

FEDERAL HOUSING FINANCE BOARD

OPEN MEETING  
OF THE BOARD OF DIRECTORS

Wednesday, June 18, 2003

10:00 a.m.

Federal Housing Finance Board  
Board Room  
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C O N T E N T S

BOARD MEMBERS:

CHAIRMAN JOHN T. KORSMO  
JOHN C. WEICHER  
ALLAN I. MENDELOWITZ  
FRANZ S. LEICHTER  
J. TIMOTHY O'NEILL

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P R O C E E D I N G S

CHAIRMAN KORSMO: I see we're late, I apologize. Just so everyone's aware of my mood today, I spent 45 minutes getting from the Labor Department to here today. I should have walked from home, it would have been faster.

With that, I call this meeting to order and welcome my colleagues. We have a full agenda today and rather than spend any more time anticipating it, why don't we get into it. The first item on our agenda is a Proposed Rule Regarding Acquired Member Assets. My Agenda says Office of Supervision. Who does that mean is in charge, Dr. Cross?

DR. CROSS: We're here to describe to you a proposal to revise the Acquired Member Assets Regulation. This is jointly developed by the Office of Supervision and the Office of the General Counsel. The principal staff people working on the proposal were Christina Muradian, Sharon Like, Tom Joseph. Christina Muradian will provide an overview of the proposal.

MS. MURADIAN: Good morning. Staff is presenting for Finance Board consideration a proposal to amend the Acquired Member Assets or AMA Regulation. This proposed

rule is the first step in an effort to shift the focus of Finance Board regulations from prescriptive rules toward supervisory review, while placing greater responsibility on the banks to design and manage their AMA programs.

This proposed rule also would clarify and simplify AMA regulations to include provisions that enhance safety and soundness. In addition, the core principles underlying the current rule have been preserved such that the member still has significant responsibility for the credit risk, while the bank manages the interest rate risk.

The Finance Board's current regulation has been in effect since July 2000. The amendments presented today are the first changes proposed to the rule since it became effective. The current rule authorizes the banks to acquire certain loans, principally conforming residential mortgage loans from their membership and housing associates as a means of advancing their housing finance mission. The current rule also prescribes in some detail the manner in which banks may do so.

Since implementation of the current rule, staff recognize that an approach that places a greater responsibility on the banks would likely prove to be more

effective and efficient in regulating the banks' mortgage purchase programs.

Additionally, now that we have several years' experience in overseeing these programs, we've identified a number of opportunities to clarify and simplify the current rule. More specifically, safety and soundness would be enhanced under the proposed rule, through provisions concerning the banks' exposure to the obligations of members to provide credit enhancement by removing certain restrictions on the use of pool insurance, and through improving the information quality of AMA data, subject to the reporting requirements.

Simplifications would be achieved by eliminating requirements associated with the terms "valid business purpose" and "expected losses," which have proven difficult to define and examine against.

Further, banks and members would assume greater responsibility for deciding how to meet the proposed regulatory requirements and that the proposed rule would streamline the criteria for credit risk-sharing, including eliminating both the requirement that membership be directly responsible for expected losses and the distinction in how

loan-level and pool insurance can be used as a credit enhancement.

The proposed rule also would codify the authority of a bank to acquire as AMA, instruments that are created by bank membership or housing associates in cooperation with the bank and that represent an interest in loans that individually could qualify as AMA.

Finally, in the preamble to the proposed rule, we are requesting comment on several topics: First, whether the Finance Board should take measures to prevent a bank from acquiring AMA assets where the loans have certain features or were made under circumstances that may be considered predatory or abusive.

Second, whether a bank should be permitted to acquire AMA directly from a member's non-member subsidiary or from a member's non-member affiliate, in general, so long as the related member provides the required credit enhancement.

Third, whether it would be appropriate to allow a member or housing associate to secure its credit enhancement obligation with collateral that is not eligible under the Bank Act to secure advances.

Fourth, whether the pricing provision included in Section 955.5(c) is still necessary or appropriate now that banks have more experience and options relating to AMA products.

And, last, whether data descriptions for purposes of reporting are clear.

Thank you, and we'd be happy to answer any questions.

CHAIRMAN KORSMO: Thank you, Ms. Muradian, are there any questions from any membership of the Board? Mr. Leichter.

DIRECTOR LEICHTER: Thank you. Does this give the banks authority to undertake any AMA activities that they currently prohibited from taking?

MS. MURADIAN: No, it doesn't.

DIRECTOR LEICHTER: It does not?

MR. SMITH: It would allow them more flexibility in designing their sharing structures but--

DIRECTOR LEICHTER: I'm sorry, I didn't hear you.

MR. SMITH: More flexibility.

DIRECTOR LEICHTER: Right, but there's nothing that presently that is prohibited that they would be allowed

to do under the AMA regulation without coming to the Finance Board?

DR. CROSS: That's correct.

