

BL-061
Rural Housing Mortgage-Backed Securities

November 12, 2009

To: Chairman, Board of Directors
Chief Executive Officer
All Farm Credit System Banks

From: Leland A. Strom
Chairman and Chief Executive Officer

Subject: Rural Housing Mortgage-Backed Securities

The Farm Credit Administration (FCA) authorizes Farm Credit System (System) banks to hold rural housing mortgage-backed securities (RHMS) as mission-related investments under § 615.5140(e) of FCA's regulations, subject to the conditions specified below.

System associations may originate rural home loans (RHLs) that meet certain criteria under § 613.3030 of FCA's regulations.¹ Under § 613.3030(d)(1), a System bank is authorized to purchase and hold RHLs in an amount not to exceed 15 percent of its total outstanding loans at any one time. Under existing authorities, a System bank may opt to hold the RHLs until maturity. In addition, if the RHLs qualify, a System bank has the authority to take one of three other actions with respect to the RHLs. First, the System bank can have its RHLs securitized into RHMS that are guaranteed by Farmer Mac for the purposes of managing credit and interest rate risk and furthering its mission of financing agriculture, up to 100 percent of its total outstanding loans, pursuant to § 615.5174.² Second, a System bank can have its RHLs securitized into RHMS that are guaranteed by Ginnie Mae,³ Fannie Mae, or Freddie Mac as eligible investments pursuant to § 615.5140.⁴ Third, the System bank can enter into a long-term standby commitment to purchase (standby agreement) with one of the government-sponsored enterprises (GSEs). Under a standby agreement, a System bank can opt to (1) sell the RHLs to the GSE for cash or (2) have its RHLs securitized into RHMS that are guaranteed by the GSE.

Under §§ 615.5132 and 615.5140(a)(5) of FCA's regulations, a System bank may hold any government- or GSE-guaranteed RHMS for the purpose of complying with its liquidity reserve requirement, managing surplus short-term funds, and managing interest rate risk. The FCA is issuing this booklet to authorize System banks to also hold RHMS as mission-related investments under § 615.5140(e) for the purpose of addressing liquidity needs in the rural housing mortgage market, subject to the following conditions:⁵

- 1) RHMS must meet the definition of "mortgage securities" as defined in § 615.5131 of FCA's regulations.
- 2) The RHLs underlying RHMS must be eligible rural home loans originated by System associations under § 613.3030.

- 3) Investments in RHMS must be fully guaranteed by the United States (e.g., Ginnie Mae), Fannie Mae, or Freddie Mac with terms of no more than 30 years.
- 4) The aggregate amount of RHMS that a System bank can hold at any one time may not exceed 15 percent of the bank's total outstanding loans. All RHLs made by System associations that have been purchased by the System bank and remain on its books must also be included in this limit. This limit is independent of any current regulatory portfolio limitations for investments in mortgage securities under §§ 615.5132, 615.5140(a)(5), and 615.5174 of FCA's regulations, or other mission-related investment limit.
- 5) RHMS must be maintained in a portfolio separate from other investments so that they are readily identifiable.
- 6) RHMS must be prudently managed in accordance with the System bank's investment policies.
- 7) RHMS must be reported in accordance with generally accepted accounting principles.
- 8) RHMS must be excluded from the liquidity reserve requirement under § 615.5134 of FCA's regulations.

In implementing this authority to hold RHMS as mission-related investments, we expect each System bank to follow prudent risk management practices such as establishing appropriate board approved exposure limits to the housing GSEs and the housing sector. We also expect each System bank to monitor these exposures through its ongoing credit oversight program. If you have any questions regarding this booklet, please contact Andrew D. Jacob, Director, Office of Regulatory Policy, at 703-883-4356 or via email at jacoba@fca.gov or Laurie Rea, Associate Director, Office of Regulatory Policy, at 703-883-4232 or via email at real@fca.gov.

¹Section 613.3030 implements the rural housing financing provisions at sections 1.11(b) and 2.4(b) of the Farm Credit Act of 1971, as amended.

²RHMS guaranteed by Farmer Mac are not within the scope of this booklet.

³Ginnie Mae (Government National Mortgage Association) is a wholly owned U.S. government corporation.

⁴Fannie Mae (Federal National Mortgage Association) and Freddie Mac (Federal Home Loan Mortgage Corporation) are housing GSEs.

⁵All references to RHMS in these conditions refer to RMHS that are backed by rural home loans originated by System associations and are held as mission-related investments.