



COLLATERAL VERIFICATIONS

Nov. 5, 2020 | 10 a.m. CT

To maximize your ability to hear the webinar, we're muting all participants. Please keep your line muted.

ABOUT THE PRESENTERS



ELAINE SHUMAKER | AVP, Financial Services Manager

Elaine joined FHLBank in 1987. She held various positions until 1999 when she was promoted to Safekeeping Manager. She now oversees Financial Services, which includes safekeeping and collateral operations.



KYLIE MERGEN | VP, Director of Financial Services

Kylie joined FHLBank in 2007. She was a Collateral Review Analyst until September 2008 when she became the Collateral Review Manager. In January of 2017, Kylie was promoted to the Director of Financial Services and oversees the safekeeping and collateral operations as well as the collateral review and verification process.



WEBINAR GOALS

GOALS

- Explain why FHLBank performs Collateral Verifications
- Identify types of Collateral Verifications
- Enhance knowledge of Collateral Verification process
- Discuss best practices to “pass” a Collateral Verification
- Provide resources for ongoing collateral information



WHY FHLBANK PERFORMS COLLATERAL VERIFICATIONS

Prudent credit practice

- Validate collateral pledged
- Monitor member loan policies and pledging practices

Regulatory requirement

- Collateral eligibility
 - Perfect security interest
 - Readily ascertainable value
 - Reliably discounted
 - Liquidate in due course

To protect FHLBank and its stockholders

- Collateral Assets
 - Properly classified
 - In compliance with FHLBank's underwriting requirements



KEY TO COLLATERAL REPORTING

Preparation is KEY!

- Individuals completing and approving QCD form must be knowledgeable of the institution's assets and FHLBank's Policies for pledging collateral
- Review FHLBank's Policies, specifically the Schedule of Eligible Collateral guidelines
- Identify and retain critical reports that categorize the eligible collateral assets
- Verify that all ineligible loans have been removed



TYPES OF COLLATERAL VERIFICATIONS

QCD Desk Audits

- Performed electronically once member regulatory data is received

Onsite Collateral Verifications

- Performed at member's location by FHLBank staff



QCD DESK AUDITS

Selection criteria

- All blanket pledge members reporting loans via the QCD form

Purpose

- Reasonability test – comparison of loans pledged on QCD form to loans reported on the member's regulatory reports
- Validate member's compliance in pledging restricted assets
- Verify current subordinations (if any)



QCD DESK AUDITS

Frequency

- Quarterly

Process

- Comparison of assets reported on the QCD form vs. Call Report numbers

Remediation

- If exceptions are noted, member contacted by email
- Resolution required from member



ONSITE COLLATERAL VERIFICATIONS

Selection criteria

- Risk based approach, taking into consideration the member's:
 - Outstanding FHLBank credit obligations
 - Financial performance
 - Approval/renewal of special collateral arrangements
 - Overall collateral coverage ratios
 - Changes in collateral reporting method (i.e., delivery to QCD reporting)
 - Results from a previous collateral verification



ONSITE COLLATERAL VERIFICATIONS

Purpose

- Validate the existence of the asset
- Validate asset classification
- Validate accuracy of data provided on the QCD Loan Support template (data integrity)
- Validate the eligibility of the asset (loan file review to determine if loan meets established underwriting guidelines for the specific asset type)



ONSITE COLLATERAL VERIFICATIONS

Frequency of the Reviews

- Annual
- Tri-annual

Criteria

- Top 20
- Annual – Average CO/Total Unsubordinated Assets \geq 15%
- Annual – Average CO/Total Unsubordinated Assets \geq 5% and a significant member
- Tri-Annual – Average CO/Total Unsubordinated Assets \geq 5% and have not had a review in the previous 24 months
- Manual



ONSITE COLLATERAL VERIFICATIONS

Process

- Annual Selection
 - 1st Business day in November
- Notification
 - Members are notified by email
- Initial contact
 - Brief phone conversation with a Collateral Review Officer
 - Determine amicable date for onsite visit
 - Establish main contact
- Provide formal engagement letter
 - Solidify the agreed upon date and provide expectations for the onsite collateral review



ONSITE COLLATERAL VERIFICATIONS

Process

- Request documentation
 - QCD Loan Support template
 - CV Questionnaire
 - Loan delinquency report
 - Watch list
 - Director/officer/employee loan list
 - List of all participation loans
 - List of subordinated loans (if applicable)
 - Loan Policy
 - Quality Control or Credit Review Policy
 - Member's internal procedures for completing QCD form
 - Servicing/Custodian agreements (if applicable)



ONSITE COLLATERAL VERIFICATIONS

Process

- Sample Selection
 - Depends on number of loans pledged
 - > 500 – use statistical sampling method (90% confidence, 5% precision, 5% error)
 - < 500 – use 10% of loans pledged
 - Based on the distribution of the asset categories utilized
 - Core Sample (20 minimum, 102 maximum)
 - Additional Selection: Largest 5 loans pledged
 - List of loans to be reviewed provided to you prior to arriving onsite



ONSITE COLLATERAL VERIFICATIONS

Process

- Complete review on-site
 - Initial meeting with member's management, if needed
 - Review each sampled loan for eligibility
 - Note
 - Mortgage
 - Title
 - Appraisal
 - Credit Review
 - Review additional requested materials (i.e., loan policy, reports, etc.)