DIRECTOR LEICHTER: Okay. And does this new rule address in any respect what's known as the Chicago Shared-Funding Plan, so that if any other bank wanted to do a similar program, would that bank have to come and seek approval from the Finance Board?

DR. CROSS: The--a bank would have to come forward through the new business activity provisions of Finance Board regulations to engage in a Shared-Funding type program. The proposed rule does address the Chicago circumstance by codifying within the rule the authority that was cited as the result of the preamble language related to the existing rule.

CHAIRMAN KORSMO: But in terms of process, nothing has changed.

MR. SMITH: Right, no change whatsoever. The process has not changed, correct.

DR. CROSS: The process of seeking Finance Board approval.

CHAIRMAN KORSMO: And authorities, really, are not changed either, I guess is what I hear--

MS. MURADIAN: Right.

CHAIRMAN KORSMO: --from Dr. Smith and Ms. Muradian.

DIRECTOR LEICHTER: Could you just briefly tell us about the data collection requirements being eliminated and why and what new ones are being imposed?

MR. SMITH: There are some data elements that are being eliminated from the collection requirement and those data elements are deemed redundant or unnecessary or they don't provide information that we use in any way shape or form. There are relatively few such data elements. The new ones that we have added are primarily for organization and to improve the informational content and, in some cases, we have sort of redefined the variable. So the changes are really very modest.

DIRECTOR LEICHTER: Can you just give an example of one item of data collection that we've eliminated and one that we've added, just so that we get a flavor of this?

MR. SMITH: I'd have to look it up.

DIRECTOR LEICHTER: Yeah.

MS. MURADIAN: One example would be--in the current rule request, type of credit enhancement. And in the current rule, that definition--in the proposed rule, the definition has been altered to ask for the amount of the credit enhancement.

CHAIRMAN KORSMO: So if I'm understanding it, the data changes that we're talking about are actually enhancements to what we--either are enhancements to what we have previously gathered or we're eliminating gathering information that we haven't used. Is that a fair assessment of what we're trying to accomplish?

DR. CROSS: And over time in practice, Finance Board staff has worked with the bank's staff to refine what was actually submitted to us by the banks, pursuant to the existing rule. That was done on an informal basis by agreement with the 12 banks, but was not reflected in the regulation.

MR. SMITH: So, you're codifying that now?

DR. CROSS: The proposed rule codifies those changes that have happened over time.

DIRECTOR LEICHTER: Thank you.

CHAIRMAN KORSMO: Dr. Leichter, any other questions?

DIRECTOR LEICHTER: No.

CHAIRMAN KORSMO: Any other directors have any questions of the staff? Am I right, we're anticipating a comment period of what?

MR. SMITH: Sixty days.

CHAIRMAN KORSMO: Sixty days. All right. I wasn't sure of whether the version I had had the final version or not. Any other questions for the staff?

DIRECTOR MENDELOWITZ: I'm curious--

CHAIRMAN KORSMO: Dr. Mendelowitz?

DIRECTOR MENDELOWITZ: --how do we decide between a 60-day commentary--a 90-day commentary?

CHAIRMAN KORSMO: Well you notice, I just wanted to ask what the comment period was, Mr. Intrater, care to comment?

MR. INTRATER: The norm is 60 days for something of this size, that's basically the standard rule. Sometimes to accommodate a search for other interests to expand it.

CHAIRMAN KORSMO: Dr. Weicher?

DIRECTOR WEICHER: If I can perhaps provide some light on that from the HUD standpoint and I was raising this beforehand. The normal OMB practice is 60 days for a typical rule. For a really complicated rule, for instance our proposal last fall, there was a 90-day comment period. I think it is possible to go as short as 30 days in special circumstances but for the Executive Branch proper, 60 is sort of normal and, at least from my standpoint, this looks sort of normal.

CHAIRMAN KORSMO: Thank you, Dr. Weicher. Any other comment, any questions I should say? Seeing none, could I have a motion to adopt the proposal?

DIRECTOR O'NEILL: I will so move.

CHAIRMAN KORSMO: Director O'Neill has moved adoption of the proposed rule. Is there discussion of the motion?

DIRECTOR LEICHTER: I just--

CHAIRMAN KORSMO: Director Leichter?

DIRECTOR LEICHTER: Yes, I just want to make a comment on one feature of the proposed rule. I'm pleased that as part of the preamble of the proposed rule that we agreed to include language requesting comment on measures

the Finance Board might consider to prevent the Federal Home Loan Banks from acquiring loans or assets backed by loans that had features or were made under circumstances that may be considered predatory. This is an important issue, certainly to the community served by the Bank System, and it is incumbent upon the Finance Board as part of its safety and soundness responsibilities and its housing finance mission to address this issue. To date, a number of other federal financial institution regulators, including OCC, OTS, and the Federal Reserve Board have utilized their authority to combat predatory practices.

