



Federal Housing Finance Board

March 18, 1999

OPINION OF THE OFFICE OF GENERAL COUNSEL

ISSUES: May the Federal Housing Finance Board (Finance Board) promulgate a regulation authorizing Federal Home Loan Banks (FHLBanks) to accept as collateral for advances under section 10(a)(2) of the Federal Home Loan Bank Act (Bank Act) individual mortgages or other individual loans, regardless of delinquency status, to the extent that such mortgage or loan is guaranteed or insured by the United States or any agency thereof?

CONCLUSIONS:

Yes. Although section 10(a)(1) of the Bank Act requires that whole mortgages loans be not more than 90 days delinquent in order to qualify as collateral eligible secure member advances, delinquent mortgages and other loans may be accepted as government securities under section 10(a)(2) to the extent that they are federally guaranteed or federally insured. The non-delinquency requirement of section 10(a)(1) exists in order to ensure that the mortgages accepted thereunder qualify as low risk assets; however, this concern is effectively addressed to the extent that the mortgage, or other loan, is federally guaranteed or federally insured.

I. Introduction

Section 10(a) of the Federal Home Loan Bank Act (Bank Act) enumerates four categories of collateral that members may use to secure Federal Home Loan Bank (FHLBank) advances:

- (1) Fully disbursed, whole first mortgages on improved residential property (not more than 90 days delinquent), or securities representing a whole interest in such mortgages.
- (2) Securities issued, insured, or guaranteed by the United States Government or any agency thereof (including without limitation, mortgage-backed securities issued or guaranteed by the Federal Home Loan Mortgage Corporation, the Federal National Mortgage Corporation, and the Government National Mortgage Corporation).

(3) Deposits of a Federal Home Loan Bank.

(4) Other real estate related collateral acceptable to the Bank if such collateral has a readily ascertainable value and the Bank can perfect its interest in the collateral. The aggregate amount of outstanding advances secured by such other real estate related collateral shall not exceed 30 percent of such member's capital.

12 U.S.C. § 1430(a). Section 935.9(a) of the Finance Board's regulations implements these statutory collateral requirements. See 12 C.F.R. § 935.9(a). While section 935.9(a) clarifies the Bank Act's reference to "securities representing a whole interest" in residential mortgage loans and lists examples of eligible "other real estate-related collateral," it otherwise restates the substance of section 10(a) of the Bank Act, without further clarification.

In response to FHLBank requests to clarify certain aspects of section 935.9(a), the Office of General Counsel (OGC) has prepared an amendment to section 935.9(a)(2)¹ to make clear that FHLBanks may accept as collateral for advances to members:

- (ii) mortgages or other loans, regardless of delinquency status, to the extent that the mortgage or loan is insured or guaranteed by the United States or any agency thereof, or otherwise is backed by the full faith and credit of the United States, and such insurance, guarantee or other backing is for the direct benefit of the holder of the mortgage or loan; and
- (iii) securities backed by, or representing an equity interest in, mortgages or other loans referred to in paragraph (a)(2)(ii) of this section.

It is the opinion of OGC that the Finance Board may authorize the FHLBanks to accept such individual federally-guaranteed and insured loans as government securities collateral under section 10(a)(2) of the Bank Act.

II. Analysis

A. The Meaning of the Word "Securities" in Section 10(a)(2) of the Bank Act is Ambiguous and, Thus, May Be Reasonably Interpreted by the Finance Board

Neither the plain language of section 10(a)(2) nor its legislative history makes clear whether Congress intended to permit FHLBanks to accept individual federally-guaranteed or insured loans (as opposed to instruments representing interests in pools of such loans) as government "securities" collateral under section 10(a)(2). See 12 U.S.C. § 1430(a); H.R. Rep. No. 222, 101st Cong., 1st Sess. 427-28 (1989). Accordingly, as the agency charged with the administration of the Bank Act, see 12 U.S.C. § 1422b(a)(1), the Finance Board must determine

¹ The rule drafted by OGC also would amend section 935.9(a) of the regulations to permit FHLBanks to accept as collateral shares of mutual funds or similar investments representing an undivided equity interest in underlying assets that qualify as eligible collateral. The statutory authority under which FHLBanks may accept such collateral has been addressed previously by OGC. See Memorandum from Sharon B. Like through Renie Y. Grohl to Beth L. Climo (March 24, 1995).

whether FHLBanks may accept as collateral such federally-insured and federally-guaranteed mortgages and other loans under section 10(a)(2) of the Bank Act.

