |
| Consolidated obligation discount notes | $ 40,293 | $ 41,564 |
| Consolidated obligation bonds | 24,021 | 22,582 |
| Subordinated notes | 944 | 944 |
| Other | 1,242 | 929 |
| **Liabilities** | 66,500 | 66,019 |
| | | |
| Capital stock | 1,733 | 1,950 |
| Retained earnings | 2,790 | 2,730 |
| Accumulated other comprehensive income (loss) | (110) | (28) |
| **Capital** | 4,413 | 4,652 |
| **Total liabilities and capital** | $ 70,913 | $ 70,671 |

**Cash and due from banks, interest bearing deposits, Federal Funds sold, and securities purchased under agreements to resell**

Amounts held in these accounts will vary each day based on the following:

- Interest rate spreads between Federal Funds sold and securities purchased under agreements to resell and our debt;
- Liquidity requirements;
- Counterparties available; and
- Collateral availability on securities purchased under agreements to resell.

**Investment Securities**

We are required to obtain FHFA approval for any new investments that have a term to maturity in excess of 270 days until such time as our MBS portfolio is less than three times our total regulatory capital and our advances represent more than 50% of our total assets. For purposes of calculating the limit on our MBS portfolio, we value our investment in MBS in accordance with FHFA regulations based on amortized cost for securities classified as held-to-maturity or available-for-sale and on fair value for trading securities. Regulatory capital consists of our total capital stock (including mandatorily redeemable capital stock) plus our retained earnings. At March 31, 2016, our MBS portfolio was 3.05 times our total regulatory capital and our advances represented 54% of our total assets.

**Advances**

Member demand for advances continued to increase in 2016 even after a significant increase during 2015. We are finding that our members in Illinois and Wisconsin have experienced increased funding needs as the economic activity in our district continues to improve. In addition, members are taking advantage of the lower net cost of borrowing from our continuing Reduced Capitalization Advance Program (RCAP) and our building member collateral capacity as discussed on page 63 in our Form 2015 10-K. While our advances increased, it is possible that member demand for our advances could decline in future periods should their funding needs change, or to the extent they elect alternative funding resources. In addition, as our advances with captive insurance companies mature, our total advance levels could decrease as further discussed in **Legislative and Regulatory Developments** on page 53 in this Form 10-Q.

**MPF Loans Held in Portfolio, Net of Allowance for Credit Losses**

MPF Loans continued to pay down as expected, a result of our past business strategy to limit the balance sheet concentration of our MPF Loans. Though we have begun adding new MPF Loans to our portfolio, we do not expect these new MPF Loans to be large enough to offset loan paydowns anticipated in the near-term. For the year to date period ended March 31, 2016, we have added $132 million in new MPF Loans to our portfolio.

In addition to our MPF Loans held in portfolio, we have MPF off-balance sheet products, where we buy and concurrently resell MPF Loans to Fannie Mae or other third party investors or pool and securitize them into Ginnie Mae MBS.

**Liquidity, Funding, & Capital Resources**

**Liquidity**

For the period ending March 31, 2016, we have maintained a liquidity position in accordance with FHFA regulations and guidance, and policies established by our Board of Directors. Based upon our excess liquidity position described below, we anticipate remaining in compliance with our liquidity requirements. See **Liquidity, Funding, & Capital Resources** on page 48 in our 2015 Form 10-K for a detailed description of our liquidity requirements. We use different measures of liquidity as follows:

Overnight Liquidity – Our policy requires us to maintain overnight liquid assets at least equal to 3.5% of total assets. As of March 31, 2016, our overnight liquidity was $7.2 billion or 10% of total assets, giving us an excess overnight liquidity of $4.7 billion.

Deposit Coverage – To support our member deposits, FHFA regulations require us to have an amount equal to the current deposits invested in obligations of the U.S. Government, deposits in eligible banks or trust companies, or advances with maturities not exceeding five years. As of March 31, 2016, we had excess liquidity of $38.2 billion to support member deposits.

Contingency Liquidity – The cumulative five business day liquidity measurement assumes there is a localized credit crisis for all FHLBs where the FHLBs do not have the ability to issue new consolidated obligations or borrow unsecured funds from other sources (e.g., purchasing Federal Funds or customer deposits). Our net liquidity in excess of our total uses and reserves over a cumulative five-business-day period was $17.1 billion as of March 31, 2016.

In addition to the liquidity measures discussed above, FHFA guidance requires us to maintain daily liquidity through short-term investments in an amount at least equal to anticipated cash outflows under two different scenarios. We may fund overnight or shorter term investments and advances with discount notes that have maturities that extend beyond the maturities of the related investments or advances. For a discussion of how this may impact our earnings, see page 22 in the **Risk Factors** section of our 2015 Form 10-K.

**Funding**

*Conditions in Financial Markets*

During the first quarter of 2016, the Federal Open Market Committee (FOMC) delayed further interest rate hikes after finally increasing interest rates at the December meeting raising the target range for the federal funds rate to 25 basis points to 50 basis points from 0 basis points to 25 basis points. Slowing global growth, financial turmoil and falling oil prices contributed to the delayed interest rate hikes; the 10-Year Treasury fell 47 basis points on the quarter ending at 1.77 percent.

We maintained ready access to funding during the quarter.