LOAN REVIEW – WHAT ARE WE LOOKING FOR?

Does the loan meet our eligibility criteria?

- Original note (and any modifications, change in terms, renewals, etc.) with appropriate terms
- Security of the note
 - Mortgage/Deed of Trust
 - Security Agreement
- Lien position
 - Title policy or UCC search
- Loan to Value
 - Appraisal or valuation



LOAN REVIEW – WHAT ARE WE LOOKING FOR?

Does the loan meet our eligibility criteria?

- Credit review
 - FICO and Debt to Income
 - Income/Employment Verification
 - Debt Service Coverage Ratio
- Supplemental information/documentation, if needed
 - Phase 1
 - Annual Financial Statement
 - PACE validation
- Technical exceptions
 - Security Instrument Issues
 - Rate charged differs from note



LOAN REVIEW – WHAT ARE WE LOOKING FOR?

Does the loan meet our eligibility criteria?

- Additional qualifications
 - Past due
 - Wholly owned (participation information)
 - Classified
 - Director/Officer/Employee
 - Servicer/Custodian information
 - Consistency throughout the file



ONSITE COLLATERAL VERIFICATIONS

Process

- Collateral Verification Findings
 - Contact with management throughout the review
 - Work with management or assigned staff while onsite
 - Provide daily update on progress and exceptions found
 - Exception threshold
 - Exception percentage is based on the number of exceptions identified divided by number of loans in Core sample
 - Must maintain a 90% confidence level
 - Collateral Verification results provided in exit conference
 - Officer will share findings and cost for review

- Collateral Opportunities
 - Work with the Officer to identify any potential eligible collateral not currently pledged



ONSITE COLLATERAL VERIFICATIONS

Process

- Upon return to FHLBank
 - Officer compiles and finalizes results
 - Report provided to management for review and approval
 - Final letter provided to member
 - Collateral review fee assessed at end of month following finalization



ONSITE COLLATERAL VERIFICATIONS

Possible Collateral Actions

- No action/response required
- Written response required from member
- Amended QCD form required
- Discount of collateral
- Follow up Onsite Collateral Verification
- Listing requirement
- Delivery of collateral
- Other actions



COMMON EXCEPTIONS IDENTIFIED

Frequently encountered issues:

- Missing documentation
- Phase 1 environmental reports not provided or available when required
- Subprime/predatory/non-traditional lending characteristics
- Title evidence/final title
- Loans not fully secured by eligible collateral
- Unpaid principal balance exceeding the Mortgage/Deed of Trust amount
- Revolving lines of credit or loans not fully advanced
- Exceeding interest only term limitations
- Matured loans



BIGGEST TOPIC OF DISCUSSION

“Wet” signature

- Electronic signatures vs scanned documents vs eNotes

WHAT AN eNOTE IS:

A note executed electronically and stored in an eVault that meets the requirements for an eNote

WHAT AN eNOTE IS NOT:

A scanned image of a wet ink signature or a note with an electronic signature that is not stored in an eVault and doesn't meet eNote requirements

- Current Project Status
- <https://www.fhlbtopeka.com/products/collateral/enotes>



Q&A

ACCURATE REPORTING OF ELIGIBLE COLLATERAL

- Establishes borrowing capacity at FHLBank
- Maximizes liquidity by allowing non-liquid assets to be used as collateral
- Reduces expenses associated with collateral verifications



EDUCATIONAL OPPORTUNITIES

Upcoming Webinars

- **2020 Virtual Regional Meeting with Esther George**
 - Nov. 13, 2020 – 9 to 11 a.m.

- **Advance Your Thinking Webinar Series**
 - Analyzing Your Liquidity – Nov. 17 or 18, 2020
 - Identifying Hidden Collateral – Dec. 16, 2020



EDUCATIONAL OPPORTUNITIES

Annual Management Conference

- Olathe, Kansas | April 21-23, 2021

Regional Meetings

- August through October in Colorado, Kansas, Nebraska and Oklahoma
 - August 30, 2021 – Lincoln, NE
 - September 27, 2021 – Lawrence, KS
 - October 14, 2021 – Oklahoma City, OK
 - Colorado meeting date is being finalized

Collateral Review Contact

- One-on-one guidance



HELPFUL RESOURCES



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FHLBank Topeka Website | www.fhlbtopeka.com

Collateral Landing Page | www.fhlbtopeka.com/Products/collateral

Member Products & Services Guide | www.fhlbtopeka.com/mpsg

