Office of Thrift Supervision
Department of the Treasury
Chief Counsel
1700 G Street, N.W., Washington, D.C. 20552 • (202) 906-6251

March 28, 1996

Mr. Ritchie W. Post
Vice President of Finance
and Administration
Neighborhood Housing Services
of America
1970 Broadway, Suite 470
Oakland, CA 94612

Re: Neighborhood Housing Services of America Securities

Dear Mr. Post:

This responds to your inquiry regarding whether and to what extent federal savings associations have authority to purchase securities backed by loan pools organized by Neighborhood Housing Services of America ("NHSA securities"). You also ask whether NHSA securities will be accorded capital treatment comparable to that provided for mortgage-related securities issued by the Federal National Mortgage Association ("FNMA") and the Federal Home Loan Mortgage Corporation ("FHLMC"), and will receive favorable consideration under the Community Reinvestment Act ("CRA").

In brief, we conclude that NHSA securities: (i) may be purchased by federal savings associations free from any percentage-of-assets limitations under section 5(c) of the Home Owners' Loan Act ("HOLA"), but subject to the loans-to-one-borrower ("LTOB") limits of HOLA § 5(u) to the extent described below; (ii) will be included in either the 50 percent or the 100 percent capital risk-weight category, depending on the type of loan backing the securities, but will not be eligible for the same 20 percent risk-weight category as FNMA and FHLMC securities; and (iii) may produce CRA benefits to the purchasing institution depending upon certain variables described below. In addition, we note that the Federal Deposit Insurance Corporation ("FDIC") has opined that NHSA securities are not "corporate debt securities" for purposes of § 28 of the Federal Deposit Insurance Act ("FDIA") and, therefore, are not required to meet rating requirements in order to be eligible for purchase by savings associations.

I. Background

NHSA is a privately-chartered nonprofit corporation that seeks to promote a secondary market for securities backed by low-interest loans made to low- and moderate-income individuals. In its role as a financial intermediary, NHSA makes or purchases low-interest loans, securitizes them, and sells them to "social investors."

NHSA is supported by the congressionally-chartered Neighborhood Reinvestment Corporation ("NRC"). The NRC provides NHSA with operating and capital grants. In addition, the NRC develops and provides technical assistance to NeighborWorks organizations, which are locally-controlled non-profit corporations. The mission of NeighborWorks organizations is to increase lending in low-and moderate-income neighborhoods and to improve housing and neighborhood conditions. The NHSA routinely purchases loans made by NeighborWorks organizations, thereby providing them with a method for replenishing their funds. The NHSA also purchases loans from financial institutions and originates some loans directly.

The NHSA creates customized loan pools for investors. Typically there is one investor per loan pool. The type of securities issued out of the NHSA pools can be grouped into five categories:

- **The Rehabilitation Loan Security**. This security is backed by a pool of housing rehabilitation loans secured by second or third liens on single family, 1-to-4 unit, owner-occupied properties.

- **The Mortgage Loan Security**. This security is backed by a pool of first mortgages or deeds of trust on owner-occupied, 1-to-4 unit single-family residences.

- **The Other Mortgage Loan Security**. This security is backed by a pool of first mortgages or deeds of trust on owner-occupied, 1-to-8 unit single family residences. Some of the underlying loans have loan-to-value ("LTV") ratios exceeding 80 percent; these loans are insured by private mortgage insurers to an LTV ratio of 80 percent.

- **The Multifamily Loan Security**. This security is backed by a pool of first mortgages or deeds of trust on nonprofit-owned or investor-owned mutual housing or rental units. The underlying loans are secured by first mortgages or deeds of trust on 5-to-40 unit properties.

- **The Housing Development Loan Security**. This security is backed by a pool of housing development loans secured by first liens on the underlying properties. These loans are short-term loans for interim-financing to cover acquisition, pre-development, and/or development activities on housing development projects.

