Federal Housing Finance Board

March 30, 1993

MEMORANDUM

TO: Philip L. Conover
Managing Director

THROUGH: Beth L. Climo BLC
General Counsel

FROM: James H. Gray Jr. JHG
Associate General Counsel

SUBJECT: Response to FHLB-New York and Krieg, DeVault Legal Analyses of the Applicability of the Non-QTL Provisions to Insurance Companies

You have referred to us for review and comment a January 14, 1993 legal analysis prepared by the Federal Home Loan Bank (FHLBank) of New York and the FHLBank of Des Moines (collectively referred to as FHLB-New York), as well as a March 16, 1993 opinion letter prepared by the law firm of Krieg, DeVault, Alexander & Capehart (Krieg, DeVault) representing seven FHLBanks.l Both analyses suggest that the non-qualified thrift lender (non-QTL) provisions in section 10(e) of the Federal Home Loan Bank Act (Bank .Act), 12 U.S.C. § 1430(e) (Supp. II 1990), need not apply to insurance companies.2

I. Backqround

The proper application of the non-QTL requirements has been given careful consideration by the FHLBanks, the Federal Housing Finance Board (Finance Board) and others since the inception of this agency in August 1989. Attached is a chronology reflecting

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1. Krieg, DeVault reiterates a number of the arguments made by the FHLB-New York. References to arguments made by the FHLB-New York in many instances also apply to Krieg, DeVault. In general, the references to arguments by' Krieg, DeVault concern arguments not made by the FHLB-New York.

2. Both the FHLB-New York and Krieg, DeVault focus their arguments on the application of the non-QTL provisions to insurance company members. The FHLB-New York notes that the same arguments apply to all other non-savings association members (i.e., commercial banks and credit unions). While not specifically so noting, the Krieg, DeVault analysis also would be equally applicable to all non-savings association members.

the extensive analysis and discussion inspired by the issue of whether the non-QTL provisions in subsection 10(e) of the Bank Act apply to all members or only to savings association members. See Attachment. After considering the recent analyses, which encompass arguments considered previously, and reviewing the legislative history and prior analyses, for the reasons set forth below, the Office of Legal and External Affairs - Legal Division concludes that, contrary to the FHLB-New York analysis and the Krieg, DeVault opinion, the non-QTL provisions of the Bank Act apply to all FHLBank members, including insurance companies.

11. Principles of Statutory Construction Support Applying the Non-QTL Requirements to All Members

A. The Plain Meaning of the Phrase "Member that is not a [QTL]" Applies to All Members.

The crux of the entire debate is whether the word 'member' as used in the phrase "member that is not a [QTL]," means all members, or whether it can be interpreted to mean only 'savings association members.' There are arguably two plausible interpretations of this statutory language. However, the Finance Board is obliged to fulfill Congress' intent if that can be discerned from considering the statute as a whole, even though there may be ambiguity in a specific provision. See Massachusetts v. Morash, 490 U.S. 107, 115 (1989) quoting Pilot Life Ins. Co. v. Dedeaux, 481 U.S. 41, 51 (1987).

The FHLB-New York suggests that "member that is not a [QTL]" may be interpreted to mean only "savings association members that are not QTLs" because only savings associations come within the definition of QTL in the Home Owners' Loan Act (HOLA) that is cross referenced in paragraph 10(e)(5) of the Bank Act.3 As discussed further below, under the FHLB-New York interpretation, the non-QTL requirements of the Bank Act currently would apply only to five savings association members.4 It is practically inconceivable that Congress created this elaborate set of non-QTL

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3. HOLA definition of QTL, 12 U.S.C. § 1467a(m); Bank Act cross reference to HOLA QTL definition, 12 U.S.C. § 1430(e)(5). See FHLB-New York Analysis (Jan. 14, 1993) p. 3.

4. Based on a telephone survey of FHLBanks between March 23 and 29, 1993, by Thomas D. Sheehan, Assistant Director, District Banks Directorate, and Edwin Avila, District Banks Directorate. Of the five non-QTL savings association members, only one had outstanding advances, which total only $6.36 million. The survey also identified four additional savings associations which have failed the QTL test since the enactment of the Financial Institutions Reform, Recovery and Enforcement Act of 1989 (FIRREA), Pub. L. 101-73, 103 Stat. 183. These four institutions are no longer FHLBank System members.

requirements to address only five members of the FHLBank System, which currently numbers 3,723 members.5

The better interpretation of the phrase 'member that is not a [QTL]" is that the word "member" in that phrase means all members, not just a limited class of members, since any member can be a 'member that is not a qualified thrift lender.' This was the interpretation used in the advances proposed rule, see 57 Fed. Reg. 45338, 45349 (1992) (to be codified at 12 CFR § 935.1) (proposed Oct. 1, 1992) (hereinafter 'proposed advances rule"). The argument for this interpretation is that the Bank Act QTL requirements were meant to distinguish between members based on their commitment to housing, not based on their charter type. Savings associations are by no means the only 'members that are not qualified thrift lenders.' Savings associations, commercial banks, and insurance companies -- indeed all members that fail to have a substantial portion of their portfolio invested in mortgage assets -- are 'members that are not qualified thrift lenders." If Congress had intended that the non-QTL provisions apply only to savings associations, it could have said, "A savings association member that is not a [QTL]," but Congress did not say this.

