

Collateral – Municipal Securities Frequently Asked Questions



Municipal securities that meet the criteria outlined in the Products and Solutions Guide will be accepted for collateral. For many members, this will be an excellent way to increase borrowing capacity and/or to better manage investment portfolios. Please see the complete list of eligibility criteria and applicable haircuts in the Guide.

The eligibility guidelines state that “proceeds of the security have been or will be used to finance the acquisition, development or improvement of real estate”. What does this mean?

Unlike U.S. Government and Agency securities, municipal securities fall under the “Other Real Estate Related Collateral” (ORERC) category of eligible collateral. By regulation, a mandatory element of the eligibility criteria is that proceeds of the security must have been or will have been used to finance the acquisition, development or improvement of real estate. Some examples of securities that may meet this requirement include:

- **Housing Revenue Bonds** of any type (common ones include multifamily housing for low- and moderate-income families, homes for first time homebuyers, and housing for the aged and veterans)
- **Utility Bonds** that involve financing the development or maintenance of electric power, gas, water, wastewater or solid waste systems
- **Transportation Bonds** to finance highways, turnpikes, airports, ports, bridges, tunnels, or mass transportation facilities (including rail/subway systems)
- **Public Safety Bonds** to finance construction or renovation of correctional facilities, fire department facilities, or other public safety facilities
- **Health Care Bonds** to finance the construction or renovation of hospitals, nursing homes, assisted living facilities, or other medical centers
- **School, College and University Bonds** to construct or finance improvements to real property (e.g., dormitories, libraries, academic buildings, etc.)

Do 100% of the bond proceeds need to have a real estate purpose as described above in order for the security to be eligible collateral?

No. If only a portion of the security can be identified as having a real estate purpose as defined above, the security will be considered eligible, but only that portion of the security with a real estate nexus will be used as the basis (pre-haircut) for calculating lendable value. Each security’s prospectus will need to be reviewed to determine a real estate nexus. The “use of funds” or introduction section of the prospectus is usually a good place to review. For example, if 50% of the use of funds is real-estate related, then 50% of the CUSIP’s value would be used to determine borrowing capacity, before application of the appropriate haircut. Please note that if the bond is used to refund previous bonds (refunding bond), the real estate test will need to be applied to the underlying refunded bond to determine the portion of eligibility.

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How are the haircuts applied if only a portion of the security is real estate related?

The haircut will be applied to the portion of the security that is real estate related. For example, if a security with a market value of \$10,000,000 is identified to have a 70% real estate purpose, then the haircut would be applied to the \$7,000,000 portion.

What is the submission process for municipal securities?

Like all securities collateral, municipal securities must be delivered to the Bank's custodian or one of the approved third-party custodians. A list of municipal securities that members wish to pledge must be submitted to the Bank prior to delivery. Documentation substantiating the proportion of bond proceeds used to finance the acquisition, development or improvement of real estate (the "real estate nexus") must also be provided by the member for each pledged municipal security. The Bank has prepared an [excel template](#) and a [real estate percentage worksheet](#) for this purpose which is located on the Bank's website.

- Once the member determines which securities they wish to pledge, the member completes the template with the required information per security (CUSIP, security description, bond type, total issuance size, NRSRO ratings, original member cost, and the substantiated real estate portion of the security).
- The completed template is then submitted to collateral@fhlbboston.com
- The FHLB Collateral Department will review the submission and provide its determination.
- For those securities for which you receive the approval, submit the securities to your FHLB designated custodian in the same way as you would submit any other security. The custodian will update the values of the securities daily and provide them to the Bank to include it in the value of other pledged collateral to determine your total eligible collateral level.

Are both revenue and general obligation bonds eligible?

Yes, revenue and general obligation bond types are eligible, although the haircuts may vary.

What are the haircuts based on?

Haircuts are based on the type of bond (general obligation or revenue bond), rating (the lowest of at least two required ratings, with a minimum of A3/A-), and duration (based on the Bloomberg duration level).

Your guidelines state that bonds rated A3/A- cannot be on rating "negative watch". What about bonds with a negative outlook? Does this impact bonds rate higher than A3/A-?

Securities that are at the lowest level of eligible ratings (A3 or A-) are not eligible for collateral if the respective NRSRO has imposed a negative watch, or such other classification that implies a likelihood that a downgrade may be imminent. Such other classifications that would render a security ineligible include "Negative" (Moody's), "CreditWatch Negative" (S&P), "Watch Downgrade" (Kroll), or "Rating Watch Negative" (Fitch). Eligibility of securities rated higher than A3 or A- is not impacted by the NRSRO's outlook or watch status.