*Cash flows from operating activities*

Our operating assets and liabilities support our mission to provide our member shareholders competitively priced funding, a reasonable return on their investment in our capital stock, and support for community investment activities. Operating assets and liabilities can vary significantly in the normal course of business due to the amount and timing of cash flows, which are affected by member-driven activities and market conditions. We believe cash flows from operations, available cash balances and our ability to generate cash through short- and long-term borrowings are sufficient to fund our operating liquidity needs. Net cash provided by (used in) operating activities was $(9) million for the three months ended March 31, 2016. This resulted from net income adjusted for non-cash adjustments, which primarily is attributable to a positive net change in the fair value of derivatives and hedging activities partially offset by a net increase in accrued interest payable.

*Cash flows from investing activities*

Our investing activities predominantly include advances, MPF Loans held for investment, investment securities, and other short-term interest-earning assets. Net cash provided by (used in) investing activities was $(553) million for the three months ended March 31, 2016. This resulted primarily from a net increase in advances funded, and a net increase in Federal Funds sold, partially offset by maturities related to held-to-maturity and available-for-sale investment securities and a net increase in securities sold under agreement to repurchase. The net increase in advances and the shift away from investment securities is consistent with our objective to make advances to our members our primary business.

**(Dollars in millions except per share amounts unless otherwise indicated)**

*Cash flows from financing activities*

Our financing activities primarily reflect cash flows related to issuing and repaying consolidated obligations. Net cash provided by (used in) financing activities was $96 million for the three months ended March 31, 2016. This was primarily driven by proceeds from the issuance of our capital stock and a net increase in issuances related to our consolidated obligation bonds partially offset by a net decrease in in our consolidated obligation discount notes.

*Consolidated Obligation Bonds and Discount Notes*

We fund our assets principally with consolidated obligations (bonds and discount notes) issued through the Office of Finance, and capital stock. Consolidated obligations have GSE status although they are not obligations of the United States and the United States does not guarantee them.

During the first three months of 2016, we relied more on bonds to fund our assets as discount notes matured. For the comparable period in 2015, discount notes and bonds decreased in a manner consistent with the decline in the level of assets being funded. For further discussion of our reliance on discount note funding, see page 24 of the **Risk Factors** section of our 2015 Form 10-K.

The following shows our net cash flow issuances (redemptions) by type of consolidated obligation:

| Three months ended March 31, | **2016** | 2015 |
|---|---|---|
| Discount notes | **$ (1,280)** | $ (583) |
| Bonds | **1,360** | (1,294) |
| Total consolidated obligations | **$ 80** | $ (1,877) |

## Capital Resources

*Capital Rules*

Under our Second Amended and Restated Capital Plan of the Federal Home Loan Bank of Chicago, effective October 1, 2015 (Capital Plan), our stock consists of two sub-classes of stock, Class B1 activity stock and Class B2 membership stock (together, Class B stock), both with a par value of $100 and redeemable on five years' written notice, subject to certain conditions. Each member is required to own capital stock in an amount equal to the greater of a membership stock requirement or an activity stock requirement. Class B1 activity stock is available for purchase only to support a member's activity stock requirement. Class B2 membership stock is available to be purchased to support a member's membership stock requirement and any activity stock requirement.

Under our Capital Plan, our Board of Directors may set a threshold of between $10,000 and $75 million on the amount of Class B2 membership stock that would otherwise be held for membership if a member has advances outstanding that have an activity stock requirement in excess of the threshold amount. In that case, the amount of Class B2 membership stock that exceeds such threshold and is necessary to support advance activity is automatically converted into Class B1 activity stock. That threshold is currently set at $10,000, which means that we will convert to Class B1 activity capital stock any capital stock supporting advances that exceeds the lesser of the member's membership requirement or $10,000.

The Board of Directors may periodically adjust members' activity stock requirement for certain new advances within a range of 2% and 6% of a member's outstanding advances. Our Board implemented this provision through RCAP as further discussed below. In addition, our Board reduced each member's activity stock requirement from 5% to 4.5% for non-RCAP advances, effective April 1, 2016.

Our Capital Plan allows for an activity stock requirement for MPF Loans acquired for our portfolio within a range of 0% and 6%, which our Board has set at 0%. Should the Board decide to introduce this capital requirement, we intend to notify members sufficiently in advance of the change and apply that change only to future acquisitions.

The Board may periodically adjust members' membership stock requirement within a range of 0.20% to 2% of a member's mortgage assets. In February 2016, our Board reduced the membership stock requirement to the greater of either $10,000 or 0.40% of a member's mortgage assets. A member's investment in membership stock is subject to a cap equal to the lesser of (1) a dollar cap set by the Board within a range of $10,000 and $75 million, and (2) 9.9% of our total capital stock outstanding as of the prior December 31. Also in February 2016 , the Board reduced the dollar cap on membership stock from $25 million to $5 million, which is less than 9.9% of the Bank's total capital stock at December 31, 2015, and thus the operative cap during the remainder of 2016 unless the Board sets a new cap.

**(Dollars in millions except per share amounts unless otherwise indicated)**

Membership stock requirements will continue to be recalculated annually, whereas the activity stock requirement and any automatic conversion of Class B2 membership stock to Class B1 activity stock related to the threshold will apply on a daily basis. The revised membership stock and activity stock requirements discussed above went into effect on April 1, 2016. As a result of these changes, we held $593 million of excess capital stock on April 1, 2016. As of April 30, 2016, we held excess capital stock of $422 million. The reduction was a result of members requesting repurchase of their excess stock and members utilizing excess stock to support new advance borrowing activities.