Further, these are the only two possible plain meaning interpretations of the phrase 'member that is not a [QTL]." Any arguable ambiguity surrounding this language is between applying the non-QTL provisions to all members or only to savings associations. There is no plausible reading of 'member that is not a (QTL]" that would support an interpretation that the phrase refers to all members except for insurance companies. Accordingly, even if.we find subsection 10(e) to be ambiguous, insurance companies alone cannot be carved out. The agency is permitted to resolve a statutory language ambiguity only with "a permissible construction of the statute." See Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc., 467 U.S. 837, 843 (1984).

Thus, our analysis examines the two plausible interpretations -- i.e., application either to all members or only to savings association members -- to determine whether the language of subsection 10(e) and extrinsic sources demonstrate a congressional imperative to follow one interpretation, or whether the language is so ambiguous that the Finance Board has the discretion to resolve the ambiguity by choosing between the two plausible alternatives. An argument can be made for the FHLB-New York position that "member" means only "savings association members." However, considering the statutory scheme and the legislative history, the compelling plain meaning is that 'member

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5. At the time FIRREA was enacted, on August 9, 1989, there were 3,217 FHLBank System members. As of February 1993, there were 3,723 FHLBank System members. February 1993 membership report, District Banks Directorate.

that is not a [QTL]" refers to all members. The law concerning Federal agency discretion to interpret statutes is discussed in more detail in part IV of this memorandum, infra.

B. Textual Analysis of Each Non-QTL Requirement Supports Applying These Requirements to All Members.

As noted in the FHLB-New York's analysis, it is an elementary rule of construction that effect must be given, if possible, to every word, clause and sentence of a statute. See FHLB-New York Analysis (Jan. 14, 1993) pp. 5-6, note 21, citing Sutherland Statutory Construction ("Sutherland") § 46.06 (Sands 4th ed. 1984). This same rule of statutory construction also states that a statute should be construed to give effect to all of its provisions, so that no part will be inoperative or superfluous, see id. But, the FHLB-New York interpretation would in fact render the non-QTL provisions virtually inoperative. The FHLB-New York interpretation would apply these very controversial FHLBank lending provisions only to savings associations that fail the HOLA QTL test, a universe that currently numbers only five institutions.

In fact, the possible application of these Bank Act non-QTL provisions is even narrower, and significantly so, than would be suggested merely by the very small universe of institutions (i.e., five) subject to the provisions under the FHLB-New York interpretation. Savings associations that fail the separate HOLA QTL requirements already are specifically barred by HOLA from receiving new FHLBank advances? Thus, if the Bank Act's non-QTL provisions apply only to savings associations that fail the HOLA QTL test, there would be almost no reason for the Bank Act provisions, since non-QTL savings associations already are barred by HOLA from receiving new advances.

The FHLB-New York and Krieg, DeVault have identified four very narrow ways (discussed below) in which the non-QTL provisions would arguably operate if applied only to such savings associations -- i.e., the five in existence that fail the QTL test. Analysis of each non-QTL requirement and the interpretation put forth by FHLB-New York and Krieg, DeVault further supports the conclusion that applying these requirements only to five non-QTL savings associations renders them ineffective. We will address the subsection 10(e) non-QTL requirements sequentially.

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6. See 12 U.S.C. § 1467a(m)(3)(B)(i)(III). In addition, savings associations that remain out of compliance with the HOLA QTL requirements for three years are required by HOLA to repay outstanding advances. See id. at (m)(3)(B)(ii)(II).

1. The Advances-To-Stock Purchase Requirement and the "Housing Finance" Purpose Requirement

The first non-QTL requirement, paragraph 10(e)(l), provides:

> (1) A member that is not a qualified thrift lender may only receive an advance if it holds stock in its [FHLBank] at the time it receives that advance in an amount equal to at least--
> (A) 5 percent of that member's total advances, divided by
> (B) such member's [ATIP].' Such members that are not qualified thrift lenders may only apply for advances under this section for the purpose of obtaining funds for housing finance.

12 U.S.C. § 1430(e)(l) (Supp. II 1990) (emphasis added).

a. Advances-to-stock purchase requirement. The FHLB-New York interpretation would have this stock purchase requirement apply only to savings associations. However, this stock requirement has no effect on the vast majority of savings associations, i.e., the approximately 1,889 which currently meet the HOLA QTL test. Instead, it would apply only to the five that are not QTLs, and only in limited instances since those five savings associations already are forbidden by HOLA from taking down new advances.

First, the FHLB-New York suggests that one of the purposes of the special advances-to-stock purchase non-QTL requirement is to increase the stock purchase requirement for non-QTL savings association members who borrow pursuant to an as yet unused special liquidity advances provision.8 If the purpose of the advances-to-stock purchase requirement was to increase stock holdings for members who borrow pursuant to this never yet used provision, then this non-QTL stock requirement would have had no effect to date.

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7. "ATIP" refers to the "Actual Thrift Investment Percentage,' a concept cross referenced from HOLA to measure the percentage of a mortgage lender's loan portfolio that consists of mortgage assets. See 12 U.S.C. § 1467a(m)(4)(A) (Supp. II 1990). The net effect of the ratio, five percent of advances over the ATIP, is that the lower the percentage of the non-QTL member's portfolio that is invested in home mortgage assets, the more FHLBank stock the non-QTL member must hold in order to borrow.