When the AMA regulations were finalized in July 2000, the Finance Board commented at that time about its intent to consider the matter. A month prior, in June of 2000, HUD and the Department of Treasury issued a joint report entitled, "Curbing Predatory Home Mortgage Lending," in which these agencies made a number of policy recommendations intended to address the problem of predatory lending nationwide. Among these recommendations were actions that the Finance Board, working to assure consistency with requirements that HUD imposes on Fannie Mae and Freddie Mac, would apply to the Federal Home Loan Banks

to prevent any involvement in abusive practices. I am pleased that some of the Home Loan Banks have taken steps to deal with concerns about predatory lending and AMA activities, including the adoption of voluntary guidelines, similar to those developed by Fannie Mae and Freddie Mac. I look forward to comments on the initiatives that are in the proposed rules and I really encourage feedback from the banks and others who are interested in this issue to see what steps ought to be taken and embodied in regulations to see that the system avoids being involved in the use of high-cost lending and, certainly, in the acquisition of AMA.

I want to thank Steve Cross, Scott Smith, Shane Goettle, and the OS staff that we've worked with on this issue and I'm pleased that we have inclusion of this language in the proposed--or in the preamble of the proposed rule and look forward to getting the comments.

CHAIRMAN KORSMO: I know this has been a concern of Director Leichter and others on the Board, I'm happy that this is part of the proposed rule and I think we can look forward to the responses that we get. Any discussion of the motion, Director Weicher.

DIRECTOR WEICHER: Just following up, Director Leichter left out one agency which is doing something about predatory lending, the Federal Housing Administration in the Department of Housing and Urban Development, when you went through those folks. We are not--

DIRECTOR LEICHTER: I certainly didn't mean, I mentioned HUD, but--

CHAIRMAN KORSMO: An oversight, I'm sure.

DIRECTOR LEICHTER: Certainly the emendation should be noted.

DIRECTOR WEICHER: Thank you, I have something more to say than just to complain a little bit. We have reregulated those lenders who provide FHA loans and we regulate them so far as their FHA loans are concerned and we have been in the process of putting through a fairly extensive regulatory agenda dealing with predatory lending. We have five rules that have gone final. Five, if I remember correctly, that are in the proposed stage and a few more coming behind. And the reason for this is that what we are trying to do is to prohibit individual practices that we consider to be unfair or deceptive, as opposed to trying to define a bright line between what is predatory and what is

not predatory, because, of course, there are all sorts of variations on loan terms in the marketplace. And we found, independently, that the Federal Trade Commission was taking the same approach; prohibiting practices rather than a category, however defined, of loans. And most recently, we put out a rule prohibiting flipping in FHA insurance, we won't insure a loan if a property is sold twice within three months; and we have criteria if it's sold twice within 12 months.

In addition, Director Leichter mentioned the GSEs and I might add, as the Directors know, HUD is responsible for setting the affordable housing goals for Fannie Mae and Freddie Mac and we do, in fact deny--we refuse to count loans which are predatory, which is defined as falling under the HOEPA triggers. We refuse to allow those loans to be counted toward the affordable housing goals. Now I don't know that any of that necessarily changes--I don't think any of that necessarily changes what we have here and I agree with Director Leichter that I think this is an important question to ask and I venture the thought that we will have lots of comments, the staff will be busy.

CHAIRMAN KORSMO: I think as Director Leichter mentioned, a number of banks have already addressed this on their own, whether or not they consider that sufficient and appropriate remains to be seen. I anticipate, as well, that we will get many comments on these particular issues.

Thank you, Director Weicher. Any other discussion of the motion? Director Mendelowitz.

DIRECTOR MENDELOWITZ: Thank you, Mr. Chairman. I just wanted to observe that the issue of Shared Funding and the approval process, obviously, has come up in the context of this proposed revision of the AMA rule. And as, under the prior rule, this rule envisions that any bank wishing to undertake an initiative similar to the Shared-Funding initiative in Chicago, will still be required to come to the Finance Board to receive approval under the terms of the new business provisions of our rules.

As I've said at earlier meetings, I felt that the Shared-Funding proposal was far too significant a matter to be resolved and reviewed and approved at the staff level. It's something that should have come to the Finance Board. I worked on a proposed rule modification that would require

such innovations and significant high visibility issues to come to the Board rather than to the staff for approval.

I've held off introducing that because it's my understanding that we currently have underway a review of the rules relating to new business practices. The staff anticipates it'll be ready for Board review sometime in September--

MR. SMITH: That is correct.

DIRECTOR MENDELOWITZ: --as I understand it, and while we're not changing the procedure for approving such things in this rule, we do anticipate there will be changes in the proposed rule brought by the staff to the Board in September and during the interim period if any such similar proposals were to come in, my intention is to use existing rules and procedures to provide for bringing those matters to the Board for review, rather than making them with the staff.