We may only redeem or repurchase capital stock from a member if, following the redemption or repurchase, the member continues to meet its minimum investment requirement and we remain in compliance with our regulatory capital requirements discussed below.

Members that withdraw from membership must wait at least five years after their membership was terminated and all of their capital stock was redeemed or repurchased before being readmitted to membership in any FHLB.

Under the terms of our Capital Plan, our Board of Directors is authorized to amend the Capital Plan, and the FHFA must approve all such amendments before they become effective.

*Reduced Capitalization Advance Program*

Since June 2015, we have offered RCAP on a monthly basis. RCAP allows members to borrow one or more advances with an activity stock requirement of only 2% for the life of the advance instead of the 4.5% requirement under our Capital Plan's general provisions, if the new advances represent an incremental increase in a member's overall level of advances and have maturity dates of at least one year.

*Capital Amounts*

The following table reconciles our capital reported in our statements of condition to the amount of capital stock reported for regulatory purposes. MRCS is included in the calculation of the regulatory capital and leverage ratios but is recorded in Other liabilities in our statements of condition.

| | **March 31, 2016** | December 31, 2015 | **Change** |
|---|---|---|---|
| Capital stock | **$ 1,733** | $ 1,950 | **$ (217)** |
| Total retained earnings | **2,790** | 2,730 | **60** |
| Accumulated other comprehensive income (loss) | **(110)** | (28) | **(82)** |
| **Total GAAP capital** | **$ 4,413** | $ 4,652 | **$ (239)** |
| | | | |
| Capital Stock | **$ 1,733** | $ 1,950 | **$ (217)** |
| MRCS | **302** | 8 | **294** |
| Total retained earnings | **2,790** | 2,730 | **60** |
| **Regulatory capital** | **$ 4,825** | $ 4,688 | **$ 137** |

Although we have had no OTTI in 2016, credit deterioration may negatively impact our remaining private-label MBS portfolio. We believe that future impairments of this portfolio are possible if unemployment rates, default, delinquency, or loss rates on mortgages were to increase, or there is a further decline in residential real estate value. We cannot predict if or when such impairments will occur, or the impact such impairments may have on our retained earnings and capital position. See page 28 of the **Risk Factors** section of our 2015 Form 10-K.

We may not pay dividends if we fail to satisfy our minimum capital and liquidity requirements under the FHLB Act and FHFA regulations.

(Dollars in millions except per share amounts unless otherwise indicated)

On April 26, 2016, our Board of Directors increased the dividend declared per share on Class B1 activity stock by 20 basis points and maintained the dividend declared on Class B2 membership stock by declaring a cash dividend at an annualized rate of 2.80% (annualized) for Class B1 activity stock and 0.60% (annualized) for Class B2 membership stock based on our preliminary financial results for the first quarter of 2016. This dividend, including dividends on mandatorily redeemable capital stock, totals $11 million and will be paid on May 12, 2016. With this action, the Board continues and enhances the practice of rewarding members that use the Bank's advances and support the financial health of the entire cooperative. Although we continue to work to maintain our financial strength to support a reasonable dividend, any future dividend determination by our Board will be at our Board's sole discretion and will depend on future operating results, our Retained Earnings and Dividend Policy and any other factors the Board determines to be relevant. For further information about our Retained Earnings and Dividend Policy, see **Retained Earnings and Dividend Policy** on page 57 in our 2015 Form 10-K**.**

We continue to allocate 20% of our net income each quarter to a restricted retained earnings account in accordance with the Joint Capital Enhancement Agreement that we entered into with the other FHLBs, as further discussed in **Joint Capital Enhancement Agreement** on page F-43 in our 2015 Form 10-K.

**Critical Accounting Policies**

The table below identifies our critical accounting policies and estimates and the page number where a detailed description of each can be found in our 2015 Form 10-K.

| | |
|---|---|
| *Estimating Credit Losses* | Page 60 |
| *Estimating Fair Value* | Pages 60-61 |

See **Note 2 - Summary of Significant Accounting Policies** and **Note 3 - Recently Issued but Not Yet Adopted Accounting Standards** to the financial statements in this Form 10-Q for the impact of changes in accounting policies and recently issued accounting standards on our financial results.

**(Dollars in millions except per share amounts unless otherwise indicated)**

**Risk Management - Credit Risk**

*Managing Our Credit Risk Exposure Related to Member Credit Products*

Our credit risk rating system focuses primarily on our member's overall financial health and takes into account the member's asset quality, earnings, and capital position. For further information please see **Member Credit Risk Ratings** on page 63 in our 2015 Form 10-K.