NHSA enhances the creditworthiness of each of the foregoing securities. The type of credit enhancement depends on the historic creditworthiness and performance of the particular security and the underlying collateral pools. The credit enhancement may be in the form of one or more of the following, for the securities indicated:

- NHSA's pledge of full recourse. If a loan in the loan pool becomes severely delinquent, NHSA will repurchase the loan at par or replace the loan with a loan of equal or greater par value (Rehabilitation Loan Securities and Mortgage Loan Securities).

- NHSA's overcollateralization of the investment. The overcollateralization is in the form of cash or marketable securities guaranteed by the federal government (all NHSA securities).

- NHSA's purchase of insurance from third parties for collateral loans with an LTV ratio exceeding 80 percent (Other Mortgage Loan Securities).

- NHSA's guarantee of a cash flow coverage ratio of 100 percent of the amount due on loans in the pool (Rehabilitation Loan Securities, Mortgage Loan Securities, Other Mortgage Loan Securities and Multifamily Loan Securities) and/or NHSA's guarantee of the payments due on the securities (Rehabilitation Loan Securities and Mortgage Loan Securities).

A trustee that is not affiliated with NHSA holds on behalf of each investor all underlying loans, as well as the cash or government securities pledged by NHSA to support each loan pool. NHSA executes and delivers to the trustee a stand-by assignment of any cash or government securities pledged to collateralize the securities.

NHSA represents that there have been no delinquencies on any payments due on any security issued by an NHSA-organized loan pool in NHSA's 15-year history. NHSA also represents that the historic underlying 90-day delinquency rate on the loan products NHSA purchases and originates is 2 percent.

II. Discussion

A. Investment Limitations

Federal savings associations are authorized to invest in various categories of loans listed in HOLA § 5(c). The term "loans" is defined by HOLA § 5(c)(6)(B) in a manner that includes both whole loans and "interests in loans."[1] Accordingly, the Office of Thrift Supervision ("OTS") has typically used a pass-through analysis when assessing the authority of federal savings associations to invest in securities representing an interest in or backed by loans.[2] A federal savings association may generally invest in such securities to the same extent as it could invest directly in the underlying loans.

1. Mortgage Loan Securities, Other Mortgage Loan Securities, Multifamily Loan Securities, and Rehabilitation Loan Securities

Section 5(c)(1)(B) of the HOLA authorizes federal savings associations to make "[l]oans on the security of liens upon residential real property" subject to no percentage-of-assets limitations.[3] For purposes of HOLA § 5(c), the term "residential real property" is defined as:

> . . . leaseholds, homes (including condominiums and cooperatives . . .) and, combinations of homes or dwelling units and business property, involving only minor or incidental business use, or property to be improved by construction of such structures.[4]

Although the terms "home" and "dwelling unit" are not defined by statute, the OTS's implementing regulations indicate that collectively these terms encompass each of the

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[1] 12 U.S.C.A. § 1464(c)(6)(B) (West Supp. 1995).

[2] E.g., OTS Op. Chief Counsel, Dec. 19, 1991; and FHLBB Op. by Raiden, Oct. 9, 1984. See also HOLA § 5(c)(1)(R), which provides an alternative legal basis for acquisitions of mortgage-backed securities that meet certain statutory criteria, including rating requirements. A pass-through analysis is not required when an institution makes an investment in reliance on HOLA § 5(c)(1)(R). Because NHSA securities are not rated, however, a pass-through analysis is required here.

[3] 12 U.S.C.A. § 1464(c)(1)(B) (West Supp. 1995).

[4] 12 U.S.C.A. § 1464(c)(6)(A) (West Supp. 1995); see also 12 C.F.R. § 541.23 (1995) for a similar definition of residential real property.

types of residential structures standing behind the NHSA's Mortgage Loan Securities, Other Mortgage Loan Securities, Multifamily Loan Securities, and Rehabilitation Loan Securities -- i.e., 1-to-4 unit single family residences, 1-to-8 unit single family residences, and 5-to-40 unit apartments, condominiums, and cooperatives.[5] Accordingly, federal savings associations may invest in each of these types of securities pursuant to HOLA § 5(c)(1)(B) without regard to percentage-of-assets limitations.[6] Applicable LTOB limits are discussed below.