8. FHLB-New York Analysis (Jan. 14, 1993) p. 6. This provision in section 10(h) of the Bank Act, 12 U.S.C. § 1430(h), allows the Office of Thrift Supervision (OTS) to make a special request for a liquidity advance to a troubled, but solvent, FHLBank member savings association. To our knowledge, no special liquidity advances have been made to date pursuant to this authority.

Second, Krieg, DeVault suggests that, even though HOLA already prohibits advances to non-QTL savings associations, that prohibition applies only to new advances and, thus, the advances-to-stock purchase requirement and the other non-QTL provisions would apply to renewals of advances outstanding to non-QTL savings associations. The making or renewal of advances to a non-QTL savings association is an unusual enough circumstance that OTS staff has informed Finance Board staff that it has not yet taken a formal position on the issue of whether the HOLA prohibition on advances to non-QTLs applies to only new advances, or to renewals as well. Even if OTS took the position suggested by Krieg, DeVault, the number of institutions affected (i.e., five) is so small that the non-QTL provisions of the Bank Act would still have miniscule applicability.

Third, the FHLB-New York suggests that this advances-to-stock purchase requirement would increase the stock requirement on already outstanding advances when a savings association becomes a non-QTL. Again, if the FHLB-New York interpretation had been followed to date, since only five savings associations failed the QTL test, this provision would have had a virtually indiscernible effect.

Fourth, the FHLB-New York cites as a putative purpose for these provisions when applied to only non-QTL savings associations, restricting advances to non-QTL savings associations in Puerto Rico and the Virgin Islands from August 1990 to June 1991, because the HOLA QTL requirements did not apply in those jurisdictions for that ten-month period. To suggest that Congress created the elaborate statutory scheme in subsection 10(e) for a purpose this narrow stretches putative legislative intent beyond credulity.

In contrast, if the phrase "member that is not a (QTL)" is interpreted to apply to all members, the advances-to-stock purchase requirement has substantial applicability, effect and purpose. Legislative history suggests that the advances-to-stock purchase requirement is designed to impose higher stock requirements on members -- such as commercial banks, credit unions and insurance companies -- that have fewer housing related assets than traditional savings association members.[9] Thus, applying the advances-to-stock purchase requirements to all members leads to the rational result that, for purposes of this stock purchase requirement, members' required FHLBank stockholdings as a percentage of advances will decline as their housing-related assets increase.

b. Advances only for housing finance. The other requirement in paragraph 10(e)(l) states that non-QTL members may receive

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9. See 135 Cong. Rec. S. 10206 (daily ed. Aug. 4, 1989) (Statement of Sen. Riegle) (quoted infra in part 1II.A.)

advances only for the purpose of "housing finance." This provision also would have virtually no effect if it applies only to savings associations. First, as stated before, there are now only five non-QTL savings associations and those five institutions are generally barred by HOLA from receiving new advances. Second, the requirement that advances be only for "housing finance" purposes directly contradicts the principal rationale suggested by the FHLB-New York in support of applying these provisions only to savings associations, namely, providing special liquidity advances for troubled non-QTL savings associations.[10]

On the other hand, if this requirement that permits advances to non-QTLs only for housing finance purposes is applied to all members as in the proposed advances rule, this provision would require that commercial banks, credit unions and insurance companies that gain access to FHLBank borrowing use that access to enhance their mortgage loan portfolios. This interpretation is consistent with legislative history indicating that commercial banks and credit unions can have access to FHLBank advances under certain conditions.[11]

2. Thirty Percent Cap for Advances to Non-QTL Members

Paragraph 10(e)(2) of the Bank Act, recently amended by the Housing and Community Development Act of 1992 (Housing Act of 1992), Pub. L. 102-550, 106 Stat. 3672, 4009 (1992) provides:

> (2) ... The aggregate amount of the advances by the [FHLBank] System to members that are not qualified thrift lenders shall not exceed 30 percent of the total advances of the [FHLBank] System.[12]

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10. Liquidity advances which assist a housing finance lender indirectly support housing finance. However, we generally interpret "obtaining funds for housing finance" to refer to advances that fund mortgage lending, whereas liquidity advances generally refer to advances that assist a member in meeting its cash requirements. See generally the definition of "residential housing finance" in the proposed advances rule, 57 Fed. Reg. 45338, 45349 (1992) (to be codified at 12 CFR § 935.1) (proposed Oct. 1, 1992).

11. See supra n.9.

12. 12 U.S.C. § 1430(e)(2) as amended by the Housing Act of 1992 (emphasis added). Prior to the Housing Act of 1992, the second sentence of 12 U.S.C. § 1430(e)(2) limited the aggregate amount of each FHLBank's advances to non-QTL members, to 30% of that FHLBank's aggregate advances. The Housing Act of 1992 changed the 30% cap from an individual FHLBank limit to a System limit because the non-QTL provisions were thought to be broadly applicable and, thus, posed a binding constraint.

Perhaps the non-QTL requirement that illustrates most vividly that the non-QTL provisions were intended to apply more broadly than to just non-QTL savings associations is the thirty percent lending cap. To date, that thirty percent cap has been interpreted to limit advances to commercial banks, credit unions and insurance companies (i.e., non-QTL members) to thirty percent of total outstanding advances. Under the interpretation put forward by the FHLB-New York, the thirty percent cap would have no purpose or effect. If applied only to non-QTL savings associations, under no circumstances would the thirty percent cap ever pose a binding constraint.[13] Recall that the few non-QTL savings associations that exist are barred by HOLA from receiving new advances.

