

**DEPARTMENT OF HOUSING AND  
URBAN DEVELOPMENT****24 CFR Part 320****[Docket No. FR-4856-F-02]****RIN 2503-AA17****Removal of Regulation Specifying  
Minimum Face Value of Ginnie Mae  
Securities****AGENCY:** The Government National Mortgage Association (Ginnie Mae), HUD.**ACTION:** Final rule.

**SUMMARY:** This final rule removes the regulation that specifies the current minimum face amount of any security issued by the Government National Mortgage Association (Ginnie Mae). The removal of the regulation allows Ginnie Mae to change the current minimum amount of \$25,000. This final rule follows publication of a proposed rule on April 13, 2004. The Department gave careful consideration to the public comments and decided to adopt the proposed rule as final without change.

**DATES:** Effective Date: July 8, 2005.

**FOR FURTHER INFORMATION CONTACT:**

Thomas R. Weakland, Senior Vice President, Office of Program Operations, or Stephen L. Ledbetter, Director, Securities Policy and Research, Government National Mortgage Association, Room 6216, Department of Housing and Urban Development, 451 Seventh Street, SW., Washington, DC 20410; telephone 202-708-2884 (this is not a toll-free number). Speech-or hearing-impaired individuals may access this number through TTY by calling the toll-free Federal Information Relay Service at 800-877-8339.

**SUPPLEMENTARY INFORMATION:****I. The April 13, 2004 Proposed Rule**

HUD published a proposed rule on April 13, 2004 (69 FR 19746) that invited public comment on the Department's proposal to remove the regulatory provision at 24 CFR 320.5(c). That regulation provided that "The face amount of any security cannot be less than \$25,000." The proposed rule stated that after this final rule becomes effective, the minimum face amount for Ginnie Mae securities would be published in Ginnie Mae's Mortgage-Backed Securities Guide. The proposed rule also indicated, among other things, that Ginnie Mae would like to offer investors different denominations of Ginnie Mae guaranteed securities in order to ensure that Ginnie Mae securities remain attractive to investors.

Five public comments were received in response to the proposed rule. The Department carefully considered the issues raised in the comments, and has decided to adopt the proposed rule as final without change. For the convenience of the reader, the comments are summarized below with HUD's response immediately following the comment.

**II. Discussion of Public Comments  
Received on the Proposed Rule**

One commenter expressed its support for the proposed rule. The commenter stated that empowering Ginnie Mae to set its minimum denominations on a flexible basis will help the marketability of Ginnie Mae mortgage-backed securities (MBS) to the benefit of FHA and VA borrowers. Other commenters raised questions or comments about the proposed rule as follows:

*Comment:* Removing the \$25,000 minimum denomination limit will drain insured deposits out of depository institutions; this could harm the liquidity of community banks, and thus weaken their ability to respond to the credit needs of their communities.

*HUD Response:* Ginnie Mae MBS are not generally considered substitutes for insured deposits. Unlike insured deposits, the cash flow of an MBS depends on the cash flow of an underlying pool of mortgages. For example, while a certificate of deposit and an MBS may have identical stated maturities, their effective durations will likely be substantially different. In addition, the duration of the MBS is generally more sensitive to changes in interest rates. Due to these fundamentally different cash flow characteristics, the Ginnie Mae MBS investor base is quite different from a community bank's depositor customer base. Removing the \$25,000 minimum denomination limit on Ginnie Mae MBS should thus have little impact on the ability of community banks to raise funds through the use of insured deposits.

It is also important to note that the fundamental premise of the Ginnie Mae business model is to help community banks and other participating institutions respond to the credit needs of their communities. The Ginnie Mae guarantee allows community banks to raise funds more easily and cheaply by creating more liquid Ginnie Mae securities. Because banks know they can pool their loans as Ginnie Mae MBS and sell them for a good price, they can use these proceeds to make additional loans in their communities. Any change in the minimum denomination that benefited investors by enhancing the liquidity of

Ginnie Mae securities would benefit community banks as well, allowing them to respond more effectively to the credit needs of their communities by offering lower rates to the low- and moderate-income borrowers that are at the core of Ginnie Mae's mission.

