Frequently Asked Questions
Collateral

FHLBank Boston

Here are some frequently asked questions we have received from members regarding collateral and on-site collateral reviews:

Q: Can deposit accounts at FHLBank Boston be included as qualified collateral?

A: Only funds placed in a collateral overnight deposit account can be included as qualified collateral. A collateral overnight deposit account pays the same rate as other overnight deposit accounts.

Q: Can capital stock be used as collateral?

A: No. Qualified collateral is limited to collateral that is listed in Appendix A of the Products and Solutions Guide. Per Federal Housing Finance Agency regulations, capital stock is excess collateral, and members cannot borrow against its value.

Q: How can I increase my borrowing capacity?

A: If your qualified collateral has increased, and you wish to increase your institution's borrowing capacity, the following steps must be taken for members that are assigned one of the three following collateral status groups:

(1) Category 1: Can submit a Qualified Collateral Report to FHLBank Boston to increase their overall borrowing capacity at any given point in time.

(2) Category 2: As stated in the Products and Solutions Guide, members pledging collateral to secure advances are required to update the collateral balances on at least a quarterly basis, or more often as FHLBank Boston may require. Members can update their balances at any time to reflect an increase in their qualified collateral.

(3) Category 3: As stated in the Products and Solutions Guide, members pledging collateral to secure advances are required to update the collateral balances on a quarterly basis at minimum, or more often as the FHLBank Boston may require. Members can also deliver additional collateral at any time to increase their borrowing capacity.

Q: What should I do if my qualified collateral decreases?

A: Per Federal Housing Finance Agency regulations and our Products and Solutions Guide, members are required to maintain at all times an amount of qualified collateral that satisfies the collateral-maintenance level established by FHLBank Boston. If the value of a member's pledged collateral declines, management must pledge additional collateral and/or substitute qualified collateral that is acceptable to FHLBank Boston in order to maintain sufficient qualifying collateral to secure advances.

For all members, any collateral deficiency identified must be corrected as soon as possible. Members should not wait for collateral deficiency notification from FHLBank Boston. (See Appendix A and Appendix

B of the Products and Solutions Guide, as well as the collateral section of the Products and Solutions Guide.)

Q: What is FHLBank Boston's position regarding overdrafts on a member's IDEAL Way account?

A: FHLBank Boston strongly discourages members from overdrawing their IDEAL Way account beyond the amount of their IDEAL Way line of credit. These overdrafts present potential liquidity and credit risks to FHLBank Boston. Therefore, each member should maintain an IDEAL Way line of credit that is sufficient to cover anticipated shortfalls in the collected balance of the member's IDEAL Way account to avoid such an overdraft. FHLBank Boston does not charge members a fee to establish or maintain an IDEAL Way line of credit.

The IDEAL Way line of credit is overdraft protection for your account. The Products and Solutions Guide notes that, "Members that have obtained an IDEAL Way line of credit may overdraw their IDEAL Way demand-deposit account and get an automatic IDEAL Way advance to cover the overdraft. FHLBank Boston typically approves an IDEAL Way line of credit equal to two percent of a member's assets." Members are required to pledge sufficient collateral to FHLBank Boston to secure their IDEAL Way line of credit at all times, including at the time that the line is established.

For additional information on establishing an IDEAL Way line of credit or increasing the size of your existing IDEAL Way line of credit, please contact the Member Funding Desk.

Q: What is the definition of a one- to four-family owner-occupied residential property?

A: In accordance with FHLBank Boston's definition for collateral purposes, a one- to four-family owner-occupied residential property is a dwelling that is the borrower's primary residence. Second homes, vacation homes, or other investor-type properties do not qualify under this collateral category. These nonowner one- to four-family residential loans must be individually listed with FHLBank Boston to receive credit.

Q: What kind of collateral may be included under the blanket lien of one- to four-family owner-occupied residential loans?