In evaluating whether one or both of the interpretations of the non-QTL provisions could plausibly reflect legislative intent, it seems unlikely that Congress intended to establish a borrowing cap that has no possible effect. Conversely, the thirty percent cap could have an effect if applied to all members. In fact, the thirty percent cap applied to all members imposed such a binding constraint that Congress relaxed the limit in the Housing Act of 1992. The limit of thirty percent of each FHLBank's advances was relaxed to thirty percent of the FHLBank System's aggregate advances. This subsequent legislative action is almost irrefutable evidence that Congress intended the thirty percent cap to be a constraint on lending to all non-QTL members, including commercial banks, credit unions and insurance companies.[14]

3. Minimum Stock Purchase Requirement

Paragraph 10(e)(3) of the Bank Act states:

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13. The fact that the 30% cap on non-QTL lending would have absolutely no purpose or effect under the FHLB-New York interpretation is vividly illustrated by the numbers. Under the interpretation urged by the FHLB-New York, the numerator of the 30% cap equation would consist of only $6.6 million, the aggregate amount of advances to the five non-QTL savings associations. The denominator would consist of the aggregate amount of advances outstanding to all members, $80.7 billion as of February 1993. Under the FHLB-New York interpretation, this would result in less than .0l% (or .000l) of advances outstanding to non-QTL members. By contrast, total outstanding advances to all non-QTL members were $6.3 billion or 7.8% of total advances as of February 1993.

14. The report of the House Banking Committee, which was the Committee that authored the provision relaxing the 30% cap, explicitly said that the 30% cap applies to commercial bank members. See H.R. Rep. No. 206, 102d Cong., 1st Sess. at 74-75 (1991). This legislative history is addressed in part 1II.B. infra.

> (3) Each member of a [FHLBank] shall, at a minimum, purchase and maintain stock in its [FHLBank] in the amount that would be required under section 1426(b) of this title if at least thirty percent of such member's assets were home mortgage loans.

12 U.S.C. § 1430(e)(3).

Even the FHLB-New York agrees that this paragraph applies to all members. This paragraph was enacted concurrently with the other FIRREA non-QTL requirements and in the same subsection of the Bank Act. Its effect is to require members not subject to the HOLA QTL, such as commercial banks, credit unions and insurance companies, to hold the amount of FHLBank stock they would be required to hold if at least thirty percent of their assets were home mortgage loans. This paragraph is clearly designed to require all FHLBank members not subject to the HOLA QTL requirements to either hold more housing assets or more FHLBank stock. This universally acknowledged intent and operation of this paragraph is consistent with what seems to be the intent behind the other subsection 10(e) provisions, i.e., to impose additional prerequisites to FHLBank borrowing on members with a lower percentage of housing finance assets, such as commercial banks, credit unions and insurance companies. Such intent is fulfilled only if the other non-QTL requirements are interpreted to apply to all members.

4. Exceptions to the Non-QTL Requirements

Certain members are specifically exempted from the non-QTL requirements, as provided in paragraph 10(e)(4):

> (4) Paragraphs (1) and (2) of this subsection do not apply to--(A) a savings bank as defined in section 1813 of this title; or
> (B) a Federal savings association in existence as a Federal savings association on August 9, 1989 [FIRREA date of enactment]--
> (i) that was chartered as a cooperative bank prior to October 15, 1982; or
> (ii) that acquired its principal assets from an institution which was chartered prior to October 15, 1982, as a savings bank or cooperative bank under State law.

12 U.S.C. § 1430(e)(4).

In this paragraph of subsection 10(e), Congress specifically excluded savings banks and certain Federal savings associations from the subsection 10(e) provisions of the Bank Act that apply to "members that are not [QTLS]." State savings banks are not within the definition of "savings associations"in HOLA or the Federal

Deposit Insurance Act. See 12 U.S.C. §§ 1462(4) and 1813(b).15 Thus, if the subsection 10(e) non-QTL provisions only apply to savings associations, there would have been no need to exempt state savings banks from these provisions.16 The fact that savings banks are specifically exempt from the Bank Act non-QTL requirements provides further evidence that the Bank Act non-QTL requirements are intended to apply more broadly than just to savings associations. If those provisions apply more broadly then just to savings associations, as stated previously, the only other way to interpret them is as applicable to all members.

Further, there is a rule of statutory construction that all omissions should be understood as exclusions. See Sutherland § 47.23. Following this rule, Congress intended that the non-QTL provisions do apply to those members not covered by the exception. The exception specifically exempts savings banks from the non-QTL provisions, but it does not exempt commercial banks, credit unions or insurance companies. See 12 U.S.C. § 1430(e)(4). Accordingly, the Bank Act's non-QTL provisions should apply to commercial bank, credit union and insurance company members -- i.e., all members not otherwise specifically excluded by paragraph 10(e)(4).

5. Definition of terms used in Subsection 10(e)

Paragraph 10(e)(5) defines the following terms referred to in subsection 10(e):

> (5) As used in this subsection--
> (A) Savings association. The term "savings association" has the same meaning as in section 1467a(s)(l)(A) of this title.
> (B) Qualified thrift lender. The term "qualified thrift lender" has the same meaning as in section 1467a(m) of this title.
> (C) Actual thrift investment percentage. The term "actual thrift investment percentage" has the same meaning as in section 1467a(m) of this title.