While a lower minimum denomination is not likely to substantially increase the investor base of Ginnie Mae MBS, it will result in increased flexibility for current Ginnie Mae investors. For example, a lower minimum would make it easier for existing investors to reinvest principal and interest payments on their Ginnie Mae MBS into more Ginnie Mae MBS. This would have the effect of increasing the demand for Ginnie Mae securities, which ultimately results in lower rates for low- and moderate-income borrowers.

*Comment:* The investors attracted to smaller denominations of Ginnie Maes are likely to be individuals who may be less sophisticated than current investors and less able to anticipate the multiple risks to which all mortgage-backed security investors are exposed. The proposed change could expose a class of individuals to risks that they are not equipped to manage. Moreover, some investors might mistakenly believe that securities issued in small denominations have the same risk characteristics as instruments covered by deposit insurance.

*HUD Response:* The current \$25,000 minimum denomination does not prevent small investors from buying Ginnie Mae securities. Small investors can already invest in Ginnie Mae securities in amounts substantially less than \$25,000; indeed, investors can invest \$1,000 or less in mutual funds that hold all Ginnie Mae MBS. Through mutual funds and other similar vehicles, those same investors can invest in corporate bonds, stocks and other securities that are much more risky than Ginnie Mae MBS.

The purpose of the \$25,000 minimum denomination requirement was not to protect less sophisticated investors; it was implemented primarily to limit the operational complexities and expenses associated with the market as it existed in 1970, when all Ginnie Mae MBS were issued as physical securities. This was not just the case for Ginnie Mae securities. For example, the U.S. Department of the Treasury and the Federal Reserve converted Treasury securities to a book-entry system over a 20-year period, starting in 1966, in order to lower the substantial costs associated with safekeeping and transferring

physical securities.<sup>1</sup> These costs were partly responsible for Treasury increasing the minimum denomination for Treasury bills from \$1,000 to \$10,000 in 1970.<sup>2</sup> The move to a book-entry system made it easier for Treasury to resume allowing Treasury securities to be offered to investors in smaller denominations; in 1998, Treasury lowered the amounts for Treasury bills and notes from \$10,000 and \$5,000, respectively, to \$1,000.

Similarly, Fannie Mae maintained a \$25,000 minimum denomination for its MBS until it moved from physical to book-entry certification. During the period when Fannie Mae allowed both, it had two different minimum denominations: \$25,000 for a "Certificate in definitive form"<sup>3</sup> and \$1,000 for a "Certificate in book-entry form." Today, both Fannie Mae and Freddie Mac MBS are book-entry securities, and, consistent with market norms, have \$1,000 minimum denominations. It should be noted that Ginnie Mae eliminated the option for Ginnie Mae MBS to be issued as physical securities as part of its conversion of the settlement of all Ginnie Mae securities from the Depository Trust & Clearing Corporation to the Federal Reserve's book-entry system in 2002.<sup>4</sup>

Ginnie Mae investors are protected from unknowingly taking risks by a statutory and regulatory framework that includes requirements that broker-dealers be registered with the Securities and Exchange Commission (SEC). In addition, most broker-dealers are required to join a self-regulatory organization (SRO). A primary mission of both the SEC and the SROs is to create and enforce rules for broker-dealers designed to protect investors. The SEC's principal method for protecting investors is to ensure that they are provided with timely, comprehensive and accurate information with respect to prospective

investments. SROs put additional requirements on their members. For example, broker-dealers are required to have reasonable grounds for believing that investments are suitable for customers, and they have a fundamental responsibility for dealing fairly with their customers. These investor protections will continue to apply for broker-dealers selling Ginnie Mae MBS regardless of what the minimum denomination requirement is.

*Comment:* Just because HUD allowed Fannie Mae and Freddie Mac (the GSEs) to offer small denomination securities, that is no justification for allowing Ginnie Mae to do the same.

*HUD Response:* This comment appears to be alluding to questions that have recently been raised with respect to certain products offered by the GSEs that are specifically targeted at retail investors. However, these products—Investment Notes for Fannie Mae and FreddieNotes® for Freddie Mac—are senior debt products that are part of their term note funding programs; they do not represent interests in or receive payments from mortgages. Thus, unlike Ginnie Mae MBS, these products have cash flows that are similar to certain types of deposit products, and may appeal to retail investors as higher-yielding substitutes for federally-insured deposits. In contrast, as discussed above, Ginnie Mae MBS are not generally considered substitutes for insured deposits.