Courts will uphold an agency's "permissible interpretation" of a statute that the agency administers if, using traditional rules of statutory construction, the court determines that "Congress has not directly addressed the precise question at issue" in the statute or its legislative history. *Chevron, U.S.A., Inc. v. Natural Resources Defense Council*, 467 U.S. 837, 843 & n.9 (1984). Under *Chevron*, a "permissible interpretation" is one that represents a "reasonable accommodation of conflicting policies that we're committed to the agency's care by the statute." *Id.* at 845 (*quoting United States v. Shimer*, 367 U.S. 374,382-83 (1961)). Even if the agency's interpretation or corresponding policy choice is one that the court would not have chosen itself, the court may not overturn the interpretation unless "it appears from the statute or legislative history that the accommodation is not one that Congress would have sanctioned." *Id. See Investment Co. Inst. v. Conover*, 790 F.2d 925 (D.C. Cir. 1986), cert. denied, 479 U.S. 939 (1986) (wherein the court granted *Chevron* deference to the Comptroller of the Currency's interpretation of the word "securities" as used in the Glass-Steagall Act).

The word "securities" does not "as a general matter . . . [have] an ascertainable ordinary meaning in all contexts." See *Conover*, 790 F.2d at 933. In that neither the Bank Act itself nor the legislative history makes clear the precise meaning of the word "securities" as used in section 10(a)(2), Congress has implicitly delegated to the Finance Board the authority to adopt a reasonable interpretation of the term. For several reasons, it is reasonable to interpret the word "securities," as used in section 10(a)(2) of the Bank Act, as including individual federally-guaranteed and insured loans.

B. It Is Reasonable for the Finance Board to Interpret Section 10(a)(2) of the Bank Act to Authorize FHLBanks to Accept as Collateral Individual Loans and Mortgages That Are Federally-Guaranteed or Insured

1. The Legislative History Reveals That Safety and Soundness, and Not an Instrument's Technical Status as a "Security," Was the Primary Concern in Drafting Section 10(a)(2)

The legislative history of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA), Pub. L. 101-73, § 714, 103 Stat. 412 (1989), which added to the Bank Act the current text of section 10(a), indicates that the intent behind section 10(a) generally was to permit the FHLBanks to accept as collateral assets that present a minimum of risk to the FHLBanks. See H.R. Rep. No. 222 at 427 (stating that amended section 10(a) limits eligible collateral to "low-risk assets"). To the extent that a security - regardless of whether it is a mortgage-backed security, a bond, or an individual loan or mortgage - is backed by federal insurance, or by a federal guarantee, there is virtually no risk of loss to the holder of the instrument or to a secured party having a lien on the instrument, even if the principal or interest payments thereon are delinquent. As such, reading the authorization in section 10(a)(2) broadly to include individual federally-insured and federally-guaranteed loans and mortgages would not be inconsistent with the apparent Congressional intent behind that provision.

2. The FHLBanks Have Previously Been Authorized to Accept Individual Federally-Guaranteed and Insured Loans as Collateral and Congress Has Shown No Intent to Overturn This Authority

Pursuant to the collateral schemes that have been set forth in earlier incarnations of section 10(a) of the Bank Act, the FHLBank System regulator has permitted FHLBanks to accept as collateral individual loans and mortgages that are insured or guaranteed by the federal government. There is no indication that, in drafting section 10(a) in 1989, Congress intended to halt this practice.

Under the Bank Act, as originally enacted in 1932, the FHLBanks were authorized to accept only mortgage loans as collateral for advances. In 1934, Congress amended the Bank Act to permit the FHLBanks to accept as collateral “obligations of the United States, or obligations fully guaranteed by the United States.” See 12 U.S.C. § 1430(a)(4) (1935). The former Federal Home Loan Bank Board (FHLBB) implemented this statutory authority through its regulations, which, from 1936 through 1984, authorized the FHLBanks to make advances to members “on the security of obligations of the United States.” See 24 C.F.R. § 5.3(a) (1937); 24 C.F.R. § 125.10 (1949); 12 C.F.R. § 525.10 (1959). In turn, the regulations defined the term “obligations of the United States” to include “all evidences of indebtedness issued by the United States or fully guaranteed as to principal and interest by the United States.” See 24 C.F.R. § 1.13 (1937); 24 C.F.R. § 121.9 (1949); 12 C.F.R. § 521.9 (1959). In that individual loan and mortgage notes clearly qualify as “evidences of indebtedness,” it appears that individual federally-guaranteed loans and mortgages were eligible to secure advances under the statutory and regulatory collateral provisions that were in place between 1936 and 1984. This view is supported by a 1952 FHLBB legal opinion that concluded that “[f]arm mortgages insured under Title I of the Bar&head-Jones Farm Tenant Act . . . are classed as obligations fully guaranteed by the United States” eligible to be used as collateral for advances under (then) section 10(a)(4) of the Bank Act. Op. G.C. FHLBB (June 10, 1952).

