

Federal Housing Finance Board

Memorandum

May 17, 1991

TO: Philip L. Conover
Director, District Banks Directorate

FROM: Beth L. Climo
General Counsel

SUBJECT: Interpretation of "Prior Year" in the Shortfall Formula
for REFCorp Interest Payments

BACKGROUND:

By memorandum dated April 8, 1991, you requested our interpretation of section 21b(f)(2)(C) of the Federal Home Loan Bank Act of 1932, as amended, (Bank Act), 12 U.S.C.A. § 1441b(f)(2)(C) (West Supp. 1990) which requires the Federal Home Loan Banks (FHLBanks) to pay interest on the obligations of the Resolution Funding Corporation (REFCorp).¹ In particular, you requested our interpretation of the term "prior year" as that term is used in the formula established by section 21b(f)(2)(C)(ii)(I) and (II) for computing each FHLBank's share of the contribution to the REFCorp interest cost when there is an earnings shortfall requiring the FHLBanks to allocate amounts owed to REFCorp in excess of twenty percent of net earnings. The issue has arisen because of disagreement among the FHLBanks over the assessment procedures for collection of the FHLBanks' contributions to REFCorp's quarterly interest payments that were provisionally approved by the Oversight Board of the Resolution Trust Corporation (Oversight Board) by letter of April 9, 1991.

1. In addition to your memorandum, we have reviewed *inter alia*, a March 4, 1991 memorandum from K. Diane Boyle, REFCorp Secretary/Treasurer, to the REFCorp directorate, concerning approval of interest assessment procedures; a March 6, 1991 memorandum from Austin C. Dowling, president of REFCorp, to Peter Monroe, President of the Oversight Board, concerning the interest assessment procedures; a March 27, 1991 letter from Paul D. Hill, Acting President, FHLBank-San Francisco, to J. Stephen Britt; an April 9, 1991 letter from Peter H. Monroe to Brian D. Dittenhafer, Chairman of the REFCorp directorate, provisionally approving the interest assessment procedures; and an April 15, 1991 opinion memorandum from Alan N. Waxman to the REFCorp directorate.

ISSUE:

Whether the phrase "prior year" in the shortfall formula should be interpreted to mean the preceding calendar year or the preceding thirteen-month period on a rolling basis?

DISCUSSION:

Section 21b(f)(2)(C) provides that the FHLBanks are to contribute \$300 million, in the aggregate, less Financing Corporation (FICO) and REFCorp defeasance payments, to pay the interest on REFCorp bonds² each "calendar year." Paragraph (C) provides a two-part formula specifying each FHLBank's share of the interest contribution. First, each FHLBank is to pay an "equal percentage of its earnings for the year for which such amount is required to be paid, up to a maximum of 20 percent of net earnings." Section 21b(f)(2)(C)(i).

Second, in instances where there is an interest payment shortfall (i.e., "...the aggregate amount required to be paid . . . exceeds 20 percent of the aggregate net earnings of the Banks for such year . . ."Section 21b(f)(2)(c)(ii)), each FHLBank's share of the excess is calculated by dividing:

(I) the average month-end level in the prior year of advances outstanding by such Bank to [SAW] members; by

(II) the average month-end level in the prior year of advances outstanding by all such Banks to [SAIF] members. Section 21b(f)(2)(C)(ii)(I) and (II).

A question has been raised concerning the appropriate interpretation of the phrase "prior year" as used in section 21b(f)(2)(C)(ii)(I) and (II). The interest assessment procedures proposed by the REFCorp directorate are based on a "rolling-year" concept and interpret "prior year" to mean the most recent thirteen-month period. For example, the portion of the April 1991 assessment based on SAIF advances would be calculated using outstanding month-end balances for the period March 1990 through March 1991.

2. The FHLBanks are to make such interest payments to the extent that earnings on assets of the REFCorp not yet invested in the purchase of REFCorp bonds (generally, interest earned on Savings Association Insurance Fund (SAIF) assessments collected prior to the actual date of REFCorp bond issuance) and certain proceeds from the Resolution Trust Corporation (RTC), are insufficient to cover the REFCorp interest payments. It is our understanding that the FHLBanks likely will be required to contribute the entire \$300 million per year for interest payments on the REFCorp bonds until maturity.

At least two FHLBanks -- FHLBank-Cincinnati and FHLBank-San Francisco -- take exception to this interest assessment procedure. They contend that the term "prior year" in section 21b(f)(2)(C)(ii)(I) and (II) must be interpreted to mean "calendar year" and, thus, the calculation would be based on the prior calendar year.

There seems to be general agreement, in which we concur, that the word "year" as used in section 21b(f)(2)(C), 21b(f)(2)(C)(i) and 21b(f)(2)(C)(ii) should be interpreted to mean a calendar year. However, we find the use of the term "prior year" in section 21b(f)(2)(C)(ii)(I) and (II) to be sufficiently ambiguous that the Congressional intent cannot be authoritatively divined from the plain words of the statute.

Calendar Year. To determine the meaning of ambiguous statutory language, we first look at the conventional meanings of terms and the internal structure of the text. Sutherland, Statutes and Statutory Construction §§ 45.14, 47.01 (4th ed. 1984). The first dictionary definition of "year" is "the period of about 365 1/4 solar days required for one revolution of the earth around the sun..." Webster's Third New International Dictionary, unabridged 2648 (4th ed. 1976). Webster lists "calendar year" as the fourth definition. See id. Thus, the dictionary definition is not dispositive.

