FHLBBoston

Onsite Collateral Review Procedures for Owner Occupied, 1-4 Family Loans

This memo highlights the major processes employed by the Federal Home Loan Bank (the Bank) collateral review staff during an owner occupied, 1-4 family collateral review. Please read through this document carefully as it is intended to answer many frequently asked questions, and to give you a better idea of what to expect during and after the collateral review. This information should also facilitate improved communication while the Bank Analysts are on-site.

Step One: Loan Selection

In order to select loans for review, the Bank staff obtains recent loan listing data for the owner occupied, 1-4 family pledge from the member. Members in Category 1 collateral status are required to submit this loan listing data prior to the review; it is typically submitted at least one month prior to the review. Members in Category 2 and 3 collateral status already list the necessary loan information with the Bank. Collateral review staff then selects a sample of loans for review, typically a random sample. If the member pledges 100 loans or less in the owner occupied, 1-4 family pledge, the Bank Analysts will typically review the entire pledge. The list of loans selected for review is then placed on the secure website for the member to access and prepare the loan files for review.

Step Two: The Review Process

During the review, Analysts evaluate the underwriting of each loan file. The member is asked to have all relevant documents available for review. All loans are analyzed in order to determine whether the member is in compliance with the collateral requirements of the Bank's "Agreement for Advances, Collateral Pledge and Security Agreement" and current Products and Solutions Guide. Please note that loans originated on or after July 10, 2007 are also reviewed for compliance with the Interagency Guidance for Subprime and Nontraditional Mortgage Product Risks. In addition to the underwriting and eligibility review, loan listing information is verified for accuracy for the loans under review. Any data accuracy issues identified will be compiled during the review and will be available to the member once the review results are completed.

Common reasons for ineligible loans include the following:

- Loans secured by investment properties or second homes;
- Loans made to directors, officers, employees, attorneys, or agents of the member institution or the Bank;
- Loans secured by ineligible property types (e.g. mixed use properties, commercial properties, mobile homes, fair condition properties);
- Loans with chronic delinquency and/or substandard credit;
- Loans secured by liens in second position; and
- Collateral dependent loans.

In addition to the loan review process above, a reconciliation of the pledged values is performed to determine the accuracy of collateral reporting, including an analysis of lower FICO score (≤660 FICO) and nontraditional pledge totals. If the reconciliation shows that these loans are not being reported accurately, the proportion of these loans found in the sample reviewed may need to be extrapolated across the entire pledge. For example, if total lower FICO score collateral is reported as zero on the QCR, but the sample shows nine percent lower FICO score loans then the member must transfer nine percent of their total 1-4 family owner occupied pledge into the lower FICO score category and resubmit their most recent QCR. This percentage of lower FICO score loans will receive the lower advance rate until more accurate totals can be provided by the member.

Please note that the above items represent the most common issues that may require adjustments to your collateral. Additional information regarding eligible collateral can be found in Appendix A of the Products and Solutions Guide at www.fhlbboston.com in the Member Resource Center tab.

Step Three: Applying an Exception Rate

Once the Bank staff has determined the number of ineligible loans in the pledge from the random sample, the exception rate or collateral adjustment factor (CAF) is calculated to account for similar ineligible loans in the total pledge. For example, using a random sample of 50 loans, if Analysts find two ineligible loans, the formula is as follows:

- 2 ineligible loans divided by 50 (2/50) or 4%

Once the exception rate is calculated, it is applied to the member's owner occupied, 1-4 family pledged collateral as a CAF. This remains in place until another review is performed that results in a different exception rate.

All ineligible loans identified during the review must be removed from the member's pledge going forward. Members that have their entire pledge reviewed are generally not subject to a CAF.

Step Four: Additional Risk Analysis

Once the review has been completed, the eligible loans from the random sample (or all eligible loans from the review) are run through an internal credit risk model that evaluates whether the current standard discount (haircut) is adequate to mitigate the credit risk in the pledge. If the model shows that the standard discount does not adequately account for the risk in the portfolio, the discount will be increased. The amount of the increase is determined by the relative credit risk of the pledged loans.

Step Five: Results Reported

Once the review has been completed and signed off by the Collateral Review Manager, a password protected Review Findings Report is sent to the member via e-mail. If it is necessary for the member to resubmit the QCR, a new QCR will be placed on the Bank's secure website for the member to upload. The QCR must be resubmitted by the member within 14 business days of the completion of the review. The collateral discounts and/or CAF will be applied to the member's owner occupied, 1-4 family pledge by the Bank no later than 15 business days after the completion of the review.