In 1982, Congress amended section 10(a) of the Bank Act by eliminating the list of specific types of eligible collateral and replacing it with a provision that authorized each FHLBank “to make secured advances to its members upon such security as the Board may prescribe.” See Pub. L. 87-779, § 352, 96 Stat. 1507 (Oct. 15, 1982). In response to this statutory change, the FHLBB amended the collateral provisions of its regulations in 1984 to permit FHLBanks to accept as collateral, *inter alia*, “[s]ecurities issued, insured or guaranteed by the United States Government or any agency thereof.” See 12 U.S.C. § 525.7 (1985). The FHLBB explained that it was adopting the provisions in response to the elimination of statutory restrictions on collateral so as to “provide the [FHL]Banks with significant flexibility in determining acceptable advances collateral from members.” See 49 Fed. Reg. 34197 (1984). Accordingly, by using the word “securities,” as opposed to “obligations,” the FHLBB did not intend to narrow the range of federally-insured and guaranteed assets that were eligible to secure advances, but merely chose to use a different term, possibly in order to make clear that the FHLBanks could accept equity, as well as debt, securities.

² Like the term “obligations,” as defined by the FHLBB, the term “securities” may include “evidences of indebtedness.” See Black’s Law Dictionary 1216-17 (5th ed. 1979).

In 1989, as part of FIRREA, Congress again amended section 10(a) of the Bank Act to appear in its current form. In doing so, Congress essentially enshrined the language of the FHLBB's existing collateral regulation into section 10(a) of the statute. *Compare* 12 C.F.R. § 525.7(a) (1989) with 12 U.S.C. § 1430(a) (1994) (paragraphs (1), (2) and (3) are identical; paragraph (4) is more restrictive in the amended Bank Act than in the FHLBB regulation). Specifically, section 10(a)(2) of the Bank Act is a verbatim transcription of the authority that was formerly set forth in section 525.7(a)(2) of the FHLBB's regulations. In the absence of any legislative history to the contrary, it is therefore reasonable to conclude that Congress intended to continue to permit the FHLBanks to accept as collateral the same types of government securities under section 10(a)(2) of the Bank Act as were permitted by the FHLBB under section 525.7(a)(2) of its regulations. Because the FHLBanks had been permitted to accept individual federally-guaranteed loans and mortgages under section 525.7(a)(2) and its predecessor provisions, it is reasonable to conclude that the FHLBanks continue to be authorized to accept these types of collateral under current section 10(a)(2) of the Bank Act.

3. The Drafters of the Original Bank Act Considered Mortgages to be Securities

Finally, while Congress gave no indication in the legislative history of FIRREA of its intent with respect to the scope of the word "securities," the legislative history of the original Bank Act clearly demonstrates a general understanding on the part of Congress in 1932 that mortgages are a "security." Most revealing is the Report of the Committee on Banking and Currency that accompanied the bill that was to become the Bank Act when it was submitted to the House of Representatives for consideration. The Report stated:

There is some \$20,000,000,000 in *mortgages* on small homes in the country to-day. Nearly \$8,000,000,000 of these are held by building and loan associations. The balance are held by banks, insurance companies, and private investors. Fundamentally, *these securities* are as sound as we have in America to-day, but these worthy institutions can not raise any funds on *their mortgages* at the present time.

H.R. Rep. No. 1418, 72d Cong., 1st Sess. 3 (1932) (emphasis added).

Similarly, in the House debates on the bill, mortgages were referred to as "securities" - both explicitly and implicitly - time and again by both supporters and opponents of the proposed legislation. For example, Rep. Hill, a member of the House Committee on Banking and Currency (which drafted the bill, see *id.* at 1), stated on the floor of the House of Representatives:

Fundamentally the *safest and soundest securities are those issued upon real estate* on a conservative basis of value. There are about twenty billions of dollars of *investments in home-loan mortgages* in this country. These are for the most part long-term loans, and while they basically safe, they have little liquidity and are therefore not readily negotiable. They constitute a \$20,000,000,000 block of frozen assets, since the banks refuse to *advance loans on securities* not capable of being readily converted into cash.