2. Housing Development Loan Securities

Under HOLA § 5(c)(6)(A), "residential real property" includes "property to be improved by construction" of residential structures. Unimproved or partially improved real estate is deemed to be property to be improved by construction of residential structures if the lender is able to demonstrate that: (i) the land is zoned exclusively for residential use; (ii) the land is zoned to permit residential use and legally enforceable covenants in the deed limit its use to structures designed primarily for dwelling; or (iii) the land is zoned to permit residential use and the borrower certifies that it intends to construct dwelling structures immediately on nearly all of the land.[7] In addition, property is considered "residential" even if it will include certain non-residential facilities, provided no more than 20 percent of the total appraised value of the property is attributable to non-residential use.[8]

Accordingly, federal savings associations will be permitted to invest, without percentage-of-assets limitations, in the NHSA's Housing Development Loan Securities provided the underlying loans are secured by properties satisfying the foregoing criteria. If the properties securing the loans do not satisfy the criteria, then the underlying loans will be classified as "nonresidential real property loans."[9] Under HOLA § 5(c)(2)(B)(i), federal savings associations generally may make nonresidential real property loans in an amount no greater than 400 percent of capital.[10]

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[5] 12 C.F.R. §§ 541.10 and 541.14 (1995).

[6] See also 12 U.S.C.A. § 1464(c)(1)(J) (West Supp. 1995) (which provides another basis for investments in the Rehabilitation Loan Securities).

[7] See OTS Op. Chief Counsel, Jan. 9, 1992; OTS Op. Chief Counsel, Nov. 6, 1991.

[8] 12 C.F.R. § 541.4 (1995).

[9] 12 U.S.C.A. § 1464(c)(2)(B)(i) (West Supp. 1995).

[10] Id.

B. LTOB Limitations

Section 5(u)(1) of the HOLA provides that the lending limits set forth in 12 U.S.C. § 84 for national banks apply to savings associations "in the same manner and to the same extent" as they apply to national banks.[11] Section 84 provides that, generally, a national bank's "loans and extensions of credit" to any one borrower may not exceed 15 percent of the bank's unimpaired capital and unimpaired surplus. The OTS's LTOB regulation expressly incorporates this 15 percent general limit,[12] and provides that the regulations of the Office of the Comptroller of the Currency ("OCC") implementing section 84 apply to savings associations.[13] Additionally, the preamble to the OTS's LTOB regulation states that the OTS will consider OCC interpretive opinions as "strong evidence of safe and sound banking practices" but will "regard these opinions as advisory only."[14]

The OCC applies two types of limitations on national bank purchases of securitized loans -- the legal lending limits and a prudential lending limit. In the OCC's view, when an institution purchases securitized loans from a seller that provides a guarantee, pledges recourse, or agrees to replace any loans that default (collectively, "recourse commitment"), "the transaction loses its character as a sale and is treated as a borrowing/lending transaction."[15] In other words, the purchaser is deemed to have made an extension of credit to the seller.[16] Under these circumstances, the legal lending limits are applied to the constructive extension of credit from the purchaser to the seller rather than to the loans standing behind the securities.

In the absence of a recourse commitment, the purchasing bank cannot be said to have made a constructive extension of credit to the seller. Accordingly, the lending limits would not apply directly as a matter of law to the transaction between the seller

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[11] 12 U.S.C.A. § 1464(u)(1) (West Supp. 1995).

[12] See 12 C.F.R. § 563.93(c)(1) (1995).

[13] The OCC's lending limit regulation is set forth at 12 C.F.R. Part 32, as amended at 60 Fed. Reg. 8526 (Feb. 15, 1995).