A: Only first mortgage loans secured by one- to four-family owner-occupied residential properties may be included in the blanket pledge of owner-occupied, one- to four-family loans. FHLBank Boston typically applies a 25% or 40% haircut to these loan types depending on FICO score.

Q: Can loans secured by second position Home Equity Lines of Credit (HELOCs) or Home Equity Loans (HELs) be included as qualified collateral?

A: In accordance with Appendix A of our Products and Solutions Guide, HELOCs and HELs are eligible under the "Other Real-Estate-Related Collateral category" and are subject to a haircut of 50% of the book value. This section allows members to pledge "other real-estate-related" collateral to FHLBank Boston in a discounted amount up to two times their GAAP capital.

HELOCs and HELs should be excluded from the blanket pledge of owner-occupied one- to four-family loans. These loans must be individually listed with FHLBank Boston to receive credit. Please contact the Collateral Department for information regarding FHLBank Boston's procedure for pledging HELOCs and HELs.

Q: Can loans secured by manufactured housing be included as qualified collateral?

A: In order for a manufactured home to be eligible, it must be (i) permanently affixed to the real estate owned by the borrower, and (ii) the member must provide FHLBank Boston with a legal opinion from its legal counsel that the manufactured home is classified as "Real Property" under applicable state law and considered by taxing authorities to be part of real estate.

Q: Can Commercial MBS be used as collateral?

A: Publicly offered commercial mortgage-backed securities (MBS) may be eligible under “Other Real Estate Related Collateral” guidelines. Commercial MBS are subject to review and acceptance by FHLBank Boston. Private placements, IO strips, and PO strips are typically not eligible collateral. Please contact the Collateral Department if you are interested in pledging commercial MBS as collateral, or if you have questions regarding whether a specific security is eligible as collateral.

Q: What is a member collateral review and why is it necessary?

A: A member collateral review is a periodic onsite review of the member's pledged one- to four- family loans by FHLBank Boston's collateral staff. The review generally includes an assessment of 50 randomly selected loans from the member's pledged one- to four-family portfolio. It is more extensive than the brief QCR review.

Its primary purpose is to determine the accuracy, eligibility, and credit-risk profile of the member's pledged one-to-four family loan collateral. Onsite collateral reviews help ensure that all extensions of credit from FHLBank Boston are adequately collateralized. They also provide members with valuable information regarding FHLBank Boston's pledging and eligibility guidelines to help them maximize their collateral value.

Q: What is a qualified collateral report verification review and why is it necessary?

A: A qualified collateral report verification is an initial, abbreviated onsite review of a Category-1 member's QCR reporting conducted by FHLBank Boston's collateral staff. The review generally includes an assessment of 100 randomly selected loans from the total QCR pledge.

The purpose of the QCR verification is twofold: First, we determine the accuracy of the member's QCR pledge of one- to four-family loans and ensure that all extensions of credit from FHLBank Boston are adequately collateralized. Second, we provide the member with information regarding FHLBank Boston's pledging and eligibility guidelines to better prepare them for a full member collateral review that will be scheduled after the QCR verification.

The QCR requires Category-1 members to separately identify pledged loans with FICO scores of less than 661 and nontraditional loans with deferred principal payments. The valuation for low FICO loans reported on the QCR is the standard 60%, and the valuation for nontraditional loans is the standard 65%. In contrast, the standard valuation for conventional loans is 75%.

Q: Can the QCR verification potentially affect a member's borrowing capacity?

A: Yes. If the QCR verification determines that the member's QCR pledge is overstated, FHLBank Boston will require the member to submit a new QCR to account for the inaccuracies identified during the verification. Correcting an overstatement of pledged collateral would reduce the member's borrowing capacity.

For example, if the verification determines that 9% of the sample has FICO scores less than 661, and the member is reporting zero in this category on the QCR, the member will be required to move 9% of the total one- to four-family owner-occupied pledge to the low FICO category and submit a new QCR. The low FICO loans will receive the lower (60%) valuation. The same holds true for incorrectly reported nontraditional loans in the QCR pledge.