CHAIRMAN KORSMO: At this point, the better part of valor, thank you Director Mendelowitz. Any other comments, any other questions or comments? Any other discussion on the motion? Seeing none, the Secretary will

please call the roll on the question of approval of the proposed rule amending our AMA provisions.

MS. GOTTLIEB: On the matter of the approval of the Proposed Rule Concerning Acquired Member Assets, Director Leichter, how do you vote?

DIRECTOR LEICHTER: Yes.

MS. GOTTLIEB: Director O'Neill?

DIRECTOR O'NEILL: Aye.

MS. GOTTLIEB: Director Mendelowitz?

DIRECTOR MENDELOWITZ: Staff did a very nice job on this, I'm happy to vote for it.

MS. GOTTLIEB: Director Weicher?

CHAIRMAN KORSMO: We'll take that as a yes vote.

DIRECTOR MENDELOWITZ: Yes.

MS. GOTTLIEB: Chairman Korsmo?

CHAIRMAN KORSMO: Yes, the motion is carried, the proposed rule is approved and will be published for notice, forthwith. Thank you all.

DIRECTOR LEICHTER: Subject as any rule to any corrections or adjustments.

CHAIRMAN KORSMO: Without objection. Thank you to the staff, this process went very well I thought, and I

appreciate that in the wake of our staff briefing on this particular issue the staff managed to accommodate concerns of several of the directors and thank you again Christina and Sharon and Steve--I was going to say you're not Steve, you're Scott; and others who were involved in the process, we appreciate it very much.

The next item on our agenda is the Rule Regarding the Privacy and Freedom of Information Acts. This particular rule is in the purview of the Office of the General Counsel. Because I see John C. Mantini sitting before me, my assumption is you will be presenting this proposal. Mr. Mantini.

MR. MANTINI: Yes sir. Good morning. Thank you, Mr. Chairman. Presented for Board consideration is a Final Rule with a 60-day comment period that revises the Finance Board's Privacy Act and Freedom of Information Act regulations.

The revisions to the Privacy Act Rule reflect a reassignment of responsibility and authority; responsibility for administering the Finance Board Privacy Act program, will be transferred to the Office of General Counsel. And

an OGC staff member has replaced the Secretary to the Board of Directors as the Finance Board's Privacy Act Official.

To make the rule more user friendly, the revised rule is written in plain language and, where appropriate, uses a question-and-answer format. We also recommend amending the fee schedule in the FOIA rule to take into account increased salary and operating costs. The Board determines the amount of the fee it charges to duplicate records under the Privacy Act, in accordance with the FOIA fee schedule. Do any of the Board members have any questions?

CHAIRMAN KORSMO: Thank you, Mr. Mantini. Are there any questions from any members of the Board? Any questions?

DIRECTOR MENDELOWITZ: What happens to any fees received for FOIA requests?

MR. MANTINI: FOIA fee schedules?

DIRECTOR MENDELOWITZ: Yes.

MR. MANTINI: It's considered income from other sources under our statutory authorization and we accumulate it into our budget. It's accounted for in our budget.

DIRECTOR MENDELOWITZ: It doesn't go to the treasury?

MR. MANTINI: No, no, it's money that we're permitted to accumulate.

CHAIRMAN KORSMO: I thought it went into the General Counsel's Office coffee fund, but I may be mistaken.

MR. INTRATER: It wouldn't pay for the coffee.

MR. MANTINI: In an appropriated fund agency, it would go into the Treasury general fund.

CHAIRMAN KORSMO: Any other questions of the staff? Seeing none, could we have a motion to adopt the interim final rule?

DIRECTOR LEICHTER: I will so move.

CHAIRMAN KORSMO: Director Leichter has moved adoption of the Interim Final Rule Regarding Revisions to the Privacy Act and Freedom of Information Act Regulations. Is there any discussion of the motion? Any discussion of the motion? Seeing none, the Secretary will please call the roll on the motion.

MS. GOTTLIEB: On the matter of the Approval of the Interim Final Rule Regarding the Privacy and Freedom of Information Acts, Director Leichter, how do you vote?

DIRECTOR LEICHTER: Yes.

MS. GOTTLIEB: Director O'Neill?

DIRECTOR O'NEILL: Aye.

MS. GOTTLIEB: Director Mendelowitz?

DIRECTOR MENDELOWITZ: Yes.

MS. GOTTLIEB: Director Weicher?

DIRECTOR WEICHER: Aye.

MS. GOTTLIEB: Chairman Korsmo?

CHAIRMAN KORSMO: Aye, the motion is carried and the Interim Final Rule is adopted. Thank you, Mr. Mantini. He's not moving so my guess is, the next item on the agenda will also be presented by Mr. Mantini. It is an amendment to our regulations updating the Description of Organization and Functions Regulation. Mr. Mantini.

MR. MANTINI: Thank you, Mr. Chairman, members of the Board. We're presenting for your consideration, this morning, a final rule required by 5 United States Code, 552(A), the Freedom of Information Act, a Final Rule Revising the Finance Board's Description of Organization and Functions to reflect agency reorganizations that have already taken effect.