[14] 55 Fed. Reg. 28144, 28148 (July 10, 1990).

[15] OCC Interp. Letter 579 (March 24, 1992), OCC Interp. Letter (Feb. 5, 1993). See also 60 Fed. Reg. at 8533 (to be codified at 12 C.F.R. § 32.2(j)(1)(iv)).

[16] Id.

and purchaser.[17] Nevertheless, the OCC applies a prudential lending limit, based on the legal lending limit, on the maximum concentration of investment risk generally appropriate under principles of safety and soundness. Thus, the OCC has opined that, as a prudential matter, national banks generally may not invest more than 15 percent of their unimpaired capital and unimpaired surplus in securitized loans derived from a single source.[18] In the OCC's view, "the decision to apply the lending . . . limit to the seller . . . even where the seller does not retain explicit liability on the underlying loans is based on the significant reliance that the purchasing bank places on the entity that originates and services the pooled loans."[19]

Following the OCC's rationale regarding the legal and prudential lending limits, the OTS also generally restricts savings association investments in securitized loans purchased from a single source -- whether sold with or without recourse -- to 15 percent of the association's unimpaired capital and surplus.[20] However, in situations where a savings association reviews each of the loans underlying the securities pursuant to the association's customary underwriting standards for loan originations and documents that the underlying loans meet those standards without reference to any recourse commitment issued by the seller, the OTS permits an association to elect to apply the LTOB limits directly to the underlying loans, rather than to the securities. A savings association that documents that the underlying loans meet its customary loan origination standards in effect rebuts the customary presumption that it has placed significant reliance on the entity that organized or sold the loan pool and on any recourse commitment issued by that entity.

This elective alternative LTOB treatment of securitized loans is based on a recognition that the process of securitizing loans generally does not detract from their investment quality. In fact, loans are often rendered more investment worthy when pooled and securitized due to risk spreading, enhanced liquidity, overcollateralization, and any related recourse commitment from the seller. The LTOB limits, which are

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[17] OCC Interp. Letter 579.

[18] Id.

[19] Id. This restriction would not apply in instances where the issuer is either a government agency or a corporation directly or indirectly owned by the United States. Cf. 60 Fed. Reg. at 8536 (to be codified at 12 C.F.R. § 32.3(c)(4)).

[20] In these instances, the underlying loans are not subject to the LTOB limit, unless the OTS concludes that a savings association has purchased loans in securitized form for the express purpose of evading the LTOB limits. For example, a savings association that makes the maximum amount of loans permissible to a single borrower and then knowingly purchases securities backed by loans to that same borrower will be deemed to have violated the LTOB limits.

intended to promote safety and soundness, should not be applied in a manner that discourages investment in a form of loan instrument that is typically safer. It would be illogical to permit savings associations to purchase unlimited amounts of whole loans from a single loan originator, but then impose a cap of 15 percent of unimpaired capital and surplus on securitized loans purchased from that same originator notwithstanding the fact that the association has scrutinized the loan pool in the same manner as if it were directly acquiring whole loans.

In summary, therefore, the general rule is that the aggregate investment of a savings association in NHSA securities may not exceed 15 percent of the association's unimpaired capital and unimpaired surplus. However, an investing association may elect to apply the LTOB limits to the loans backing the NHSA securities, if the association documents that those loans satisfy the association's loan origination underwriting guidelines without reference to any recourse commitment issued by the seller.

C. Risk-Based Capital Treatment

NHSA requests that NHSA securities acquired by savings associations receive capital treatment comparable to that given to FNMA and FHLMC securities. Under the risk-based capital regulations, FNMA securities and FHLMC securities, along with mortgage-related securities that are rated in one of the two highest rating categories by at least one nationally recognized statistical rating organization, are considered "high quality mortgage-related securities" and are placed in the 20 percent risk-weight category.[21] Thus, for NHSA securities to be included in the 20 percent risk-weight category, at least one nationally recognized statistical rating organization would have to rate the securities in one of the two highest rating categories.