The following table presents the number of members and related credit outstanding to them by credit risk rating. Credit outstanding consists primarily of outstanding advances and letters of credit. MPF credit enhancement obligations, member derivative exposures, and other obligations make up the rest. Of the total credit outstanding, $38.1 billion were advances (par value) and $7.2 billion were letters of credit at March 31, 2016, compared to $36.6 billion and $6.7 billion at December 31, 2015.

| | **March 31, 2016** | | | | | December 31, 2015 | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| Rating | **Number of Members** | **% of Total** | **Credit Outstanding** | **% of Total** | **Collateral Loan Value** | Number of Members | % of Total | Credit Outstanding | % of Total | Collateral Loan Value |
| 1-3 | **486** | **95%** | **$ 45,188** | **100%** | **$ 92,943** | 482 | 94% | $ 43,090 | 100% | $ 90,366 |
| 4 | **9** | **2%** | **60** | **—%** | **150** | 12 | 2% | 158 | —% | 318 |
| 5 | **15** | **3%** | **145** | **—%** | **229** | 20 | 4% | 145 | —% | 353 |
| Total | **510** | **100%** | **$ 45,393** | **100%** | **$ 93,322** | 514 | 100% | $ 43,393 | 100% | $ 91,037 |

*MPF Loans and Related Exposures*

For details on our allowance for credit losses on MPF Loans, please see the **MPF Risk Sharing Structure** on page F-14 in our 2015 Form 10-K.

Mortgage Repurchase Risk

We are exposed to mortgage repurchase risk in connection with our sale of MPF Loans to third party investors and MPF Loans securitized into MBS when a loan eligibility requirement or other warranty is breached. We may require the PFI from which we purchased the ineligible MPF Loan to repurchase that loan from us or indemnify us for related losses.

For the three months ended March 31, 2016, we have repurchased $3 million of unpaid principal balances related to MPF Loans. Due to recoveries from PFIs, we incurred no material losses on these loans. As of March 31, 2016, we have $37 million of unpaid principal with respect to mortgage loans that represent unresolved claims with investors, in which a repurchase demand may occur, compared to $38 million at December 31, 2015; see **Note 14 -Commitments and Contingencies** to the financial statements.

For further details, see **Mortgage Repurchase Risk** on page 66 in our 2015 Form 10-K.

**(Dollars in millions except per share amounts unless otherwise indicated)**

*Investment Securities*

We hold a variety of investment securities we believe are low risk and mostly government backed or insured such as GSE debt, and FFELP ABS. There was no material change in the credit ratings of these AA or better rated securities since December 31, 2015, and except for private-label MBS as noted below, we have never taken an impairment charge on these securities. For further details see page 69 in our 2015 Form 10-K.

Our private-label MBS are predominantly variable rate securities rated below investment grade (BBB). There was no material change in overall credit quality since December 31, 2015, nor have we acquired any new private-label MBS. We last had an other-than-temporary impairment (OTTI) loss on private-label MBS in 2012. We currently have unrealized gains on these securities as their market values have improved from the impaired values and subsequent to 2012 we have begun recording accretion gains on these securities back into income. For further details see Note 5 - Investments Securities to the financial statements in this Form 10-Q as well as pages F-27 and F-28 in our 2015 Form 10-K.

*Unsecured Short-Term Investments Credit Exposure*

For further details on our unsecured short-term investments as well as policies and procedures to limit and monitor our unsecured credit risk exposure, see page 72 in our 2015 Form 10-K.

The following table presents the credit ratings of our unsecured investment credit exposures by the domicile of the counterparty or the domicile of the counterparty's parent for U.S. branches and agency offices of foreign commercial banks. This table does not reflect the foreign sovereign government's credit rating. The unsecured investment credit exposure presented in the table may not reflect the average or maximum exposure during the period as the table reflects only the balances at period end.

| **As of March 31, 2016** | **AA** | **A** | **Total** |
|---|---|---|---|
| **Domestic U.S.** | | | |
| Interest-Bearing Deposits | $ — | $ 650 | $ 650 |
| Fed Funds Sold | 625 | 300 | 925 |
| **U.S. branches and agency offices of foreign commercial banks - Federal Funds sold:** | | | |
| Canada | — | 1,385 | 1,385 |
| Finland | 700 | — | 700 |
| Netherlands | — | 500 | 500 |
| Sweden | — | 100 | 100 |
| **Total unsecured credit exposure** | $ 1,325 | $ 2,935 | $ 4,260 |

All $4.260 billion of the unsecured credit exposure shown in the above table were overnight investments.

**(Dollars in millions except per share amounts unless otherwise indicated)**

*Managing Our Credit Risk Exposure Related to Derivative Agreements*

Refer to **Note 9 - Derivatives and Hedging Activities** to the financial statements for a discussion of how we manage our credit risk exposure related to derivative agreements.

The following table presents our derivative positions only where we have a net credit exposure to a counterparty. The rating used was the lowest rating among the three largest NRSROs. Non-cash collateral pledged consists of initial margin we posted through our FCMs, on behalf of the DCOs for cleared derivatives and is included in our derivative positions with credit exposure.

| | Net Derivatives Fair Value Before Collateral | Cash Collateral Pledged | Non-cash Collateral Pledged | Net Credit Exposure to Counterparties |
|---|---|---|---|---|
| **As of March 31, 2016** | | | | |
| **Non-member counterparties -** | | | | |
| Asset positions with credit exposure - | | | | |
| Bilateral derivatives - | | | | |
| A rated | $ 7 | $ (6) | $ — | $ 1 |
| Liability positions with credit exposure - | | | | |
| Cleared derivatives | (413) | 399 | 103 | 89 |
| **Non-member counterparties** | (406) | 393 | 103 | 90 |
| Member institutions | 1 | — | — | 1 |
| **Total** | $ (405) | $ 393 | $ 103 | $ 91 |
| | | | | |
| As of December 31, 2015 | | | | |
| **Non-member counterparties -** | | | | |
| Liability positions with credit exposure - | | | | |
| Bilateral derivatives - | | | | |
| AA rated | $ (14) | $ 14 | $ — | $ — [a] |
| A rated | (4) | 4 | — | — [a] |
| Cleared derivatives | (147) | 136 | 62 | 51 |
| **Non-member counterparties** | (165) | 154 | 62 | 51 |
| Member institutions | 1 | — | — | 1 |
| **Total** | $ (164) | $ 154 | $ 62 | $ 52 |

[a] Less than $1 million.