We are proposing this rule at this time because there have been several reorganizations that have occurred since 1996 and this rule will properly reflect the agency's organization in that time. The final rule will update the description of the Finance Board functions and general organization to reflect the agency's current structure. It also provides general information to the public so that individuals who want to request information from the Finance Board know where to direct their requests.

CHAIRMAN KORSMO: And that, as I understand it, is really the genesis for us having this--the organization described in our regs. For the benefit of my colleagues on the Board, I had asked the question, again, even prior to the reorganization that took place last August, as to why the current regs didn't reflect the reality that existed prior to that organization and had suggested at the time that as we were going through the process of reviewing our regulations, why don't we just eliminate this title all together? But as I understand it now, the reason we have this descriptive element in our regs is to accommodate the Freedom of Information Act requirements, is that correct?

MR. MANTINI: That's correct. Also, by way of information, it's interesting that some of us on the--myself included--have received requests from individuals from all over the country for such things as: How do I get a mortgage? And that type of thing. By providing this information, it basically lets people know what we really do--

DIRECTOR MENDELOWITZ: Really do--

MR. MANTINI: --that we're not a mortgage originator.

CHAIRMAN KORSMO: Thank you.

DIRECTOR LEICHTER: What are your terms?

MR. MANTINI: We'll send you a copy of the regs.

CHAIRMAN KORSMO: Are there any questions for Mr. Mantini on the proposed amendment to this potential reg? Any questions for Mr. Mantini? Seeing none, the chair will entertain a motion to approve the reg.

DIRECTOR WEICHER: So moved.

CHAIRMAN KORSMO: Thank you Director Weicher. Dr. Weicher has moved adoption of the proposed changes to our description of organization functions regulations. Is there any discussion of the motion?

DIRECTOR LEICHTER: Yes.

CHAIRMAN KORSMO: Director Leichter?

DIRECTOR LEICHTER: Yes, I just want to clarify that my vote for this particular regulation should not be misconstrued as my necessarily approving or disapproving the organizational structure as it's set forth. In fact I made clear that there have been changes in the organization of the agency that I do not approve of. These were done without consultation, deliberation or action of the Board of Directors and I continue to reserve my right to express my disagreement with that reorganization. But insofar as all we're doing--

CHAIRMAN KORSMO: No one has ever assumed you would step back from your right to disagree.

DIRECTOR LEICHTER: --and express it, thank you. That's what makes a five-member Board more interesting than a single proprietorship. But I just see this as a ministerial act and, insofar as I understand it, I think it's an accurate description of how the agency presently functions and my vote is meant solely to affirm that.

CHAIRMAN KORSMO: So noted. Any other discussion on the motion, Director Mendelowitz?

DIRECTOR MENDELOWITZ: In the interest--

CHAIRMAN KORSMO: Are you going to "amen" to this?

DIRECTOR MENDELOWITZ: In the interest of brevity, everything that Director Leichter said, goes for me, too.

CHAIRMAN KORSMO: Again noted. Any other discussion of the motion? Any other discussion? Hearing none, the Secretary will please call the roll.

MS. GOTTLIEB: On the Approval of the Final Rule Concerning the Description of the Finance Board's Organization and Functions, Director Leichter, how do you vote?

DIRECTOR LEICHTER: Yes.

MS. GOTTLIEB: Director O'Neill?

DIRECTOR O'NEILL: Aye.

MS. GOTTLIEB: Director Mendelowitz?

DIRECTOR MENDELOWITZ: Yes.

MS. GOTTLIEB: Director Weicher?

DIRECTOR WEICHER: Aye.

MS. GOTTLIEB: Chairman Korsmo?

CHAIRMAN KORSMO: Yes, with all the caveats noted, the motion is approved, the regulation is adopted.

The next item on our agenda is the Appointment of a Director to the Board of Directors of the Federal Home Loan Bank of Topeka. My colleagues will recall that Daniel N. Witt who had been appointed to serve on the board resigned due to the pressures of his business and asked to be replaced. I am nominating for your consideration, Aida Diaz Kirby to replace Mr. Witt to fill out the unexpired term that expires on December 31 of 2004. Ms. Kirby is the founder and director of Comtech International, Inc., a full-service training company, specializing in customized interactive multimedia programs delivered on CD-ROM and corporate Intranets. I wish I had an understanding of what exactly that is. Comtech was listed in "Colorado Business Magazine's" top 100 minority-owned companies, and top 100 women-owned companies. It was also featured in "Hispanic" magazine's entrepreneur 100 list. The company has won numerous awards and recognition for excellence.

Prior to becoming an entrepreneur, Ms. Kirby spent 24 years at US West in Denver. She ended her career as the executive director of a special markets development project in Denver, Colorado, where she was responsible for managing over 200 employees and a budget in excess of \$20 million.