12 U.S.C. § 1430(e)(5).

Paragraph 10(e)(5) creates some confusion by attempting to import into the Bank Act the HOLA's QTL concept. Each of these

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15. In fact, state savings banks are defined as 'banks," rather than as 'savings associations." See 12 U.S.C. § 1813(a) and (b).

16. The Federal savings associations that are also exempted from the Bank Act non-QTL provisions are within the HOLA definition of *'savings association," but they are specifically exempt under HOLA from the HOLA QTL requirements. Thus, exempting such Federal savings associations from the Bank Act non-QTL requirements merely provides parallel treatment under both laws and has no bearing one way or the other on the issue addressed in this memo.

terms is defined by cross referencing the definition of the same term as used in HOLA. Uncertainty arises because, unlike the Bank Act, HOLA applies only to savings associations. This paragraph lends some credence to the FHLB-New York argument, because the cross-referenced definitions from HOLA all refer only to savings associations -- which is to be expected in that HOLA applies only to savings associations.

In sum, paragraphs 10(e)(l)-(4) make a strong case for the proposition that the non-QTL requirements were intended to apply to all members. In our view, this is the only interpretation that gives tangible meaning to the substantive requirements in subsection 10(e). Taking into consideration the statutory language and considering the operation of each paragraph in subsection 10(e) individually, Congress could only have intended to apply the non-QTL requirements to all members.

III. Legislative History Supports Applying The Non-QTL Requirements to All Members

A. FIRREA Legislative History.

The legislative history of FIRREA supports the interpretation that the non-QTL requirements apply to all members. The most authoritative legislative history is a Conference Committee's report. See Sutherland § 48.08. In this instance, FIRREA's conference report is clear:

> In addition, this section imposes special eligibility requirements for advances to members that are not qualified thrift lenders. Such members may only receive advances for the purpose of obtaining funds for housing finance. In addition, a member that is not a qualified thrift lender may only receive an advance if it holds stock in its Bank at the time it receives the advance in an amount at least equal to five percent of that member's total advances, divided by that member's actual thrift investment percentage.
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> The Board by regulation must also establish a priority for advances to members who are qualified thrift lenders, and each Bank's advances to members that are not qualified thrift lenders cannot exceed 30% of the Bank's total advances.

Conf. Rep. No. 222, 10lst Cong., 1st Sess. 428 (emphasis added). [17]

17. The FHLB-New York cites other FIRREA conference report language discussing the 10% mortgage related asset requirement for membership, rather than the non-QTL provisions, for the proposition that legislative history provides a basis to apply the non-QTL provisions to all members other than insurance companies. See FHLB-New York Analysis (Jan. 14, 1993) p. 7. The legislative

Just as in the statute, the FIRREA conference report clearly states that the non-QTL provisions are applicable to "members that are not qualified thrift lenders." Nothing in the conference report suggests that the non-QTL provisions were intended to be limited to savings association members or to apply only in the very limited circumstances that have been posited by the FHLB-New York and Krieg, DeVault.

The Senate Floor Manager for FIRREA made a floor statement during the Senate's consideration of FIRREA which also supports the interpretation that the Bank Act's non-QTL requirements are intended to apply to all members:

> The Conference Report allows federally insured commercial banks and credit unions to become Federal Home Loan Bank members. This was done in recognition of the fact that some financial institutions that do not have thrift charters have nonetheless demonstrated substantial commitments to providing credit to purchasers of single family residences.
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> Originally, the Senate bill required a bank or credit union to pass the qualified thrift lender (QTL) test in order to gain access to advances from a Federal Home Loan Bank. This would have required a bank to fund 100 percent of its new single family mortgage lending without any help from a Federal [Home] Loan Bank. Once it reached the QTL plateau, it could use advances from the Federal Home Loan Bank for additional residential mortgage lending. The Conference Report allows insured banks and credit unions to have access to loans from the Federal Home Loan Banks under certain conditions. Generally, new members must have demonstrated a substantial commitment to residential mortgage lending. If a member is not a qualified thrift lender, it must hold additional stock in its Federal Home Loan Bank. All advances or extensions of credit by the Federal Home Loan Banks must be secured by eligible collateral.

135 Cong. Rec. S. 10206 (daily ed. Aug. 4, 1989) (Statement of Sen. Riegle, emphasis added).

The floor manager's statement addresses the change made during the FIRREA drafting process -- from a requirement that commercial banks and credit unions meet the QTL test, to the final law which allows commercial banks and credit unions to have access

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(Footnote 17 continued from previous page)
history cited by the FHLB-New York is to a different section of the Bank Act than the one containing the non-QTL provisions for advances -- in fact, it is legislative history to a section that by its very terms applies only to depository institutions.

to advances without meeting the QTL test, but instead requires that commercial banks and credit unions (and insurance companies) hold additional FHLBank stock. The floor manager's statement is directly contrary to the FHLB-New York and Krieg, DeVault interpretations and supports the interpretation in the proposed advances rule that the non-QTL provisions apply to all members.18

The above-quoted conference report language and the floor manager's statement are the *only two* items of FIRREA legislative history of which we are aware that specifically address the applicability of the Bank Act's non-QTL requirements. We are unable to discern anything from this legislative history that supports any conclusion other than that the Bank Act's non-QTL requirements are intended to apply to all FHLBank members.