75 Cong. Rec. H12,604 (1932) (emphasis added). *See also* 75 Cong. Rec. H12,586 (1932) (statement of Rep. Reilly) (expressing support by stating that “[h]ome mortgages constitute sound securities”); *id.* at H12,588 (statement ‘of Rep. Reilly) (expressing support by stating that “home-mortgage institutions . . . have plenty of good securities, but because of the depression they lack liquid funds, and this bill provides a method by which they may secure such funds”); *id.* at H12,594 (statement of Rep. Williams) (expressing opposition by stating that “[u]nder [current] conditions mortgage securities can not be brought together to furnish the basis for a sound legal bond issue”); *id.* at H12,605 (statement of Rep. Hill) (expressing support by stating that “it is easier and less expensive to finance any business or industry or any commodity than it is to finance the building or purchasing of a home” because “the long-term home loan securities, are not now liquid”).

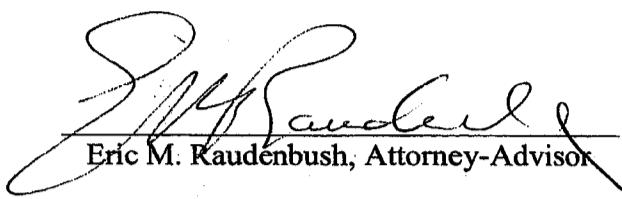
Based in part upon this legislative history, the Finance Board has interpreted the word “securities,” as used in the provisions of the Bank Act governing FHLBank investment powers, see 12 U.S.C. §§ 1431(h), 1436(a), to include whole mortgage loans. See Memorandum from Deborah F. Silberman, Deputy General Counsel, to Bruce A. Morrison, Chairman (May 13, 1996); Finance Board Res. No. 96-44 (July 3, 1996); Finance Board Res. No. 96-111 (Dec. 23, 1996); Finance Board Res. No. 98-41 (Sept. 23, 1998); *Texas Savings & Community Bankers Ass'n v. Federal Housing Finance Board*, No. A-97-CA-421-SS (W.D. Tex. June 25, 1998) (upholding Finance Board interpretation). Although this legislative history is more conclusive regarding the Bank Act’s investment provisions (which were part of the original Act in 1932) than regarding the 1989 collateral provisions, it further indicates that a characterization of individual mortgages (if not other types of loans) as “securities” under the Bank Act is reasonable. In addition, when interpreting statutory language, courts generally presume that the same words used twice in the same statute have the same meaning. See *ICC Indus., Inc. v. United States*, 812 F.2d 694 (9th Cir. 1987); *Sutherland Stat. Const.* § 46.06 (5th ed. 1992).

C. The Non-Delinquency Requirement for Mortgages Set Forth In Section 10(a)(1) Need Not Be Applied to Federally-Guaranteed and Insured Mortgages Under Section 10(a)(2)

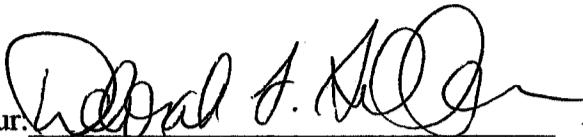
Although individual loans and mortgages may be considered to be “securities” under section 10(a)(2) of the Bank Act, section 10(a)(1) specifically addresses acceptance of whole residential mortgages as collateral for FHLBank advances and requires that such mortgages be “not more than 90 days delinquent” to qualify as eligible collateral. See 12 U.S.C. 1430(a)(1). Read technically, this provision might be construed as preventing the FHLBanks from accepting delinquent federally-insured and guaranteed mortgages (but not other types of loans) as collateral.

However, as evidenced by the legislative history of FIRREA, referenced above, the non-delinquency requirement of section 10(a)(1) appears to have been included in order to ensure that whole mortgages accepted by a FHLBank as collateral qualify as “low risk” assets. Because the additional risk inherent in a delinquent mortgage is effectively eliminated to the extent that the principal and/or interest payments thereon are federally-guaranteed or federally-insured, there is no conflict in regarding the federally-insured or federally-guaranteed portions of delinquent mortgages to be government securities for purposes of section 10(a)(2), while continuing to

require that other whole mortgages meet the requirements of section 10(a)(1) of the Bank Act in order to be eligible as collateral. See *Faircloth Frederick Smiling v. Lundy Packing Co.*, 91 F.3d 648 (4th Cir. 1996) (statutory interpretations should both strive to implement the policy of Congress and harmonize all provisions of the statute).



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I concur.

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