Ms. Diaz is a native of Cuba; like Secretary Martinez, she was--came to this country under the Pedro Pan program, lived in an orphanage and foster homes until striking out on her own. She's supported herself since high school. After a ten-year separation from her family, she managed to get her parents out of Cuba and here to the United States. She's a woman whose talent and accomplishments have been recognized by numerous organizations and publications. And I take great pride in having the opportunity to nominate Aida Diaz Kirby to serve as a director of the Federal Home Loan Bank of Topeka?

Are there any other nominations to fill this position? Director O'Neill?

DIRECTOR O'NEILL: I don't have any nominations, but I just wanted to note for the record that Aida is a member of the Jesuit Alpha Sigma Nu Honor Society and being under the Jesuits for eight years, anybody that is honored by them, is very good in my book. And the other question I just had, briefly, is how long did Dan Witt serve?

DR. CROSS: Half a year, a good year and a half?

CHAIRMAN KORSMO: Did we just appoint him this last year or was it the year before?

DR. CROSS: If the term expired 2004--

CHAIRMAN KORSMO: Four--it would have been in 2001, that's right, so he was appointed--he was there a year and a half. Are there any other nominations? Are there any other nominations? Hearing none, the Secretary will please call the roll on the appointment of Aida Diaz Kirby to serve as a director of the Federal Home Loan Bank of Topeka with a term expiring December 31, 2004.

MS. GOTTLIEB: On the appointment of Aida Diaz Kirby, to fill the vacant appointed directorship at the Home Loan Bank of Topeka, Director Leichter, how do you vote?

DIRECTOR LEICHTER: Yes.

MS. GOTTLIEB: Director O'Neill?

DIRECTOR O'NEILL: Aye.

MS. GOTTLIEB: Director Mendelowitz?

DIRECTOR MENDELOWITZ: Yes.

MS. GOTTLIEB: Director Weicher?

DIRECTOR WEICHER: Aye.

MS. GOTTLIEB: Chairman Korsmo?

CHAIRMAN KORSMO: Aye. Aida Diaz Kirby is appointed to the Board of the Federal Home Loan Bank of Topeka for a term expiring December 31, 2004.

The next item on our agenda is kind of a housekeeping item because we missed it a couple of meetings ago when we replaced Nancy Miller-Herron as a director of the Board of the Federal Home Loan Bank of Cincinnati. You will recall that Ms. Miller-Herron resigned, as a director of the Cincinnati Board, I think to become a judge in Kentucky. And at that time--

DIRECTOR O'NEILL: I think, in Tennessee.

CHAIRMAN KORSMO: Is it Tennessee? Yeah, that's right, I apologize, yes, she's in Nashville, is she not? In Tennessee. At that time, we replaced Ms. Miller-Herron, with Mr. Wick. However, at the time, we failed to note that Ms. Miller-Herron also served with the designation of being a community interest director. That means we have to replace--not replace, but designate an additional appointed director on the Cincinnati Bank Board as a community interest director. I'm recommending and nominating today for appointment as a community interest director Donald R. Ball. You will recall, Mr. Ball is a home builder; has been a member of the Cincinnati Board for sometime. He meets the requirements of having served as a member of an organization with more than two-year history of representing consumer

community interests; on banking services, credit services, housing or financial consumer protections, which is a requirement for serving as a community interest director. He's been very active, as I think all of you are aware, in housing organizations and affordable-housing organizations and consumer issues dealing with housing. And so it is my great pleasure to nominate for designation as a community interest director on the Board of the Federal Home Loan Bank of Cincinnati, Mr. Donald R. Ball. I'm not quite sure how to handle this, whether there are other--it really isn't a nomination question, I'm guessing it's without objection, perhaps, but let's go with, I'm making that recommendation and ask if there's any comment from any member of the Board about issuing this designation. Any comment?

DIRECTOR MENDELOWITZ: Sure, I can't pass up the opportunity to--

CHAIRMAN KORSMO: I knew that, I had great confidence, Director Mendelowitz?

DIRECTOR MENDELOWITZ: To do two things, one is just to note again, the wonderful value and service that Nancy Miller-Herron provided in her years on the Board of Directors at Cincinnati Bank. She brought great value,

great leadership and I think it is a real loss. And I know that we all greatly appreciate the service she provided.

Secondly, I'm happy to support Mr. Ball's designation. He's clearly an outstanding member of the Board who brings great experience and assets as a community affairs director.

CHAIRMAN KORSMO: Thank you, is there any other comment? Again, I'm at a loss as to exactly how to handle this, but we'll take it as--the General Counsel is smiling, I don't know whether that's objection or acquiescence, but it's--

DIRECTOR MENDELOWITZ: Just call the vote.

CHAIRMAN KORSMO: In the absence of comment, why don't we do that. The question--I'll ask the Secretary to please call the roll on the question of designating Donald R. Ball as a community interest director on the Board of the Federal Home Loan Bank of Cincinnati.