## Legislative and Regulatory Developments

Significant regulatory actions and developments for the period covered by this report are summarized below.

**Joint Proposed Rule on Incentive-Based Compensation Arrangements**

On April 26, 2016, the FHFA, jointly with five other federal regulators, issued the rule contemplated by Section 956 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), which requires implementation of regulations or guidelines to (1) prohibit incentive-based payment arrangements that these regulators determine encourage inappropriate risks by certain financial institutions by providing excessive compensation or that could lead to material financial loss; and (2) require those financial institutions to disclose information concerning incentive-based compensation arrangements to the appropriate federal regulator.

The proposed rule identifies three categories of institutions that would be covered by these regulations based on average total consolidated assets, applying less prescriptive incentive-based compensation program requirements to the smallest covered institutions (Level 3) and progressively more rigorous requirements to the larger covered institutions (Level 1). The proposed rule specifies that the Bank would fall into the middle category, Level 2. The proposed rule would supplement existing FHFA executive compensation rules.

The proposed rule would prohibit the Bank from establishing or maintaining incentive-based compensation arrangements that encourage inappropriate risks by “senior executive officers” and “significant risk-takers” (each as defined in the proposed rule, together “covered persons”) that could lead to a material financial loss.

If adopted in its current form, the proposed rule would, among other things, impose requirements related to our incentive-based compensation arrangements for covered persons, related to:

- mandatory deferrals of 50 percent and 40 percent of annual incentive based compensation payments for senior executive officers and significant risk takers, respectively, over no less than 3 years;
- risk of downward adjustment and forfeiture of awards;
- clawbacks of vested compensation; and
- limits on the maximum incentive-based compensation opportunity.

Comments are due on the proposed rule by July 22, 2016. The Bank is currently assessing the effect of the proposed rule.

**FHFA Final Rule on FHLB Membership**

On January 20, 2016, the FHFA issued a rule effective February 19, 2016, that, among other things:

- makes captive insurance companies ineligible for FHLB membership; and
- defines the "principal place of business" of an institution eligible for FHLB membership to be the state in which it maintains its home office and from which the institution conducts business operations.

The rule defines a captive insurance company as a company that is authorized under state law to conduct insurance business but whose primary business is the underwriting of insurance for affiliated persons or entities.

Captive insurance company members that were admitted as FHLB members prior to September 12, 2014, (the date the FHFA proposed this rule) will have their memberships terminated by February 19, 2021. Captive insurance company members that were admitted as FHLB members after September 12, 2014, will have their memberships terminated by February 19, 2017. There are restrictions on the level and maturity of advances that FHLB can make to these members during the sunset periods.

In the final rule, the FHFA declined to adopt certain proposed provisions that would have required FHLB members to hold specified levels of home mortgage loan assets on an ongoing basis.

As of March 31, 2016, our captive insurance company members had $13.0 billion in advances outstanding at par, which was 34% of our total advances outstanding, and held $294 million in capital stock, which was 14% of our total capital stock outstanding. We have reclassified this capital stock as mandatorily redeemable capital stock, as further discussed in **Note 11 - Capital and Mandatorily Redeemable Capital Stock (MRCS)** to the financial statements. All advances made to our captive insurance company members prior to the final rule taking effect, which range in maturity up to ten years with a current weighted remaining tenor of 4.5 years, may remain outstanding until such advances mature. However, once our three captive insurance company members have their membership terminated and their advances mature, our advance and capital stock levels would decrease. Unless we experience an increased demand for our advance products from our current or future members, this will result in a material decrease in our outstanding advance levels and our results of operations may be adversely affected. Further, we could experience lower demand for advances and other products and services, including letter of credit activity. In addition, our core mission asset ratio may be negatively impacted. The magnitude of the impact will depend, in part, on our size and profitability at the time of membership termination or maturity of related advances.

**(Dollars in millions except per share amounts unless otherwise indicated)**

## Item 3. Quantitative and Qualitative Disclosures About Market Risk.

### Measurement of Market Risk Exposure

To measure our exposure, we discount the cash flows generated from modeling the terms and conditions of all interest rate-sensitive securities using current interest rates to determine their fair values or spreads to the swap curve for securities where third party prices are used. This includes considering explicit and embedded options using a lattice model or Monte Carlo simulation. We estimate yield curve, option, and basis risk exposures by calculating the fair value change in relation to various parallel changes in interest rates, implied volatility, prepayment speeds, spreads to the swap curve and mortgage rates.

