



Loan Collateral Eligibility: eNotes and Other Electronic Documents

August 11, 2021

Members of the Federal Home Loan Banks (FHLBanks) continue to transform their lending channels through the implementation of new and innovative technologies in pursuit of efficiencies, cost savings, and an improved borrower experience. The FHLBanks are committed to supporting our members on this transformation as can be seen in the implementation of the [Member Collateral Electronic Promissory Notes \(eNotes\) Acceptance Requirements and Guidelines](#).

The purpose of this document is to address common questions focused on the deployment of this new technology and its impact on loan eligibility. Our goal is to ensure all members have the information they need to inform the best business decisions while optimizing collateral capacity with FHLBank Indianapolis.

Glossary of Terms:

eNote: A promissory note that is originated, signed, and stored electronically according to the standards for a transferable record. An authoritative electronic copy of the note exists in a file format known as a MISMO SMARTDoc and is registered with an eRegistry and stored in an eVault. In order to be acceptable as pledged collateral, an eNote must be a valid and enforceable transferable record pursuant to the Uniform Electronic Transactions Act ("UETA"), the Electronic Signatures in Global and National Commerce Act ("ESIGN") or otherwise applicable law. All eNotes must meet the FHLBanks' acceptance requirements and guidelines.

MERS eRegistry: The MERS® eRegistry is the mortgage industry's "system of record" for holders of eNotes. A national eNote registry is part of the industry's response to develop systems that can rely upon the UETA and ESIGN to establish legal effectiveness of electronic notes for mortgage loans. The registry identifies the current Controller (holder) and Location (custodian) of the Authoritative Copy of an eNote. The Controller of an eNote can have the equivalent rights as that of a "Holder in Due Course" of a paper negotiable promissory note.

MISMO: MISMO® is the standards development body for the mortgage industry. MISMO developed a common language for exchanging information for the mortgage finance industry. MISMO is a subsidiary of the Mortgage Bankers Association and MISMO stands for *Mortgage Industry Standards Maintenance Organization*.

eVault: An eVault is a specialized document storage system, sometimes referred to as a data warehouse, that holds eNotes (and other digital loan documents) and manages their transfer across various eVaults. eVault technology works by permanently binding electronic signatures to a document and creating a tamper-proof audit trail that demonstrates ownership and compliance.



Transferable Record: An electronic record as described in Section 16 of UETA and in Title II, Section 201 of ESIGN.

Hybrid Closing: A loan where some mortgage loan documents have been signed electronically, but a paper note and note related items have been executed with a Wet Ink Signature.

Wet Ink Signature: An original signature written on paper documentation, as opposed to a fax copy or to an agreement offered verbally or electronically.

Imaged Note: Loan where a Wet Ink Signature paper note had been executed and electronically scanned.

Frequently Asked Questions:

What eligible loan types will the FHLBanks accept as eNotes?

1-4 family closed-end first mortgage loans ("1-4 Family Loans").

What is preventing the FHLBanks from accepting eNotes in other eligible asset classes?

The infrastructure and market standards required to support eNotes in other asset classes is not yet established like it is for 1-4 Family Loans. Roadblocks include:

- The MERS eRegistry is an integral part of the FHLBanks' acceptance requirements as it allows the FHLBanks to control and perfect our security interest in 1-4 Family Loans. Currently the MERS eRegistry does not accept eNotes for other asset classes and there is no other active industry-accepted registry that will handle eNotes for non 1-4 Family Loans.
- The lack of defined and standardized documents prevents validation of the electronic record for other asset classes. Standardized documentation is necessary for effective interoperability between any potential Registry and an eVault to validate eNote records.

If a lender can legally foreclose on a promissory note executed with a digital signature that does not meet the eNote requirements, why will the FHLBanks not accept the loan as eligible collateral?

The FHLBanks acknowledge that documents executed with a digital signature may be enforceable provided they comply with all applicable laws including ESIGN and UETA; however, pledging these types of loans as collateral to the FHLBanks presents several issues:

- If the member is required to deliver loan documents to the FHLBanks, the FHLBanks would not be able to obtain control over the loan; and
- In the case of a default under the Advances Agreement, the FHLBanks' ability to liquidate the loans in a timely manner could be impaired.
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Without the infrastructure, documents, and technology embedding the required protections in the closing process used by members to originate eNotes, the FHLBanks have no way of confirming that they are holding the true original note ("Authoritative Copy"), and additionally that the note has not been altered. The FHLBanks would have no control or protection in the process as a secured lender.

For eligible 1-4 Family Loan eNotes, why do the FHLBanks require delivery of the authoritative copy of the eNote to their eVaults? If a member is not currently required to pledge on delivery for non-eNotes (traditional paper notes), why is delivery of an eNote needed?

The FHLBanks require eNotes to be delivered to our eVault for the following reasons:

- Delivery of the eNote provides absolute certainty that FHLBanks are in control of the Authoritative Copy. The FHLBanks' requirements are heavily reliant upon the MERS eRegistry and designation as Secured Party. Possession of the eNote creates redundancy of control that protects the FHLBanks in the event of a MERS system failure; and
- It is impractical for the FHLBanks to perform due diligence, onboard and continually monitor every eVault vendor solution that is offered in the marketplace. By requiring delivery of the Authoritative Copy of the eNote the FHLBanks avoid potential inter-operability issues with our eVault and member technology solutions. We are hopeful that in the future the mortgage industry can create a designation or certification for vendors that potentially alleviates this issue.

Do eligible 1-4 family eNotes receive the same margin as traditional paper notes?

Yes, the FHLBanks currently apply the same margins for both traditional paper executed notes and eNotes. The FHLBanks' margins are published in the FHLBank Indianapolis Credit Policy and margins are subject to change in accordance with any future policy updates.

Will the FHLBanks accept Hybrid Closing loans for all loan types?

Yes, the FHLBanks will accept Hybrid Closing loans, where all documents with the exception of the original promissory note can be executed electronically or imaged, for all eligible loan types.

Why do the FHLBanks need to be able to take possession of a physical note or eNote if we have an image?

In order to protect the interests of the cooperative, the FHLBanks may require members to deliver loan collateral so that in the event of a liquidation or bankruptcy the FHLBanks' security interest in the loan collateral is protected. Without being able to take possession of an original note or eNote, the FHLBanks run the risk that its interest in the collateral may be compromised during the liquidation process.

When will the FHLBanks be able to accept Imaged Notes where the original is not retained?

The FHLBanks have no plans to allow members to pledge loans where the original note has not been retained and only an imaged note is available. An Imaged Note does not meet the FHLBanks' requirements as an acceptable original note or eNote due to the fact that they fail to meet the requirements established by ESIGN and UETA to make them transferrable records.



Who can I contact if I have questions about the eNote Acceptance Requirements?

If you are evaluating changes to your lending channels to adopt eNotes or have already implemented eNotes and have questions about the FHLBanks' acceptance requirements, we encourage you to contact [Collateral](#) Operations at CreditTeam@fhlbi.com or 800-442-2568. Please also reference the FHLBank Indianapolis' website for additional information (<https://www.fhlbi.com/products-services/credit-products/how-to-access-credit/enotes>).