## Findings and Certifications

### Regulatory Planning and Review

The Office of Management and Budget (OMB) reviewed this rule under Executive Order 12866, Regulatory Planning and Review. OMB determined that this rule is a "significant regulatory action" as defined in section 3(f) of the Order (although not an economically significant regulatory action under the Order). Any changes made to this rule as a result of that review are identified in the docket file, which is available for public inspection in the office of the Regulations Division, Office of General Counsel, Room 10276, 451 Seventh Street, SW., Washington, DC 20410–5000.

### Environmental Impact

This rule removes an existing regulation. The rule does not direct, provide for assistance or loan and mortgage insurance for, or otherwise govern or regulate, real property acquisition, disposition, leasing, rehabilitation, alteration, demolition, or new construction, or establish, revise, or provide for standards for construction or

construction materials, manufactured housing, or occupancy. Therefore, in accordance with 24 CFR 50.19(c)(1), this rule is categorically excluded from the requirements of the National Environmental Policy Act (42 U.S.C. 4321 *et seq.*).

### Unfunded Mandates Reform Act

The Unfunded Mandates Reform Act of 1995 (2 U.S.C. 1531–1538) establishes requirements for federal agencies to assess the effects of their regulatory actions on state, local, and tribal governments and on the private sector. This rule does not impose a federal mandate on any state, local, or tribal government, or on the private sector, within the meaning of the Unfunded Mandates Reform Act of 1995.

### Regulatory Flexibility Act

The Regulatory Flexibility Act (5 U.S.C. 601 *et seq.*) generally requires an agency to conduct a regulatory flexibility analysis of any rule subject to notice and comment rulemaking requirements unless the agency certifies that the rule will not have a significant economic impact on a substantial number of small entities. There are no anti-competitive discriminatory aspects of the rule with regard to small entities, and there are no unusual procedures that will have to be complied with by small entities. The rule removes an existing regulation. Accordingly, the undersigned certifies that this rule will not have a significant economic impact on a substantial number of small entities.

### Executive Order 13132, Federalism

Executive Order 13132 (entitled "Federalism") prohibits an agency from publishing any rule that has federalism implications if the rule either imposes substantial direct compliance costs on state and local governments and is not required by statute, or the rule preempts state law, unless the agency meets the consultation and funding requirements of section 6 of the executive order. This rule does not have federalism implications and does not impose substantial direct compliance costs on state and local governments and does not preempt state law within the meaning of the executive order.

### List of Subjects in 24 CFR Part 320

Mortgages, Securities.

Accordingly, for the reasons described in the preamble, HUD amends 24 CFR part 320 as follows:

<sup>1</sup> In an article published in the December 2004 volume (Vol. 10, No. 3) of FRBNY Economic Policy Review, Kenneth D. Garbade of the Federal Reserve Bank of New York points out that "the cost of safekeeping a bearer municipal bond in the mid-1980s was about \$6 per year, and [the] safekeeping costs for bearer Treasury bonds in the mid-1960s were comparable." Obviously, this fee would be prohibitively expensive on a low minimum denomination security.

<sup>2</sup> See Chapter 7 of *Instruments of the Money Market*, edited by Timothy Q. Cook and Robert K. Laroche, Federal Reserve Bank of Richmond.

<sup>3</sup> See, for example, the prospectus dated November 12, 1987, for Fannie Mae Guaranteed Mortgage Pass-Through Certificates.

<sup>4</sup> Although all Ginnie Mae securities are issued in book-entry form, investors still have the option, after initial issuance, to convert their securities to physical form.

**PART 320—GUARANTY OF  
MORTGAGE-BACKED SECURITIES**

■ 1. The authority citation for part 320 continues to read as follows:

**Authority:** 12 U.S.C. 1721(g), 1723a(a), and 42 U.S.C. 3535(d).

**§ 320.5 [Amended]**

■ 2. Amend § 320.5 by removing and reserving paragraph (c).

Dated: May 23, 2005.

**Michael J. Frenz,**

*Executive Vice President, Government  
National Mortgage Association.*

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