The table below summarizes our sensitivity to various interest rate risk exposures in terms of changes in market value.

| | | Option Risk | | Basis Risk | |
|---|---|---|---|---|---|
| | Yield Curve Risk | Implied Volatility | Prepayment Speeds | Spread to Swap Curve | Mortgage Spread |
| **As of March 31, 2016** | | | | | |
| Advances | **$ (4)** | **$ —** | **$ —** | **$ (10)** | **$ —** |
| MPF Loans | **(1)** | **—** | **(3)** | **(2)** | **1** |
| Mortgage Backed Securities | **(4)** | **(1)** | **(1)** | **(5)** | **—** |
| Other interest earning assets | **(1)** | **—** | **—** | **(3)** | **—** |
| Interest-bearing liabilities | **4** | **2** | **—** | **4** | **—** |
| Derivatives | **5** | **(1)** | **—** | **—** | **—** |
| Total | **$ (1)** | **$ —** | **$ (4)** | **n/m** | **$ 1** |
| | | | | | |
| As of December 31, 2015 | | | | | |
| Advances | $ (3) | $ — | $ — | $ (10) | $ — |
| MPF Loans | (1) | (2) | (2) | (2) | 1 |
| Mortgage Backed Securities | (4) | (1) | (1) | (5) | — |
| Other interest earning assets | (1) | — | — | (3) | — |
| Interest-bearing liabilities | 6 | 5 | — | 6 | — |
| Derivatives | 3 | (3) | — | — | — |
| Total | $ — | $ (1) | $ (3) | n/m | $ 1 |

n/m Spread movements to the swap curve within each category are independent of the other categories and therefore a total is not meaningful.

*Yield curve risk* – Change in market value for a one basis point parallel increase in the swap curve.
*Option risk (implied volatility)* – Change in market value for a one percent parallel increase in the swaption volatility.
*Option risk (prepayment speeds)* – Change in market value for a one percent increase in prepayment speeds.
*Basis risk (spread to swap curve)* – Change in market value for a one basis point parallel increase in the spread to the swap curve.
*Basis risk (mortgage spread)* – Change in market value for a one basis point increase in mortgage rates.

As of March 31, 2016, our sensitivity to changes in implied volatility was nil. At December 31, 2015, our sensitivity to changes in implied volatility was $(1) million. These sensitivities are limited in that they do not incorporate other risks, including but not limited to, non-parallel changes in yield curves, prepayment speeds, and basis risk related to differences between the swap and the other curves. Option positions embedded in our mortgage assets and callable debt impact our yield curve risk profile, such that swap curve changes significantly greater than one basis point cannot be linearly interpolated from the table above.

(Dollars in millions except per share amounts unless otherwise indicated)

Duration of equity is another measure to express interest rate sensitivity. We report the results of our duration of equity calculations to the FHFA each quarter. We measure duration of equity in a base case using the actual yield curve as of a specified date and then shock it with an instantaneous shift of the entire curve. The following table presents the duration of equity reported by us to the FHFA in accordance with the FHFA's guidance, which prescribes that down and up interest-rate shocks equal 200 basis points. The results are shown in years of duration equity.

| **March 31, 2016** | | | December 31, 2015 | | |
|---|---|---|---|---|---|
| **Down 200 bps** | **Base** | **Up 200 bps** | Down 200 bps | Base | Up 200 bps |
| **2.6** | **1.0** | **0.9** | 2.8 | 0.6 | 0.7 |

Duration gap is another measure of interest rate sensitivity. Duration gap is calculated by dividing the dollar duration of equity by the fair value of assets. A positive duration gap indicates an exposure to rising interest rates. As of March 31, 2016, our duration gap was 0.9 months, compared to 0.5 months as of December 31, 2015.

As of March 31, 2016, on a U.S. GAAP basis, our fair value surplus (relative to book value) was $339 million, and our market value of equity to book value of equity ratio was 107%. At December 31, 2015, our fair value surplus was $351 million and our market value of equity to book value of equity ratio was 108%. The reduction in market value to book value was partly driven by the increase in our capital and the gradual pay down of assets at a fair value premium to book value that are replaced by assets at par. Our market to book value of total capital for regulatory risk-based capital purposes differs from this GAAP calculation, as discussed in **Note 11 - Capital and Mandatorily Redeemable Capital Stock (MRCS)** to the financial statements.

Our Asset/Liability Management Committee provides oversight of market risk management practices and policies. This includes routine reporting to senior management and the Board of Directors, as well as maintaining the Income and Market Value Risk Policy, which defines our interest rate risk limits. The table below reflects the change in market risk limits under the Income and Market Value Risk Policy.

| | **March 31, 2016** | | December 31, 2015 | |
|---|---|---|---|---|
| **Scenario as of** | **Change in Market Value of Equity** | **Loss Limit** | Change in Market Value of Equity | Loss Limit |
| -200 bp | **$ 45.8** | **$ (185.0)** | $ 123.0 | $ (370.0) |
| -100 bp | **99.7** | **(77.5)** | 65.2 | (155.0) |
| -50 bp | **47.0** | **(30.0)** | 21.8 | (60.0) |
| -25 bp | **16.4** | **(15.0)** | 7.5 | (30.0) |
| +25 bp | **(11.8)** | **(30.0)** | (6.4) | (30.0) |
| +50 bp | **(20.8)** | **(60.0)** | (13.9) | (60.0) |
| +100 bp | **(39.0)** | **(155.0)** | (31.3) | (155.0) |
| +200 bp | **(81.0)** | **(370.0)** | (62.8) | (370.0) |

## Item 4. Controls and Procedures.

### Disclosure Controls and Procedures

Under the supervision and with the participation of management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended, as of the end of the period covered by this report (the Evaluation Date). Based on this evaluation, the principal executive officer and principal financial officer concluded as of the Evaluation Date that the disclosure controls and procedures were effective such that information relating to us that is required to be disclosed in reports filed with the SEC (i) is recorded, processed, summarized, and reported within the time periods specified in SEC rules and forms, and (ii) is accumulated and communicated to management, including our principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

### Changes in Internal Control Over Financial Reporting

For the current year quarter presented in this Form 10-Q, there were no changes in our internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

### Consolidated Obligations

Our disclosure controls and procedures include controls and procedures for accumulating and communicating information relating to our joint and several liability for the consolidated obligations of other FHLBs. For further information, see **Item 9A. Controls and Procedures** on page 82 of our 2015 Form 10-K.