B. Housing Act of 1992 Legislative History

The legislative history on the modification of the thirty percent cap in the Housing Act of 1992 -- from an individual FHLBank cap to a System-wide cap -- seems to be dispositive of the non-QTL issue. The House Banking Committee's report, which included the modification of the thirty percent cap, provided in pertinent part:

> H.R. 2900 amends Section 10(e)(2) of the Federal Home Loan Bank Act to change the 30% cap on advances to nonqualified thrift lenders from a district-by-district test to a System-wide standard. Under current law, a Bank may not make advances to non-qualified thrift lender members in excess of thirty percent of the Bank's total outstanding advances.
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> Because of increased commercial bank membership and contraction in the thrift industry, some [of] the Banks may be close to the point where they will have to deny advances to commercial bank members. This would have the undesired effect of eliminating their access to advances, the principal reason most commercial bank members are willing to hold the Bank stock. By lifting this limit, it is the Committee's intent to encourage commercial banks to become more active in home mortgage lending. . . .

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18. The FHLB-New York relies on explanatory material in the legislative history on the definition of QTL as used in HOLA and some rejected FIRREA language. Even though the QTL definition in HOLA is cross referenced in the Bank Act, it is clear that QTL as used in HOLA only applies to savings associations and, thus, legislative history on the meaning of QTL in HOLA is unenlightening as to the meaning of QTL in the Bank Act. The FIRREA provision rejected by the Conference Committee is the one discussed and explained in the floor manager's statement.

H.R. Rep. No. 206, 102d Cong., 1st Sess. 74-75 (1991).

If there was any doubt about how Congress intended for the non-QTL provisions to apply, this committee report excerpt makes it clear that Congress intends for the thirty percent cap (and the other non-QTL provisions) to apply to commercial bank members. See id. Since the only two interpretations of the applicability of the section 10(e) provisions are all members or only savings association members, this legislative history demonstrates that Congress intended the provisions to encompass the former.

IV. A Reviewing Court would Likely Uphold the Advances Rulemaking Only if it is Based on the Plain Meaning of the Law

The non-QTL requirements definitions contained in paragraph 10(e)(5) of the Bank Act create some confusion by cross referencing definitions from a law that only applies to savings associations. However, when one considers the precise statutory language ("members that are not [QTLs]"), the practical effect of the two alternative interpretations, the context of subsection 10(e) to encourage non-savings association members to hold more housing assets, and the legislative history, we believe the plain meaning of subsection 10(e) and the intent of Congress is clear and unambiguous: that the non-QTL requirements apply to all members. This is the approach taken in the proposed advances rule.

The Finance Board might determine that despite the plain meaning and the legislative history, the Board would prefer to apply the non-QTL provisions only to non-QTL savings associations. That raises the question, how deferential would courts be to this narrow interpretation in the somewhat likely event of a judicial challenge?

The Supreme Court has established parameters for an agency's authority to construe statutes that it administers. The first inquiry is whether there is ambiguity in the statute such that congressional intent cannot be determined. See Chevron, 467 U.S. at 842. In a number of recent cases, the Supreme Court has been critical of agency attempts to find ambiguity where none exists. See Marlin Industries, U.S. v. Primary Steel, Inc., 497 U.S. 116, 131 (1990), Department of Treasury v. Federal Labor Relations Auth. 494 U.S. 922, 932 (1990). In striking a regulatory review procedure, the Supreme Court said, "The strained interpretation offered by the Secretary [of Health and Human Services] is inconsistent with the express language of the statute." Bethesda Hosp. Assn. v. Bowen, 485 U.S. 399, 404 (1988).

As demonstrated above in this memorandum, careful analysis of the statutory language, the effect of the alternative interpretations, and the legislative history all strongly suggest that the only meaning Congress could have intended was to apply the non-QTL provisions to all members. The interpretation proposed by the FHLB-New York while arguably plausible on its

face, is not a reasonable and permissible interpretation of subsection 10(e) in light of the statutory language and legislative history.

The Supreme Court has determined that even when it is necessary to look at the statute as a whole to resolve confusion in statutory language, the agency is obliged to implement congressional intent where it can be ascertained. See Morash, 490 U.S. at 115. In a challenge to Office of Management and Budget (OMB) regulations, the court held that while the Paperwork Reduction Act did not specifically address the question at issue, the OMB's regulations were invalid to the extent they were inconsistent with congressional intent. See Dole v. United Steelworkers of America, 494 U.S. 26, 35, 42 n.10 (1990). Similarly, Finance Board regulations could be ruled invalid to the extent they are inconsistent with congressional intent.

Even if an ambiguity is found in the non-QTL provisions, the Finance Board's interpretation must be consistent with the alternatives that are raised by the ambiguity. The interpretation proposed by Krieg, DeVault, that insurance companies alone can somehow be carved out of "member that is not a [QTL]," is an implausible interpretation on its face. Under no circumstances can Congress be said to have intended a meaning that cannot be derived from the statutory language. In K Mart Corp. v. Cartier, Inc., 486 U.S. 281 (1988), the Court invalidated regulations because they were not based on an interpretation within the purview of the statute. See id. at 294. The Supreme Court has ruled that "no deference is due to agency interpretations at odds with the plain meaning of the statute itself." Public Employees Retirement System v. Betts, 492 U.S. 158, 171 (1989). An agency interpretation must be based on a permissible construction of the statute. See Chevron, 467 U.S. at 843.

