



Federal Housing Finance Board

February 1, 1994

TO: Philip L. Conover
Managing Director

FROM: Beth L. Climo
General Counsel

SUBJECT: Effect of an Acquisition on the QTL Status of
Advances

ISSUES:

- (A) Whether advances assumed pursuant to an acquisition of a member that is a Qualified Thrift Lender ("QTL") by a non-QTL institution are subject to the non-QTL advances-to-stock purchase requirements set forth at 12 C.F.R. § 935.15(a)(2): (1) at the time the non-QTL institution becomes a Federal Home Loan Bank ("FHLBank") member, where the non-QTL institution was not a FHLBank member at the time of the acquisition; or (2) at the time of the acquisition, where the non-QTL institution already is a FHLBank member; and
- (B) Whether the assumed advances must be included in the calculation of the non-QTL member's advances-to-stock purchase requirement pursuant to 12 C.F.R. § 935.13(a)(1)(ii) when the non-QTL member applies for new advances or for a renewal of advances.

CONCLUSIONS:

- (A) A non-QTL institution is not required to purchase additional FHLBank stock for advances that were originally made to a QTL member of a FHLBank and subsequently were assumed by the non-QTL institution pursuant to an acquisition, either: (1) at the time the non-QTL institution becomes a FHLBank member, where it was not a member at the time of the acquisition; or (2) at the time of the acquisition, where the non-QTL institution was a FHLBank member at the time of the acquisition. See 12 C.F.R. § 935.15(a)(2).

- (B) The assumed advances must be included in the calculation of the non-QTL member's advances-to-stock purchase requirement when the non-QTL member applies for new advances or requests a renewal of advances. See 12 C.F.R. § 935.13(a)(1)(ii).

DISCUSSION:

1) BACKGROUND

In a letter dated September 14, 1993, the Federal Home Loan Bank of Boston ("the Bank") asked the Office of Legal and External Affairs of the Federal Housing Finance Board ("Finance Board") to evaluate the QTL status of advances originally made to a FHLBank member exempt from the non-QTL special stock purchase requirements ("the QTL member") which was acquired by a non-QTL institution that was not a FHLBank member at the time of the acquisition ("the non-QTL institution"). The Bank allowed the acquiring non-QTL institution to assume the advances pursuant to the orderly liquidation of the QTL member's indebtedness. The advances were to be paid upon maturity. The acquiring non-QTL institution subsequently became a member of the Bank ("the non-QTL member"), which prompted the Bank to question the QTL status of the assumed advances.

Although the Bank has presented a situation involving an assumption of QTL advances by a non-QTL institution that was not a FHLBank member at the time of the acquisition, the same issues presented by the Bank arise when a non-QTL member assumes outstanding advances pursuant to the acquisition of a QTL member. The fact that the non-QTL institution in the instant case was not a FHLBank member at the time of the acquisition and assumed the QTL advances pursuant to an "orderly liquidation" of the advances is not dispositive of the issues presented. The questions presented apply to situations that arise any time a non-QTL institution that either is a FHLBank member or subsequently becomes a FHLBank member assumes outstanding QTL advances pursuant to an acquisition of a QTL member.

1. Note that the section of the Finance Board's advances regulation regarding intradistrict transfers of advances indicates that a FHLBank may allow one of its members to assume an advance extended by the FHLBank to another of its members, provided the assumption complies with the Finance Board's regulations governing the issuance of new advances. 12 C.F.R. § 935.17 (effective December 15, 1993, section 935.17 was amended to authorize the transfer of advances from non-FHLBank members to FHLBank members). This opinion addresses only the assumption of advances pursuant to an acquisition. It does not address the QTL status of advances transferred from a QTL member to a non-QTL member pursuant to an intradistrict transfer.

11) NEITHER THE LAW GOVERNING ADVANCES NOR THE LAW GOVERNING MEMBERSHIP REQUIRES A NON-OTL INSTITUTION TO MAKE ADDITIONAL ADVANCES-TO-STOCK PURCHASES WHEN IT ASSUMES ADVANCES PURSUANT TO THE ACQUISITION OF A OTL MEMBER

In addition to the minimum subscription requirements for membership in a FHLBank, the Federal Home Loan Bank Act ("Bank Act") specifies two stock purchase requirements based on advances levels. See 12 U.S.C. § 1426(b); 12 C.F.R. § 933.7 ("advances-to-stock purchase requirements"). One provision requires all members to hold FHLBank stock in an amount equal to at least five percent of outstanding advances (i.e., a FHLBank may not allow a member's aggregate amount of outstanding advances to exceed 20 times the amount paid in for capital stock in the FHLBank). See 12 U.S.C. § 1430(c); 12 C.F.R. § 935.15(a)(1). Non-QTL members must hold FHLBank stock, at the time an advance is received, in an amount equal to five percent of the member's total advances, divided by the member's actual thrift investment percentage ("ATIP"). See 12 U.S.C. § 1430(e)(1); 12 C.F.R. § 935.13(a)(1)(ii).