Since NHSA securities are not rated, they must be placed in either the 50 or the 100 percent risk-weight category depending on the type of loans standing behind each security.[22] The securities will be placed in the 50 percent risk-weight category if they are secured by "qualifying mortgage loans" or certain "qualifying multifamily mortgage loans." All other NHSA securities will be placed in the 100 percent risk-weight category.[23]

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[21] 12 C.F.R. §§ 567.1(k) and 567.6(a)(1)(ii)(H) (1995).

[22] See 12 C.F.R. § 567.6(a)(1)(iii) and (iv) (1995).

[23] See 12 C.F.R. § 567.6(a)(1)(iii)(C) (1995).

A "qualifying mortgage loan" is a 1-4 family residential first mortgage loan that satisfies certain prudential criteria, including a documented LTV ratio not exceeding 80 percent (at origination) unless insured to at least 80 percent by private mortgage insurance provided by an insurer that is approved by FNMA or FHLMC.[24] A non-qualifying mortgage loan with an LTV ratio above 80 percent may become a qualifying mortgage loan if it is paid down to an LTV ratio of less than 80 percent and meets all other requirements for qualifying mortgage loans.[25]

A "qualifying multifamily mortgage loan" is a loan secured by a first lien on multifamily residential properties consisting of five or more units that satisfies certain prudential standards specified in the capital regulations regarding, inter alia, amortization period, LTV ratio, debt servicing, and payment history.[26] Also, loans that were "qualifying multifamily mortgage loans" on March 18, 1994, under the then existing rule, are deemed "qualifying multifamily mortgage loans" under the current rule.[27] Securities backed by qualifying multifamily mortgage loans are includable in the 50 percent risk-weight category, provided the purchasing savings association is receiving timely principal and interest payments. Payments are generally deemed timely if they are not more than 30 days past due.[28]

Below we briefly indicate how the foregoing capital rules apply to each type of NHSA security.

Mortgage Loan Securities. To the extent Mortgage Loan Securities are backed by loans that satisfy the "qualifying mortgage loan" criteria (as appears to generally be the case), they will be includable in the 50 percent risk-weight category.

Rehabilitation Loan Securities. As discussed above, one requirement of a qualifying mortgage loan is that it be secured by a first lien. Rehabilitation Loans are generally secured by second and third liens and thus do not constitute qualifying mortgage loans. Accordingly, Rehabilitation Loan Securities will be includable in the 100 percent risk-weight category.

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[24] 12 C.F.R. § 567.1(u) (1995).

[25] Id.

[26] 12 C.F.R. § 567.1(v)(1) (1995).

[27] 12 C.F.R. § 567.1(v)(2) (1995).

[28] See 12 C.F.R. § 567.6(a)(1)(iii)(C) (1995).

Multifamily Loan Securities. Multifamily Loan Securities will be includable in the 50 percent risk-weight category if: (i) they are backed by loans that satisfy either the existing qualifying multifamily mortgage loan criteria set forth at 12 C.F.R. § 567.1(v)(1) or the grandfathering provision set forth at 12 C.F.R. § 567.1(v)(2); and (ii) timely interest and principal payments are being made on the securities. Multifamily Loan Securities not meeting these standards will be placed in the 100 percent risk-weight category.

Other Mortgage Loan Securities. Because Other Mortgage Loan Securities are backed by loans secured by 1-to-8 units, they must be analyzed under the standards for qualifying mortgage loans and qualifying multifamily mortgage loans. Other Mortgage Loan Securities that are backed exclusively by qualifying mortgage loans and qualifying multifamily mortgage loans will be placed in the 50 percent risk-weight category. Conversely, Other Mortgage Loan Securities backed by one or more non-qualifying mortgage loans or non-qualifying multifamily mortgage loans will be placed in the 100 percent risk-weight category, even if they also are backed by some qualifying mortgage loans or qualifying multifamily mortgage loans.