Q: What is a collateral adjustment factor and how does it affect members' borrowing capacity?

A: A collateral adjustment factor is the discount FHLBank Boston applies to a member's loan pledge to adjust for ineligible loans found during the member collateral review. The adjustment percentage is derived from the collateral review exception rate, which is based on the number of ineligible loans found during a member collateral review.

Q: Do all member collateral reviews result in a collateral adjustment factor?

A: No. A collateral adjustment factor is only applied if the member collateral review determines that the member has overstated their pledged collateral by including ineligible loans.

Q: Can a member reduce its collateral adjustment factor after the member collateral review is completed?

A: Yes. The collateral review staff may determine that a reduced collateral adjustment factor is warranted provided the member can identify and remove ineligible loan types found during the member collateral review.

The member must provide supporting documentation and a signed letter stating that the ineligible loans have been removed from the pledge. In addition, Category-1 members will be required to submit a new QCR. Category-2 and Category-3 members will be required to provide a new loan listing.

A member may also request a follow-up member collateral review, which will require advance notice and be scheduled based on available resources.

Q: How does FHLBank Boston's residential loan credit-risk model used for valuation purposes work? Which loan attributes have the most impact on the model's assessment of the credit risk within a portfolio?

A: FHLBank Boston uses a third-party loss-estimation model to determine the credit risk associated with a member's residential loan collateral pledge. The model calculates potential losses, defaults, and loss severities (loss given default) within a portfolio based on the loan-level characteristics and economic factors, such as house-price movements.

The most important loan-level characteristics are FICO score; original and adjusted loan-to-value ratios; location and occupancy; loan type; loan purpose; documentation type; property type; debt-to-income ratio; appraisal type; asset verification; and payment history. The model adjusts loan-to-value ratio based on the most recent FHFA house-price index.

Q: How does the model affect a member's collateral valuation relative to the standard valuation(s)?

A: The credit-risk model is used to determine FHLBank Boston's standard (weighted average) valuations that are applied to one- to four-family owner-occupied residential loans pledged by Category-1 members that do not provide loan-level data for these pledged loans. The standard valuations are 75% for conventional loans, 65% for nontraditional loans, and 60% for low FICO score loans. The standard valuations are derived from the weighted average credit risk of loans for which FHLBank Boston has loan-level information, including data from member collateral reviews.

Category-2 and Category-3 members are required to provide a loan-level listing of their pledged loans. This information is run through the model. In cases where the model shows a higher level of credit risk in the pledge than FHLBank Boston's standard valuation, the difference reduces the valuation of the individual member's portfolio.

Q: If the credit-risk model indicates that the credit risk of a member's pledged loans is less than the standard, will the member's valuation be increased?

A: Yes. Category-1 members that choose to provide a loan-level listing of their pledged loans may receive a higher valuation than the standard valuations for one-to-four family owner-occupied loans.

Q: Is a collateral adjustment factor applied at the conclusion of a QCR verification review?

A: Generally, no. In most cases, there is no collateral adjustment factor applied after a QCR verification. However, a substantial overstatement of pledged collateral could require some sort of collateral adjustment factor until FHLBank Boston's staff can return for a follow-up review.

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Q: How can a member assure more accurate reporting of its low FICO score loans on the QCR?

A: A member generally has three options:

1. If available, utilize FICO scores from internal data systems.
2. If currently unavailable, perform a scrub of the pledged loan credit files to collect and electronically store FICO scores.
3. Obtain soft hit or refreshed FICO scores electronically from any of the major credit bureaus, and load into its servicing system.

Q: What will the FHLBank Boston review staff need while they are onsite?

A: The collateral staff will need workspace sufficient to accommodate a laptop computer with access to an electrical power source, adequate workspace in which to perform the review, and immediate access to all requested loan files, reports, etc. All required loan files should be pulled and ready for review upon the collateral staff's arrival. The majority of information for the loan file review will be contained in the credit and collateral files. Additional items may be requested as the need arises.