If the Finance Board adopts either the insurance company carve out or the savings associations only interpretation of the non-QTL provisions, we believe there is a likelihood, in the event of a challenge, that the advances rulemaking would be overturned by a Federal court as not in accordance with the law. If the Board promulgates the advances final rule as drafted, which implements the non-QTL provisions consistently with their plain meaning and applies them to all members, we are confident that this interpretation of the non-QTL provisions would be upheld in the event of a judicial challenge.

Attachment

cc: Renie Y. Grohl

ATTACHMENT

CHRONOLOGY OF MAJOR DOCUMENTS AND STATEMENTS ADDRESSING THE APPLICABILITY OF THE BANK ACT'S NON-QTL PROVISIONS

- Kirkpatrick & Lockhart memorandum. Legal memorandum from Kirkpatrick & Lockhart to its FHLBank clients concluding that the Bank Act's non-QTL provisions apply to all members. August 9, 1989

- FHLB-New York memorandum. Memorandum from Susan G. Evans to Brian Dittenhafer, former FHLB-New York president, raising the question whether the Bank Act's non-QTL provisions should apply to commercial banks and credit unions. July 31, 1990

- FHLB-New York memorandum. Memorandum from Debra L. Kriss, FHLB-New York staff attorney, concluding that the Bank Act's non-QTL provisions do not apply to commercial banks, credit unions, or insurance companies, since they are not savings associations subject to the QTL test in section 10(m) of HOLA. September 11, 1990

- Buchanan, Ingersoll memorandum. Memorandum from outside counsel to FHLB-Pittsburgh concluding that a FHLBank may sell participation interests to other FHLBanks in non-QTL advances made to non-savings association members in order to prevent the FHLBank from exceeding its 30% limitation on advances to non-QTL members. (Cf. Finance Board General Counsel's Legal opinion dated August29, 1992 below.) April 19, 1991

- FHLB-Pittsburgh and FHLB-New York memorandum. Memorandum from Counsels to the FHLB-Pittsburgh and the FHLB-New York to Beth L. Climo, Finance Board General Counsel, concluding that the Bank Act's non-QTL provisions do not apply to commercial banks and credit unions. June 14, 1991

- FHLB-San Francisco letter. Letter from FHLB-San Francisco's General Counsel to Beth L. Climo, Finance Board General Counsel, concluding that all members are subject to the Bank Act's non-QTL provisions. July 19, 1991

- OGC (OL&EA) staff draft memo. **Internal Finance Board memorandum summarized and analyzed the arguments in the** 6/14/91 FHLB-Pittsburgh and FHLB-New York memorandum and in the 7/19/92 FHLB-San Francisco letter. July 21, 1991
As a result of this analysis and since this time OL&EA - Legal Division has taken the position that the non-QTL requirements apply to all members.

- FHLBank Counsel's meeting with then OGC (now OL&EA). At the FHLBank Counsel's 1991 fall meeting, Dana Yealy, FHLB-Pittsburgh General Counsel, led a discussion on the June 14, 1991, memorandum prepared by the FHLB-Pittsburgh and the FHLB-New York, which concluded that the Bank Act non-QTL provisions do not apply to commercial banks and credit unions. August 5, 1991

- Finance Board General Counsel's Legal Opinion on Participating Advances. Legal opinion from the Finance Board General Counsel concluding that the Bank Act does not prohibit a FHLBank from participating to another FHLBank its non-QTL advances made to non-savings association members and that such participation does not violate the capital stock subscription requirements for non-QTL members. August 29, 1991

- Taft, Stettinius & Hollister letter. Letter from outside counsel to the FHLB-Cincinnati concluding that insurance companies are not subject to the Bank Act's non-QTL provisions. November 7, 1991

- FHLBank Counsel's meeting with then OGC (now OL&EA). At the 1992 winter FHLBank Counsel's meeting, staff discussed the Finance Board's General Counsel's August 29, 1991 legal opinion on participating advances as a means of alleviating the 30 percent restriction on non-QTL advances. Implicit in that discussion was the need to find relief from the 30% limitation on non-QTL advances because of the application of the Bank Act's non-QTL provisions to all members. January 29, 1992

- Chairman Evans statements before the Subcommittee on Housing and Community Development on Baker/Neal Bill. The Chairman stated that commercial banks and credit unions are considered non-QTL members that are subject to more stringent stock purchase requirements for membership and borrowing than apply to savings associations and savings bank members. He emphasized that these provisions place a disproportionately high cost on commercial banks and credit unions contemplating joining the System. When asked whether the removal of these restrictions on commercial banks and credit unions would be unfair to savings associations required by law to be members, the Chairman stated that the Finance Board, in turn, would support legislation that would make membership voluntary for all members. See pages 186 through 188 of unpublished statements of Daniel F. Evans Jr. on Baker/Neal Bill (to be published as The Federal Home Loan Bank System Modernization Act of 1992, Hearing on H.R. 4973 Before the Subcommittee on Housing and Community Development, 103rd Cong., 2d Sess. (1992) (statement of Daniel F. Evans Jr., Chairman, Finance Board). June 9, 1992

- Draft advances regulation circulated to FHLBank Presidents. Draft regulation states that all members are subject to the Bank Act's non-QTL provisions. July 14, 1992

- FHLBank-Topeka's informal comment on draft advances regulation. Memorandum from George A. Kattermann, FHLB-Topeka Senior Vice President, to Frank Lowman, FHLB-Topeka President, informally commenting on the July 14, 1992 draft regulation, and recommending that the Bank Act's non-QTL provisions should not apply to insurance companies. July 29, 1992

