



REGULATORY INTERPRETATION 1999-RI-12

Date: July 9, 1999

Subject: Eligibility of Guaranteed Student Loans to be Accepted as Government Securities Collateral for Federal Home Loan Bank Advances

Request Summary:

A Federal Home Loan Bank (FHLBank) sought an interpretation as to whether, under section 935.9(a)(2)(ii) of the Federal Housing Finance Board (Finance Board) regulations, 12 C.F.R. § 935.9(a)(2)(ii), the FHLBank may accept as eligible advances collateral guaranteed student loans (GSLs) made under the Federal Family Education Loan Program (FFELP), where the member pledging the GSLs as collateral administers the state's FFELP GSL guarantee program, in addition to holding GSLs in portfolio.

Background:

Section 935.9(a)(2)(ii) (12 C.F.R. § 935.9(a)(2)(ii)) authorizes the FHLBanks to accept certain federally insured or guaranteed instruments as collateral for advances, as follows:

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[.]

Under the FFELP, the holder of a GSL enjoys the benefit of a guarantee provided by a state-chartered guarantee agency established and operating under the parameters set forth in Title IV of the Higher Education Act of 1965, as amended. 20 U.S.C. §§ 1001 *et seq.* If a borrower defaults on a GSL, or if certain other contingencies occur, the holder of the GSL may file a claim with the appropriate guarantee agency, which, provided that the GSL has been properly originated and serviced, pays the holder all or a portion of the unpaid principal balance and accrued interest. 20 U.S.C. § 1078(c). In turn, the Department of Education (DOE) has a contractual obligation, imposed by statute, to reimburse the guarantee agency for amounts properly paid to holders of GSLs that are in default or that meet the other statutory contingencies. 20 U.S.C. § 1078(c). The Higher Education Act further provides that, if the Secretary of Education determines that a guarantee agency is unable to meet its obligations as guarantor, holders of GSLs may submit insurance claims directly to the DOE and the DOE must pay to the holder of the GSL the full obligation of the guarantee agency until such time as the obligations are transferred to a new guarantee agency capable of meeting these obligations. 20 U.S.C. § 1082(o).

Discussion:

As indicated in the preamble to the recent final rule that added section 935.9(a)(2)(ii) to its regulations, *see* 64 Fed. Reg. 16621 (Apr. 6, 1999), the Finance Board generally does not consider either GSLs reinsured by the DOE under the FFELP, or certificates issued by Sallie Mae that are backed by pools of such GSLs, to be eligible collateral under section 935.9(a)(2)(ii). Although GSL holders may look directly to the DOE for payment on defaulted GSLs when a guarantee agency is unable to fulfill its obligation, GSL holders are not, under normal circumstances, the direct beneficiaries of the DOE reinsurance. For this reason, and because the state guarantee agencies against whom GSL holders have a direct claim are not part of the United States Government, GSLs originated under the FFELP normally may not be considered to be backed by a federal guarantee or insurance that is “for the direct benefit of the holder of the mortgage or loan,” as required under section 935.9(a)(2)(ii) of the regulations.

However, the member in question is in a unique position with respect to GSLs originated under the FFELP in that it is not only a holder of the GSLs, but is also the administrator of the state’s FFELP guarantee program. As such, the member is the direct beneficiary of the DOE reinsurance on every FFELP GSL it holds. Because the member in question has the contractual right, as administrator of the state’s FFELP GSL guarantee program, to receive insurance proceeds directly from the DOE, the staff of the Finance Board believes that the DOE insurance is, in this case, “for the direct benefit of the holder of the . . . loan” for purposes of section 935.9(a)(2)(ii).

Conclusion:

Where, as here, because of its status as administrator of a states’ FFELP GSL guarantee program a member benefits directly from the DOE reinsurance on the GSLs it holds, the FHLBank may accept the guaranteed portions of these GSLs as collateral for advances. It continues to be the Finance Board’s position that ordinarily GSLs originated under the FFELP, as well as Sallie Mae certificates backed by such GSLs, do not qualify as eligible “government securities” collateral under the Advances Regulation for the reasons stated above.

<p>A <u>Regulatory Interpretation</u> is applicable only to the transaction or activity proposed by the requestor and is subject to modification or rescission by action of the Board of Directors of the Finance Board. <i>See</i> 12 C.F.R. part 907.</p>