NHSA indicates that Other Mortgage Securities are sometimes backed by 1-to-4 unit loans that have an LTV ratio exceeding 80 percent. However, NHSA represents that these loans are all insured to the extent they exceed an 80 percent LTV ratio by private mortgage insurance. However, NHSA does not state whether the insurer is approved by FNMA or FHLMC. If the insurer is approved by FNMA or FHLMC, then the underlying 1-to-4 unit loans will be deemed qualifying mortgage loans.

Other Mortgage Loan Securities are also sometimes backed by loans on more than four units. Securities backed by these loans will be includable in the 50 percent risk-weight category if: (i) the loans satisfy either the existing qualifying multifamily mortgage loan criteria set forth at 12 C.F.R. § 567.1(v)(1) or the grandfathering provision set forth at 12 C.F.R. § 567.1(v)(2); and (ii) timely interest and principal payments are being made on the securities. Other Mortgage Loan Securities backed by loans on more-than-four unit properties that do not satisfy these criteria will be includable in the 100 percent risk-weight category. Because one of the criteria listed in 12 C.F.R. § 567.1(v)(1) is an LTV ratio of not more than 80 percent, Other Mortgage Loan Securities backed by loans with LTV ratios in excess of 80 percent and not satisfying the grandfathering provision will be includable in the 100 percent risk-weight category. Private mortgage insurance does not affect the capital treatment of multifamily loans with high LTV ratios.[29]

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[29] See 12 C.F.R. § 567.1(v)(1)(vi)(A) (1995).

Housing Development Loan Securities. Housing Development Loan Securities are backed by loans that appear to fall outside the definition of "qualifying mortgage loan" and "qualifying multifamily mortgage loan" and thus will be includable in the 100 percent risk-weight category.[30] In the unlikely event that all the loans in a Housing Development Loan pool happened to be qualifying, the related securities would, of course, be placed in the 50 percent risk-weight category.

C. CRA Treatment

The OTS regulations implementing the Community Reinvestment Act of 1977, as amended, were revised substantially in May 1995.[31] The revised regulations are being phased-in during a transition period.[32] Since the transition period runs from January 1, 1996 through July 1, 1997, the CRA treatment of the purchase of NHSA securities must be analyzed under both the CRA regulations being phased out and those being phased in.

1. CRA Regulations Being Phased Out

The CRA regulations that are being phased out provide that the OTS will evaluate a savings association's record in helping to meet the credit needs of its local community.[33] In assessing a savings association's CRA performance in its delineated community, OTS examiners consider the 12 "assessment factors" listed in the regulations.[34] Under two of the assessment factors, OTS examiners must evaluate:

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[30] 12 C.F.R. § 567.6(a)(1)(iv)(D) and (H) (1995).

[31] See 60 Fed. Reg. 22156 (May 4, 1995).

[32] Beginning January 1, 1996, the OTS will evaluate small savings associations, as defined below, under the new CRA rule. In addition, any savings association that files and obtains approval of a strategic plan for CRA compliance under the new rule will be evaluated under that plan once the association has been operating under an approved plan for at least one year. Large retail institutions and institutions that request and receive designations as wholesale or limited purpose institutions may elect to be evaluated under the new rule beginning January 1, 1996, provided the institution provides the required data. Beginning July 1, 1997, all institutions will be evaluated under the new CRA rule. See 60 Fed. Reg. at 22220 (to be codified at 12 C.F.R. § 563e.51(b)).

[33] See 12 C.F.R. § 563e.2 (1995).

[34] See 12 C.F.R. § 563e.7 (1995).

- The savings association's participation, including investments, in local community development and redevelopment projects or programs;[35] and

- Other factors that, in the [OTS's] judgment, reasonably bear upon the extent to which a savings association is helping to meet the credit needs of its entire community.[36]

In addition, as a matter of practice, OTS examiners consider loans and investments made outside a savings association's delineated community, provided: (i) the savings association would otherwise receive CRA consideration for making the investment but for its geographic location; and (ii) the savings association's overall CRA performance in its delineated community is at least at a "satisfactory" level.