- FHLBank-New York's informal comment letter on draft advances regulation. Letter from Brian Dittenhafer, FHLB-New York President, to Philip L. Conover, Finance Board Managing Deputy Director, informally commenting on the July 14, 1992 draft regulation, and recommending that the Bank Act's non-QTL provisions should only apply to savings associations. August 12, 1992

- Issues paper on proposed advances regulation. Issues paper on proposed advances regulation is sent to Finance Board which summarized how the proposed advances regulation will continue to apply the Bank Act's non-QTL provisions to all FHLBank members. The issues paper informs the Finance Board of the objections the FHLB-New York and FHLB-Des Moines made in their informal comment letters on the draft advances regulation regarding the applicability of the non-QTL provisions to non-savings association members, and explains the reasons why the proposed rule applies the restriction to such institutions. See Exhibit I to Item 2 of the September 23, 1992, Board book. September 18, 1992

- Board briefins on advances regulation. The Finance Board is briefed in a pre-board meeting briefing by staff on the proposed advances regulation and the issues paper. Staff provided a summary of how the proposed rule would continue to apply the Bank Act's non-QTL provisions to all members, and explained the reasons why this approach was taken. September 23, 1992

- September 23, 1992 Board meeting. While summarizing the key provisions of the proposed advances regulation, staff informed the Finance Boardthat the proposed regulation would continue the current practice of applying the Bank Act's non-QTL provisions to all members. The Board unanimously approved the proposed advances regulation. See Lines 13 through 19 on page 49 of the September 23, 1992, Board meeting transcript. September 23, 1992

- Proposed Advances Resulation Published in Federal Register The proposed advances regulation was published in the Federal Register on October 1, 1992 requesting public comment on or before November 30, 1992. Section 935.13 of the proposed rule continued the practice of applying the Bank Act's non-QTL provisions to all members. See 57 Fed. Reg. 45338, 45351 (1992) (to be codified at 12 C.F.R. § 935.13). The preamble to the proposed rule provided the following reasons for applying the non-QTL provisions to all members: (1) the Bank Act's non-QTL provisions on advances must apply to non-savings association members, since the HOLA prohibits savings association members that fail the QTL test from receiving any further advances, and (2) the explicit exemption of savings banks, but not other non-savings association members, suggests that the requirement was intended to have broader application than to just savings associations. See id. at 45344 October 1, 1992

- Comments on the proposed advances regulation. The Finance Board received seven comment letters opposing in part or in whole the proposed advances regulation's application of the non-QTL provisions to all non-savings associations.

  - Life Insurance Council of New York. November 20, 1992
  -- New York Life Insurance Company. November 20, 1992
  __ FHLB-New York. November 24, 1992
  -- Lincoln National Investment Management Company. November 25, 1992
  -- American Council of Life Insurance. November 30, 1992
  - Meridian Insurance Company. November 30, 1992
  -- FHLB-Des Moines. November 30, 1992

- Draft final rule on advances. The draft final rule would continue to apply the Bank Act's non-QTL provisions to all members.

- FHLB-New York letter to the Board members. Less than one week before the Finance Board's scheduled consideration of the advances final rule, the FHLB-New York sent a letter to the Finance Board objecting to the draft final rule's application of the Bank Act's non-QTL provisions to insurance companies. Attached to the letter was a memorandum from Harold J. Fletcher to Alfred A. DelliBovi, FHLB-New York President, raising no new arguments. Also attached was a legal analysis that raised the same arguments raised earlier and suggested that the non-QTL provisions may be construed very narrowly to apply only to a never used provision for special liquidity advances made at the request of the OTS to troubled savings associations under section 10(h) of the Bank Act. January 21, 1993

- FHLBank Counsel's meeting with OL&EA. At the FHLBank Counsels' winter meeting in Washington, Counsels for the FHLB-Des Moines, FHLB-New York, and FHLB-Pittsburgh took the position that the Bank Act could be construed as giving the Finance Board the flexibility to interpret the non-QTL provisions as inapplicable to commercial banks, credit unions, and insurance companies. They maintained that it is a policy decision for the Finance Board, rather than a legal issue. They agreed to provide the OL&EA with a legal analysis in support of their position. February 3, 1993

- FHLB-Indianapolis retains Krieg, DeVault, Alexander & Capehart. The FHLB-Indianapolis took the lead for a group of FHLBanks who are trying to marshal arguments that the Bank Act's non-QTL provisions do not apply to insurance companies, commercial banks, and credit unions. February 5, 1993

- Conference Call between OL&EA staff and FHLBank counsel. OL&EA staff spoke with counsels from the FHLBanks of Indianapolis, New York, Des Moines, and Pittsburgh, as well as lawyers from the law firm of Krieg, DeVault. The FHLBank counsels and Krieg, DeVault were seeking to understand the arguments they are up against in attempting to limit the applicability of the non-QTL provisions. February 8, 1993

- Krieg DeVault issues opinion. Krieg, DeVault's legal opinion, that the non-QTL provisions need not apply to insurance companies, is provided to their FHLBank clients and the Finance Board. March 16, 1993 (provided to the Finance Board on March 19, 1993)

- OL&EA memorandum. The Finance Board's OL&EA provides a memorandum to the Finance Board concluding that the non-QTL provisions are probably intended to apply to all members and that in no event may insurance company members alone be carved out. March 30, 1993

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March 30, 1993