Nothing in the Bank Act requires a non-QTL institution to make additional advances-to-stock purchases when, pursuant to an acquisition, it assumes advances originally made to a QTL member. In fact, by providing that a non-QTL "may only receive an advance if it holds stock in its FHLBank at the time it receives the advance [in an amount equal to five percent of the member's total advances divided by the member's ATIP]" Congress seemed to intend that the advances-to-stock purchase requirements were to be applied only at the time of the making of a new advance. 12 U.S.C. § 1430(e)(1) (emphasis added).

The Finance Board advances regulation has interpreted the statutory advances-to-stock purchase requirements to apply at the time of the making or renewal of advances. See

2. The Home Owners' Loan Act ("HOLA") prevents savings associations from obtaining any "new advances" from a FHLBank if such institutions fail to become and remain QTLs. See 12 U.S.C. § 1467a(m)(3)(B)(i)(III). Although the Bank Act does not use the specific language "new advances" in the non-QTL advances-to-stock purchase requirements, the provision is a similar provision intended to apply at the time of the making of a new advance. See id. § 1430(e).

3. The Finance Board's advances regulation does not attempt to interpret or implement the HOLA restrictions on non-QTL savings associations. See 58 Fed. Reg. 29458, 29465 (May 20, 1993) (Comment accompanying Final Rule, 12 C.F.R. § 935). The Office of Thrift Supervision ("OTS") is responsible for monitoring savings associations' compliance with the QTL test, and for interpreting and enforcing any HOLA restrictions

12 C.F.R. § 935.13(a)(1). The regulation provides that a Bank "may make or renew an advance to a non-QTL member" only under specified conditions, including the special stock purchase requirements for non-QTL members. Id. § 935.13(a)(1) (emphasis added). The Finance Board's usage of the language "may make or renew" contemplates application of the stock-purchase requirements when a FHLBank member takes down new advances or renews advances. Id.

The Finance Board's membership regulation lends further support for the application of the advances-to-stock purchase requirements at the time a new advance is made or an advance is renewed.- See 12 C.F.R. § 933.12(d)(2)(ii)(A). When a non-member institution acquires a member and assumes its advances, the statutory and regulatory membership requirements provide for orderly liquidation of the disappearing institution's advances, as determined by the FHLBank. See 12 U.S.C. § 1426(e); 12 C.F.R. §§ 933.12; 933.16; 935.19. While the assumed advances are being liquidated, the FHLBanks require the consolidated institution to hold FHLBank stock until the advances are repaid, and do not allow redemption of the stock necessary to support the already outstanding advances.⁴ The membership regulation requires a consolidated institution approved for membership to "purchase any additional amount of stock required to meet the minimum subscription requirement." 12 C.F.R. § 933.12(d)(2)(ii)(A) (emphasis added). This language, and the absence of any provision in the advances

(Footnote 3 continued from previous page)
applicable to institutions that fail the QTL test, including the restrictions on advances to non-QTL savings associations. See id.

4. See 12 U.S.C. § 1426(e) (requiring an orderly liquidation of a FHLBank member's indebtedness to its FHLBank, as determined by the FHLBank, at the time such FHLBank member's membership is terminated); id. § 1430(c) (providing that the FHLBank shall have a lien upon and shall hold the stock of FHLBank members receiving advances as collateral security (in addition to obtaining a security interest in qualifying collateral set forth at 12 U.S.C. § 1430(a)) for all indebtedness of the FHLBank member); 12 C.F.R. §§ 933.16; 935.19. As stated in Section I above, the analysis herein does not turn on the fact that advances were assumed pursuant to an orderly liquidation, but on the fact that the Bank Act and the Finance Board's advances regulation require a calculation of stock purchase requirements only at the time a new advance is received or an advance is renewed. See 12 U.S.C. §§ 1426(e), 1430(e)(1); 12 C.F.R. §§ 933.16; 935.13(a)(1); 935.19; Section I, supra.; Section III, infra. (noting that when a non-QTL member applies for new advances or a renewal of existing advances, the assumed advances must be included in the non-QTL member's advances base in determining its advances-to-stock purchase requirement).

regulation requiring new non-QTL members to purchase additional stock to meet the non-QTL advances-to-stock purchase requirements, seems to recognize that the consolidated institution already holds sufficient FHLBank stock to support the advances it assumed. See id.