## PART II - OTHER INFORMATION

### Item 1. Legal Proceedings.

On October 15, 2010, the Bank instituted litigation relating to 64 private-label MBS bonds purchased by the Bank in an aggregate original principal amount of $4.29 billion. Of the three cases that were filed by the Bank, only the action filed in the Circuit Court of Cook County, Illinois remains active. As of April 30, 2016, this litigation covers four private-label MBS bonds in the aggregate original principal amount of $77.5 million.

In this action, the Bank asserts claims for untrue or misleading statements in the sale of securities, signing or circulating securities documents that contained material misrepresentations, and negligent misrepresentation. The Bank seeks the remedies of rescission, recovery of damages, and recovery of reasonable attorneys' fees and costs of suit. As of April 30, 2016, Morgan Stanley & Co., Incorporated, and certain of its affiliates, remain as the sole defendants in the Illinois action.

The Bank may also be subject to various other legal proceedings arising in the normal course of business. After consultation with legal counsel, management is not aware of any other proceedings that might have a material effect on the Bank's financial condition or results of operations.

### Item 1A. Risk Factors.

In addition to the information presented in this report, readers should carefully consider the factors set forth in the **Risk Factors** section on page 19 in our 2015 Form 10-K, which could materially affect our business, financial condition, or future results. These risks are not the only risks facing us. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial may also severely affect us.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.**

Not applicable.

**Item 3. Defaults Upon Senior Securities.**

None.

**Item 4. Mine Safety Disclosures.**

Not applicable.

**Item 5. Other Information.**

None.

**Item 6. Exhibits.**

| | |
|---|---|
| 3.1 | Federal Home Loan Bank of Chicago Bylaws[1] |
| 31.1 | Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 by the Principal Executive Officer |
| 31.2 | Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 by the Principal Financial Officer |
| 32.1 | Certification pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 by the Principal Executive Officer |
| 32.2 | Certification pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 by the Principal Financial Officer |
| 101.INS | XBRL Instance Document |
| 101.SCH | XBRL Taxonomy Extension Schema Document |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase Document |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase Document |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document |

[1] Filed with our 8-K Current Report on February 1, 2016

**Glossary of Terms**

**Advances:** Secured loans to members.

**ABS:** Asset-backed-securities.

**AFS:** Available-for-sale securities.

**AOCI:** Accumulated Other Comprehensive Income.

**Capital Plan:** The Second Amended and Restated Capital Plan of the Federal Home Loan Bank of Chicago, effective as of October 1, 2015.

**CBSA:** Core Based Statistical Areas (CBSAs), which are based upon an assessment of the individual housing markets. CBSA refers collectively to metropolitan and micropolitan statistical areas as defined by the United States Office of Management and Budget; as currently defined, a CBSA must contain at least one urban area with a population of 10,000 or more people.

**CDFI:** Community development financial institution.

**CFTC:** Commodity Futures Trading Commission.

**Consolidated Obligations (CO):** FHLB debt instruments (bonds and discount notes) which are the joint and several liability of all FHLBs; issued by the Office of Finance.

**Consolidated obligation bonds:** Consolidated obligations that make periodic interest payments with a term generally over one year, although we have issued for terms of less than one year.

**DCO:** Derivatives Clearing Organization. A clearinghouse, clearing association, clearing corporation, or similar entity that enables each party to an agreement, contract, or transaction to substitute, through novation or otherwise, the credit of the DCO for the credit of the parties; arranges or provides, on a multilateral basis, for the settlement or netting of obligations; or otherwise provides clearing services or arrangements that mutualize or transfer credit risk among participants.

**Discount notes:** Consolidated obligations with a term of one year or less, which sell at less than their face amount and are redeemed at par value when they mature.

**Dodd-Frank Act:** Dodd-Frank Wall Street Reform and Consumer Protection Act, enacted July 21, 2010.

**Excess capital stock:** Capital stock held by members in excess of their minimum investment requirement.

**Fannie Mae:** Federal National Mortgage Association.

**FASB:** Financial Accounting Standards Board.

**FCM:** Futures Commission Merchant.

**FDIC:** Federal Deposit Insurance Corporation.

**FFELP:** Federal Family Education Loan Program.

**FHA:** Federal Housing Administration.

**FHFA:** Federal Housing Finance Agency - The Housing and Economic Recovery Act of 2008 enacted on July 30, 2008 created the Federal Housing Finance Agency which became the regulator of the FHLBs.

