



Highlights of [GAO-10-792](#), a report to the Chairman, Subcommittee on Capital Markets, Insurance, and Government Sponsored Enterprises, Committee on Financial Services, House of Representatives

Why GAO Did This Study

The Federal Home Loan Bank System is a government-sponsored enterprise comprising 12 regionally-based Federal Home Loan Banks (FHLBank), the primary mission of which is to support housing finance and community and economic development. Each FHLBank makes loans (advances) to member financial institutions in its district, such as banks, which traditionally are secured by single-family mortgages. In 1999, the Gramm-Leach-Bliley Act (GLBA) authorized FHLBanks to accept alternative forms of collateral, such as agricultural and small business loans, from small members. GAO was asked to assess (1) factors that may limit the use of alternative collateral; and (2) selected aspects of the Federal Housing Finance Agency's, (FHFA) related regulatory oversight practices.

GAO reviewed FHLBank policies and FHFA documentation; and interviewed FHLBank and FHFA officials, and a nongeneralizable random sample of 30 small lenders likely to have significant levels of agricultural or small business loans in their portfolios.

What GAO Recommends

FHFA should revise its examination guidelines to include periodic analysis of alternative collateral, and enforce its regulation pertaining to quantitative goals for products related to agricultural and small business lending. FHFA agreed with these recommendations.

[View GAO-10-792](#) or [key components](#). For more information, contact William Shear at (202) 512-8678 or shearw@gao.gov.

FEDERAL HOUSING FINANCE AGENCY

Oversight of the Federal Home Loan Banks' Agricultural and Small Business Collateral Policies Could Be Improved

What GAO Found

FHLBank and FHFA officials cited several factors to help explain why alternative collateral represents about 1 percent of all collateral that is used to secure advances. These factors include a potential lack of interest by small lenders in pledging such collateral to secure advances or the view that many such lenders have sufficient levels of single-family mortgage collateral. Officials from two FHLBanks said their institutions do not accept alternative collateral at all, at least in part for these reasons. Further, FHLBank officials said alternative collateral can be more difficult to evaluate than single-family mortgages and, therefore, may present greater financial risks. To mitigate these risks, the 10 FHLBanks that accept alternative collateral generally apply higher discounts, or haircuts, to it than any other form of collateral, which may limit its use (see table). For example, an FHLBank with a haircut of 80 percent on alternative collateral generally would allow a member to obtain an advance worth 20 percent of the collateral's value. While GAO's interviews with 30 small lenders likely to have significant alternative collateral on their books found that they generally valued their relationships with their local FHLBanks, officials from half said the large haircuts on alternative collateral or other policies limited the collateral's appeal.

FHFA's oversight of FHLBank alternative collateral policies and practices has been limited. For example, FHFA guidance does not direct its examiners to assess the FHLBanks' alternative collateral policies. As a result, the FHLBanks have wide discretion to either not accept alternative collateral or apply relatively large haircuts to it. While the FHLBanks may view these policies as necessary to mitigate potential risks, 9 of the 12 FHLBanks did not provide documentation to GAO to substantiate such policies. Further, the documentation provided by three FHLBanks suggests that, in some cases, haircuts applied to alternative collateral may be too large. Also, the majority of the FHLBanks have not developed quantitative goals for products related to agricultural and small business lending, such as alternative collateral, as required by FHFA regulations. FHFA officials said that alternative collateral has not been a focus of the agency's oversight efforts because it does not represent a significant safety and soundness concern. However, in the absence of more proactive FHFA oversight from a mission standpoint, the appropriateness of FHLBank alternative collateral policies is not clear.

Range of FHLBank Haircuts Applied to Various Collateral Types

| FHLBank district | Alternative collateral haircuts | | | Single-family mortgages | Commercial real estate mortgages |
|------------------|---------------------------------|------------|--------------------|-------------------------|----------------------------------|
| | Small business | Small farm | Small agribusiness | | |
| Ranges | 40-80% | 40-80% | 40-80% | 7-44% | 40-67% |

Source: GAO analysis of FHLBank collateral policies.