In sum, neither the advances regulation nor the membership regulation require a non-QTL institution that assumes advances pursuant to an acquisition of a QTL member to make additional advances-to-stock purchases for the assumed advances, either at the time of the acquisition, where the non-QTL institution is an existing FHLBank member, or, where the non-QTL institution was not a FHLBank member at the time of the acquisition, at the time the non-QTL institution becomes a FHLBank member. See id. §§ 933.12(d)(2)(ii)(A); 935.13(a)(1)(ii).

III) THE NON-OTL ADVANCES-TO-STOCK PURCHASE PROVISIONS REQUIRE THE CALCULATION OF A NON-QTL MEMBER'S TOTAL ADVANCES TO INCLUDE ASSUMED OTL ADVANCES AT THE TIME OF THE MAKING OF A NEW ADVANCE OR THE RENEWAL OF AN ADVANCE

Although the capital stock requirement for the advances assumed by the non-QTL institution as a result of an acquisition remains unchanged at the time of the acquisition, the assumed debt must be included in the non-QTL member's total advances base to determine its advances-to-stock purchase requirements at the time new advances are made or previous advances are renewed. See 12 U.S.C. § 1430(e)(1); 12 C.F.R. §§ 935.13(a)(1); 935.15(a)(2).

The Finance Board's advances regulation implements the non-QTL advances-to-stock purchase requirements in section 10 of the Bank Act, requiring a member to hold FHLBank stock at the time it obtains an advance in an amount equal to at least five percent of the outstanding principal amount of the [FHLBank] member's total advances, divided by such member's ATIP." Id. § 935.13(a)(1)(ii) (emphasis added); 12 U.S.C. § 1430(e)(1). Section 935.1 sets forth the definition of "advance:"

[a]dvance means a loan from a [FHL]Bank that is:

- (1) Provided pursuant to a written agreement;
- (2) Supported by a note or other written evidence of the borrower's obligation; and
- (3) Fully secured by collateral in accordance with the [Bank] Act and this part.

12 C.F.R. § 935.1. See also 12 U.S.C. § 1430(a).

Although the statute does not define the phrase "total advances," Webster's Dictionary (9th ed. 1990) defines "total" as "comprising or constituting a whole: entire." Therefore, the plain meaning of the phrase "total advances" would be the entire

amount of advances held by the FHLBank member at the time a new advance is made or a previous advance is renewed. See 12 C.F.R. § 935.13(a)(1)(ii); 12 U.S.C. § 1430(e).

The policy underlying the non-QTL advances-to-stock purchase requirements supports including the assumed advances in the non-QTL member's total advances at the time advances are renewed or new advances are made. The Financial Institutions Reform, Recovery and Enforcement Act of 1989, Pub. L. 101-73, 103 Stat. 183 (Aug. 9, 1989) ("FIRREA") expanded membership in the FHLBank System to include non-thrift institutions such as commercial banks and credit unions engaged in mortgage lending, but retained preferential treatment for QTLs. See H.R. Conf. Rep. No. 222, 101st Cong., 1st Sess. 424-25 (1989). In order to allow non-thrift institutions to gain access to FHLBank advances for housing finance without first requiring the institutions to satisfy the QTL test (requiring a minimum of 65 percent of assets in "qualified thrift investments"), Congress placed higher stock requirements on FHLBank members that are not QTLs. See 135 Cong. Rec. S. 10206 (daily ed. Aug. 4, 1989) (Statement of Sen. Riegle); 12 U.S.C. §§ 1467a(m) (HOLA definition of QTL); 1430(e)(1). The effect of the ratio used to determine stock purchase requirements for non-QTL members (five percent of advances divided by the ATIP) is that the lower the percentage of the non-QTL member's portfolio invested in home mortgage assets, the more FHLBank stock the non-QTL member must purchase in order to receive advances. See 12 U.S.C. § 1430(e)(1); 12 C.F.R. § 935.13(a)(1)(ii).

Therefore, the non-QTL advances-to-stock purchase provisions require the FHLBank to include the assumed advances in calculating the non-QTL member's total advances base at the time new advances are made or previous advances are renewed. See id.

CONCLUSION:

Neither the law governing advances nor the law governing membership requires a non-QTL institution to purchase additional FHLBank stock as a result of an assumption of advances pursuant to an acquisition of a QTL member, either at the time of the acquisition, where the non-QTL institution is a FHLBank member, or at the time the non-QTL institution becomes a FHLBank member, where the institution was not a FHLBank member at the time of the acquisition. Id. See 12 U.S.C. §§ 1426(b)(2); 1430(c); 12 C.F.R. §§ 933.12(d); 935.13(a)(1)(ii). However, the statutory and regulatory provisions governing non-QTL advances-to-stock purchases require the inclusion of assumed advances in the non-QTL member's total advances base in order to determine the non-QTL member's advances-to-stock purchase

requirement at the time new advances are made or previous advances are renewed. 12 U.S.C. § 1430(e)(1); 12 C.F.R. § 935.13(a)(1)(ii).



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