However, considerable legal authorities suggest the interpretation that "prior year" means calendar year. Ordinarily, if the same word is used twice in the same paragraph of a statute, it is interpreted to have the same meaning. See Sutherland supra at § 47.16. Based on this principle, "prior year" should be interpreted to refer to the preceding calendar year, since "year" is used earlier in the same subsection referring to a calendar year.

Another principle of statutory construction also supports the calendar year interpretation: "Where the meaning of a word is unclear in one part of the statute but clear in another part, the clear meaning can be imparted to the unclear usage on the assumption that it means the same thing throughout the statute." Id. Thus, the use of the more specific phrase "calendar year" should control the meaning of the more general "prior year" when the two terms are grouped together in the same portion of the statute. However, Professor Sutherland notes that this rule only applies if the result is consistent with legislative intent. Id., see id. at § 48.06.

Since intent is not entirely clear from the plain words of the statute or the context in which they are used, we turn to extrinsic statutory interpretive aids, i.e. background information on the text, such as legislative history. Id. at § 48.01.

Senate bill 774, the Senate-passed version of the bill that ultimately became the Financial Institutions Reform, Recovery and Enforcement Act, Pub. L. No. 101-73, 103 Stat. 183 (Aug. 9, 1989) (FIRREA), made a change from the Administration's original proposal, introduced as Senate bill 413, in the allocation among the FHLBanks of any shortfall in payments required to pay the interest on REFCorp obligations. The Administration's proposal and the House-passed bill both provided for any shortfall in the REFCorp interest payments to be allocated by reference to the same provisions which allocated each FHLBank's share of a shortfall in principal contributions, i.e., section 21b(e)(3)-(6). Paragraph (e)(5) of that section specifically provided for amounts in excess of \$1 billion to be divided according to an asset ratio that is based on a calendar year formula.

The Senate-passed bill changed the interest shortfall formula contained in the Administration's proposal, basing it instead entirely on average advances in the "prior year," rather than on assets or other aspects of the formula allocating a shortfall for REFCorp defeasance: In commenting on the reasons for this change, the Senate Committee on Banking, Housing and Urban Affairs said:

This formula more closely approximates an ability-to-pay measure than that in the Administration bill. Thus, it reduces the discrepancies among [FHLBanks] in the effects of the legislation on dividend yields that the [FHLBanks] will be able to offer.

S. Rep. No. 19, 101st Cong., 1st Sess. 34 (1989). The FIRREA Committee on Conference seemed to settle on the Senate approach to this issue, opting for an interest shortfall allocation formula that closely tracked the Senate-approved formula and language.

The change from the Administration's original formula to the adopted formula is from one that was based on assets in a calendar year to one that was based on advances "in the prior year." A calendar year interpretation in the context of the new formula -- namely, based on advances rather than assets -- is consistent with the explicitly stated legislative intent to adopt a measure that "...more closely approximate(s) an ability-to-pay... ." Id.

Rolling year. On the other hand, dropping the Administration's asset-based, calendar year approach also may suggest that in using "prior year," Congress may have intended to adopt an alternative to a calendar year. The very same legislative history addressed above supports a rolling-year interpretation because it also "more closely approximate(s) an ability-to-pay." In fact, a rolling year is a more current measure of ability to pay than a calendar year. However, it must be recognized that nowhere in the legislative history does Congress expressly refer to a rolling-year approach.

An additional factor in interpreting the legislative history as reflecting a desire to more closely approximate "ability-to-pay" is the conferees' changes to the Senate language further adjusting the formula in a fashion that seems to reflect a decision to better account for the FHLBanks' relative earnings. The Senate formula:

the average month-end level of advances made in the prior year by such bank to [SAIF] members;
§ 21b(f)(2)(B)(ii)(I), S. Rep. No. 19 supra at 213,

was changed by the conferees to:

the average month-end level in the prior year of advances outstanding by such Bank to [SAIF] members; 3

The change from "advances made" to "advances outstanding" takes into account both advances in portfolio and advances paid off. Therefore, "advances outstanding" is a more current indication of FHLBank earnings from advances.

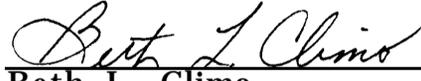
Considerable legal authorities -- both statutory construction and legislative history -- support the interpretation advanced by the FHLBank-San Francisco that "prior year" means prior calendar year. The legislative history of FIRREA indicates that Congress sought a funding mechanism for REFCorp that took into consideration both the ability of each FHLBank to pay and the proportion of each FHLBank's business that is derived from SAIF insured members. This legislative history can support both a calendar-year and rolling-year interpretation. Assuming, however, that SAIF advances are an accurate barometer of each FHLBank's ability to pay, the rolling-year interpretation is a more current indication of outstanding SAIF advances.

CONCLUSION:

We believe it is reasonable for the Oversight Board to adopt an interest assessment formula which calculates each FHLBank's share of any earnings shortfall by interpreting the term "prior year" as used in section 21b(f)(2)(C)(ii)(I) and (II) to mean either: (1) the preceding calendar year; or (2) the preceding

3. § 21b(f)(2)(C)(ii)(I). The quoted language represents the numerator for the ratio in each case. Each formula has analogous language in paragraph (II) describing the denominator for the ratio which reflects advances to all FHLBank System SAIF members.

thirteen-month period on a rolling basis. The calendar-year interpretation is better supported by statutory construction and achieves the intention reflected in legislative history. On the other hand, the rolling-year interpretation gives a more current measure of the objectives expressed in the legislative history.



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