**FHLB Act:** The Federal Home Loan Bank Act of 1932, as amended.

**FHLBs:** The 11 Federal Home Loan Banks or subset thereof.

**FHLB System:** The 11 FHLBs and the Office of Finance.

**FHLB Chicago:** The Federal Home Loan Bank of Chicago.

FHLB Chicago

Federal Home Loan Bank of Chicago

**Freddie Mac:** Federal Home Loan Mortgage Corporation.

**GAAP:** Generally accepted accounting principles in the United States of America.

**Ginnie Mae:** Government National Mortgage Association.

**Ginnie Mae MBS:** Mortgage-backed securities guaranteed by Ginnie Mae.

**Government Loans:** Mortgage loans insured or guaranteed by the Federal Housing Administration (FHA), the Department of Housing and Urban Development (HUD), the Department of Veteran Affairs (VA) or Department of Agriculture Rural Housing Service (RHS).

**GSE:** Government sponsored enterprise.

**HFS:** Held for sale.

**Housing Act:** Housing and Economic Recovery Act of 2008, enacted July 30, 2008.

**HUD:** Department of Housing and Urban Development.

**HTM:** Held-to-maturity securities.

**LIBOR:** London Interbank Offered Rate.

**Master Commitment (MC):** Pool of MPF Loans purchased or funded by an MPF Bank.

**MBS:** Mortgage-backed securities.

**Moody's:** Moody's Investors Service.

**MPF®:** Mortgage Partnership Finance.

**MPF Banks:** FHLBs that participate in the MPF program.

**MPF Direct product:** The MPF Program product under which we acquire jumbo MPF Loans from PFIs and concurrently resell them to a third party investor.

**MPF Government MBS product**: The MPF Program product under which we aggregate Government Loans acquired from PFIs in order to issue securities guaranteed by the Ginnie Mae that are backed by such Government Loans.

**MPF Loans:** Conforming conventional and government fixed-rate mortgage loans secured by one-to-four family residential properties with maturities from five to 30 years or participations in such mortgage loans that are acquired under the MPF Program.

**MPF Program:** A secondary mortgage market structure that provides liquidity to FHLB members that are PFIs through the purchase or funding by an FHLB of MPF Loans.

**MPF Xtra® product:** The MPF Program product under which we acquire MPF Loans from PFIs and concurrently resell them to Fannie Mae.

**MRCS:** mandatorily redeemable capital stock.

**Nonaccrual MPF Loans:** Nonperforming mortgage loans in which the collection of principal and interest is determined to be doubtful or when interest or principal is past due for 90 days or more, except when the MPF Loan is well secured and in the process of collection.

**NRSRO:** Nationally Recognized Statistical Rating Organization.

**Office of Finance:** A joint office of the FHLBs established to facilitate issuing and servicing of consolidated obligations.

**OIS:** Fed Funds Effective Swap Rate (or Overnight Index Swap Rate).

**OTTI:** Other-than-temporary impairment.

**OTTI Committee:** An FHLB System OTTI Committee formed by the FHLBs to achieve consistency among the FHLBs in their analyses of the OTTI of private-label MBS.

**PFI:** Participating Financial Institution. A PFI is a member (or eligible housing associate) of an MPF Bank that has applied to and been accepted to do business with its MPF Bank under the MPF Program.

**PMI:** Primary Mortgage Insurance.

**PwC:** PricewaterhouseCoopers LLP.

**RCAP:** Reduced Capitalization Advance Program.

**Recorded Investment:** Recorded investment in a loan is its amortized cost basis plus related accrued interest receivable, if any. Recorded investment is not net of an allowance for credit losses but is net of any direct charge-off on a loan. Amortized cost basis is defined as either the amount funded or the cost to purchase MPF Loans. Specifically, the amortized cost basis includes the initial fair value amount of the delivery commitment as of the purchase or settlement date, agent fees (i.e., market risk premiums or discounts paid to or received from PFIs), if any, subsequently adjusted, if applicable, for accretion, amortization, collection of cash, charge-offs, and cumulative basis adjustments related to fair value hedges.

**Regulatory capital:** Regulatory capital stock plus retained earnings.

**Regulatory capital stock:** The sum of the paid-in value of capital stock and mandatorily redeemable capital stock.

**REO:** Real estate owned.

**RHS:** Department of Agriculture Rural Housing Service.

**SEC:** Securities and Exchange Commission.

**System or FHLB System:** The Federal Home Loan Bank System consisting of the 11 Federal Home Loan Banks and the Office of Finance.

**TBA:** A forward contract on a mortgage-backed security (MBS), typically issued by a U.S. government sponsored entity, whereby a seller agrees to deliver an MBS for an agreed upon price on an agreed upon date.

**TDR:** Troubled Debt Restructuring

**UPB:** Unpaid Principal Balance.

**U.S.:** United States

**VA:** Department of Veteran's Affairs.

FHLB Chicago
Federal Home Loan Bank of Chicago

**Signatures**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

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| | **FEDERAL HOME LOAN BANK OF CHICAGO** |
| | /s/ Matthew R. Feldman |
| | By: Matthew R. Feldman |
| | Title: President and Chief Executive Officer |
| Date: May 5, 2016 | (Principal Executive Officer) |
| | /s/ Roger D. Lundstrom |
| | By: Roger D. Lundstrom |
| | Title: Executive Vice President and Chief Financial Officer |
| Date: May 5, 2016 | (Principal Financial Officer and Principal Accounting Officer) |