MS. GOTTLIEB: On the Designation of Donald R. Ball as Community Interest Director on the Board of Directors of the Federal Home Loan Bank of Cincinnati, Director Leichter, how do you vote?

DIRECTOR LEICHTER: Yes.

MS. GOTTLIEB: Director O'Neill?

DIRECTOR O'NEILL: Aye.

MS. GOTTLIEB: Director Mendelowitz?

DIRECTOR MENDELOWITZ: Yes.

MS. GOTTLIEB: Director Weicher?

DIRECTOR WEICHER: Aye.

MS. GOTTLIEB: Chairman Korsmo?

CHAIRMAN KORSMO: Yes, Donald R. Ball will be designated a Community Interest Director on the Board of Directors of the Federal Home Loan Bank of Cincinnati.

The final item on our agenda today is the Designation of Federal Home Loan Bank Director Directorships for the Year 2003. The Office of Supervision will present this item, excuse me, I guess and, also, the Office of General Counsel. Pat Sweeney and Neil Crowley are here to present this. It is a somewhat complicated presentation of the Byzantine formula under which we operate. So, with that by way of introduction, Pat, the floor is yours, please.

MS. SWEENEY: Thank you. Good morning. Staff has provided the Board with a resolution and two attachments for its consideration and approval of the annual allocation of directorships at each of the 12 Federal Home Loan Banks.

With the exception of two changes, the Board approval will approve the current number of directorships at each of the banks for 2004.

Much of the designation of directorships process is prescribed by law. Section 7(a) of the Bank Act provides that the Board of Directors of each bank shall have a minimum of 14 directors, six appointed and eight elected. Section 7(b) of the Bank Act requires that the Finance Board annually allocate the elective directorships at each bank in the states in the bank district.

Each state is guaranteed a minimum of one elective directorship, but may earn more seats based on its stock allocations, in this case as of year end 2002.

Section 7(c) of the Bank Act requires that the Finance Board allocate the elective directorships at each bank among the states in the approximate ratio of the amount of bank stock that the members in each state were required to own as of the end of the prior year. The Finance Board conducts the annual allocation of directorships in accordance with a mathematical formula known as the method of equal proportions. I'll leave it with that.

Section 7(c) of the Bank Act also includes a grandfather provision, which requires that each state must have at least as many elective directorships as it had on December 31, 1960. So, after applying the--

CHAIRMAN KORSMO: A critical year in the history of our nation.

MS. SWEENEY: --after applying the method of equal proportions, if the allocation of eight seats results in states having fewer than their grandfathered number of elective directorships, the Finance Board must create additional elective directorships to make sure these states maintain the number that they were entitled to as of 1960.

Separately, with regard to the districts with five or more states, Section 7(a) of the Bank Act authorizes the Finance Board to increase the number of elective directorships up to 13 and to increase the number of appointed directorships up to three-fourths the number of elective directorships. Thus, for the districts of Boston, Atlanta, Des Moines, Dallas, and Seattle, the Finance Board may reauthorize the elective and appointive discretionary seats that it has established in previous years.

The Finance Board may also choose to establish additional discretionary seats for these banks and/or may decline to reauthorize any or all of the discretionary seats if it so chooses to do.

Now back to this year's allocation of elective directorships. Based on the application of the method of equal proportions and the grandfather provision, there's a minimal change in the number of directorships. In fact, the total number remains constant at 108 seats. This reflects a gain of one stock-based seat in the District of Boston and the loss of one stock-based seat in the District of Pittsburgh. These two changes are based on fluctuations in the amount of stock held by members in these two states in those districts relative to the amount of stock held by the members located in other states in those two districts.

For the remaining 10 banks, the application of the method of equal proportions and the grandfather provision results in no change in either the number of elective directorships or the state to which they are allocated.

Thus, the Board will be approving a total of 108 elected director stock-based seats that result from the method of equal proportions and the grandfather provision.

Now, on to discretionary seats, just briefly. At the present, there are a total of 19 discretionary seats, nine elective and 10 appointive in the five districts that have five or more states. The creation of these directorships is purely a matter of discretion for the Board and is not dependent on the amount of stock owned by the members in any particular state or on any other factor.

As a part of the Board package before you, the designation of directorships resolution effective for 2004 has been drafted consistent with past practice to maintain the existing discretionary seats that is, specifically, to serve all 19 discretionary seats.

This Board has the discretion once again to decline to reauthorize any or all of these directorships if it so chooses. Declining to reauthorize any directorship would cause it to terminate at the end of this year; even if the term had not expired.

Because the number of appointive directorships cannot exceed three-fourths the number of elective directorships, if the Board were to terminate any of the discretionary elective directorships, that action would

cause discretionary elective directorships to terminate as well.

This concludes my brief summary of the 2003 designation of directorships and Neil and I are ready to take any questions.