Under these standards, the CRA impact of NHSA securities will vary depending on the location of the loans standing behind them. The purchase by a savings association of an NHSA security that is backed by loans in the savings association's delineated community will be favorably considered when analyzing an institution's CRA performance -- especially because all the underlying loans support housing for low- and moderate-income individuals. If a savings association's overall CRA performance in its delineated community is at least at a satisfactory level, the purchase of NHSA securities backed by loans benefitting areas outside the savings association's delineated community will also be favorably considered as part of the CRA review.

2. CRA Regulations Being Phased In

Under the recently-issued final CRA rule, the standards used to evaluate an institution's CRA performance will vary depending upon the type of institution. The new regulations establish performance tests for the following categories of institutions: (a) large, retail institutions; (b) small institutions; (c) wholesale or limited purpose institutions; and (d) institutions that elect to operate under an approved strategic plan.

The lending, investment, and service tests will be the primary methods by which the OTS will assess the CRA performance of large, retail savings associations, i.e., those with at least $250 million in assets on a stand alone basis or those affiliated with holding companies that have at least $1 billion in combined bank and thrift

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[35] 12 C.F.R. § 563e.7(h) (1995).

[36] 12 C.F.R. § 563e.7(l) (1995).

assets.[37] Under the investment test, examiners will consider any investment that: (i) is deemed a "qualified investment"; and (ii) benefits the savings association's assessment area(s) or "a broader statewide or regional area that includes the savings association's assessment area(s)."[38] "Qualified investment" is defined as an investment with a primary purpose of community development.[39] The preamble to the regulation provides examples of qualified investments including investments "in or to financial intermediaries that primarily lend or facilitate lending . . . to low- and moderate-income individuals in order to promote community development."[40] Thus, investments in NHSA securities will be treated as qualified investments. Accordingly, a savings association will receive positive CRA consideration under the investment test if the purchased NHSA securities are backed by loans that benefit the savings association's assessment area(s) or a broader statewide or regional area that encompasses the association's assessment area(s).

A small savings association[41] will have the option of being evaluated pursuant to a streamlined small savings association test.[42] Under this test, OTS examiners will, among other things, assess the reasonableness of a small institution's loan-to-deposit ratio. In assessing the reasonableness of this ratio, OTS examiners will consider other appropriate factors, such as the association's qualified investments. In addition, when a small savings association is considered for an "outstanding" CRA rating, examiners may consider, among other factors, the association's qualified investments.[43] Thus, when qualified investments are considered as part of the examiner's review of the reasonableness of an institution's loan-to-deposit ratio or in

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[37] See 60 Fed. Reg. at 22213 (to be codified at 12 C.F.R. § 563e.21(a)(1)).

[38] 60 Fed. Reg. at 22215 (to be codified at 12 C.F.R. § 563e.23(a)).

[39] 60 Fed. Reg. at 22213 (to be codified at 12 C.F.R. § 563e.12(r)).

[40] 60 Fed. Reg. at 22162, Fn. 3. The term "community development" is defined in the regulation to include affordable housing, community services targeted to low- or moderate-income individuals, and activities that revitalize or stabilize low- or moderate-income geographies. 60 Fed. Reg. at 22212 (to be codified at 12 C.F.R.§ 563e.12(g)).

[41] "Small savings association" is defined as an independent thrift with less than $250 million or an affiliate of a holding company with total banking and thrift assets of less than $1 billion. 60 Fed. Reg. at 22213 (to be codified at 12 C.F.R. § 563e.12(s)).

[42] See 60 Fed. Reg. at 22216 (to be codified at 12 C.F.R. § 563e.26).

[43] See 60 Fed. Reg. at 22223 (to be codified at 12 C.F.R. § 563e, App. A(d)(2)).

connection with a potential outstanding rating, favorable consideration may be given to investments in NHSA securities.[44]

Wholesale or limited purpose savings associations, regardless of their size, may elect to be assessed under a community development test that takes into consideration the savings association's community development lending, qualified investments, and community development services.[45] For these types of institutions, OTS examiners will consider qualified investments that: (i) benefit the savings association's assessment area(s) or a broader statewide or regional area that includes the association's assessment area(s), or (ii) benefit an area outside the association's assessment area(s) so long as the savings association has adequately addressed the needs of its assessment area(s).[46] Accordingly, a wholesale or limited purpose savings association will receive positive CRA consideration for NHSA securities backed by loans that benefit the savings association's assessment area(s) or a broader statewide or regional area that encompasses the association's assessment area(s). A wholesale or limited purpose savings association will also receive positive CRA consideration for NHSA securities backed by loans that benefit other areas so long as it has adequately addressed the needs of its assessment area(s).

Finally, all savings associations have the option of being evaluated pursuant to a pre-approved strategic plan.[47] Strategic plans must contain measurable goals that specify how the savings association will help meet the credit needs of each assessment area covered by the plan.[48] The CRA impact of NHSA securities held by a savings association operating under a strategic plan will depend on whether and to what extent investment in the securities is consistent with the strategic plan.

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[44] See 60 Fed. Reg. at 22216 (to be codified at 12 C.F.R. § 563e.26(a)(1)). Note that this provision does not impose express geographic limits on the activities that may be considered by the agencies when reviewing the reasonableness of a loan-to-deposit ratio. At this time, the agencies are discussing whether to consider only those activities made in the savings association's assessment area(s) or a broader statewide or regional area that encompasses the association's assessment area(s).

[45] See 60 Fed. Reg. at 22215 (to be codified at 12 C.F.R. § 563e.25(a)).

[46] See 60 Fed. Reg. at 22216 (to be codified at 12 C.F.R. § 563e.25(e)).

[47] See 60 Fed. Reg. at 22216 (to be codified at 12 C.F.R. § 563e.27).

[48] See 60 Fed. Reg. at 22216 (to be codified at 12 C.F.R. § 563e.27(f)).

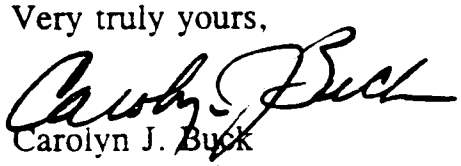
E. FDIA § 28 Restrictions on Corporate Debt Securities

Section 28 of the FDIA prohibits savings associations from acquiring or retaining any "corporate debt security not of investment grade," unless the security is issued or guaranteed by certain government-sponsored corporations.[49] Since NHSA securities are not rated or government issued or guaranteed, if the FDIC, which has jurisdiction to interpret § 28, classified NHSA securities as corporate debt securities, savings associations would be prohibited from purchasing NHSA securities. However, the FDIC recently opined that NHSA securities will not be considered corporate debt securities for purposes of FDIA § 28.[50] Accordingly, savings associations are not prohibited from purchasing NHSA securities by FDIA § 28.

In reaching the foregoing conclusions, we have relied upon the specific factual representations contained in the materials you submitted to us and made in conversations with OTS staff, as summarized herein. Our conclusions depend upon the accuracy and completeness of those factual representations. Any material change in facts or circumstances from those described herein could result in different conclusions.

If you have any questions regarding these matters, please feel free to contact John Flannery, Attorney, at (202) 906-7293.

Very truly yours,



Carolyn J. Buck
Chief Counsel

Enclosure

cc: All Regional Directors
All Regional Counsel

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[49] 12 U.S.C.A. § 1831e(d) (West 1989 & Supp. 1995).

[50] See FDIC Interp. Letter (Sept. 18, 1995) (copy enclosed).