MR. CROWLEY: Yeah, I don't have any separate presentation.

CHAIRMAN KORSMO: It looked like you were anxious to go there for a minute. Thank you, Pat. Are there any questions of Pat or Neil regarding the formulas and the proposed directorship numbers? Director O'Neill.

DIRECTOR O'NEILL: One of the reasons that we're doing it now is that the banks are waiting for us to do the allocation so they can start their election process.

MS. SWEENEY: That's right.

DIRECTOR O'NEILL: When, normally, does that process begin?

MS. SWEENEY: For many of the banks, they'll be starting--the majority of the banks will start their election before the end of this month.

CHAIRMAN KORSMO: In fact I saw one yesterday that had begun the process effective June 10--June 10 was the day of beginning to accept nominations for elective seats.

DIRECTOR O'NEILL: Are we ahead, behind or about the time that we usually do this?

MS. SWEENEY: We're one week behind what we did last year and that was the result of the postponement of the Board meeting for one week. So, in respect to that, I'd say we're right where we--

CHAIRMAN KORSMO: Would it make any sense for us to move this process to an earlier month, in other words--

MS. SWEENEY: In May?

CHAIRMAN KORSMO: --in other words to do this in May next year as opposed to June?

MS. SWEENEY: Yes, that would be--

CHAIRMAN KORSMO: My guess is--

MS. SWEENEY: --we didn't do that this year, of course, because there was no May Board meeting.

CHAIRMAN KORSMO: My assumption, again, based on what I've seen in correspondence from the various banks is that they've been ready to start the process and June is

their ordinary starting date for many, if not all of the banks--

MS. SWEENEY: For many.

CHAIRMAN KORSMO: --so, perhaps we could be better served or they would be better served if we went through this exercise next May. Again, we didn't have a meeting in May and we did move this meeting back a week to accommodate directors' schedules, but maybe this is something for us to consider for next year when we plan our meeting schedule.

DIRECTOR O'NEILL: I think that would be prudent. Thank you.

CHAIRMAN KORSMO: Are there any other questions of the staff? Director Mendelowitz?

DIRECTOR MENDELOWITZ: Last year we made certain decisions to increase discretionary seats, but we did it with the understanding that those seats would have a one-year term.

MR. CROWLEY: Did we give that a one-year term?

MS. SWEENEY: Yes, one year.

DIRECTOR MENDELOWITZ: And all discretionary seats, by definition, are one-year terms.

MR. CROWLEY: Technically, they have a three-year term, but they are reauthorized--

DIRECTOR MENDELOWITZ: Each year, right. And so that, in effect, while we haven't changed in this allocation the number of discretionary seats, what we're doing, in fact, is only binding going forward one year.

MR. CROWLEY: Correct, and that's the same every year, with respect to the discretionary seats.

CHAIRMAN KORSMO: Any other questions of the staff? Any other questions of the staff? Hearing none, the chair would entertain a motion to approve the allocation of the 2003 elective seats. Is there a motion? Director Weicher? Too late Allan. Director Weicher has moved adoption of the staff recommendations regarding, actually, it's a resolution, I guess, regarding the 2003 designation of Federal Home Loan Bank directorships. Is there any discussion of the motion? Any discussion of the motion? Director Mendelowitz?

DIRECTOR MENDELOWITZ: Mr. Chairman, last October at a meeting, we discussed this issue. I raised some issues regarding the designation of Home Loan Bank directors. One issue that I raised up was the appropriate size of the Board

of Directors for the Home Loan Bank. During that meeting, we asked the staff to look at the issue during the horizontal review of corporate governance. That review isn't yet totally complete and, therefore, we haven't benefitted in this review numbers of discretionary seats from that review. But I'm hopeful that the review will be completed soon and I look forward to hearing the staff's views on this matter so we can incorporate their recommendations for next year's allocations.

CHAIRMAN KORSMO: I appreciate your comment in that regard. Maybe I could call either on Arnie Intrater or Steve Cross just to comment on it as to where we are in this process and give the directors some sense of when we can expect the results of the review.

DR. CROSS: The report--the reviews have been completed; the report should be issued no later than the end of this month. And the issue that you raised during the course of the October deliberations is addressed in the report without a firm recommendation, but identifying facts and circumstances out of the review that may pertain to some of the points that you and others raised during that meeting.

DIRECTOR MENDELOWITZ: Appreciate the update.

CHAIRMAN KORSMO: Thank you, Dr. Cross. Is there any other discussion of the motion? Any other discussion of the motion? Seeing none, the Secretary will please call the roll on the adoption of the Resolution Designating Federal Home Loan Directorships for 2003, Mary.

MS. GOTTLIEB: On the approval of the Resolution Regarding the Designation of Home Loan Bank Directorships for 2003, Director Leichter, how do you vote?

DIRECTOR LEICHTER: Yes.

MS. GOTTLIEB: Director O'Neill?

DIRECTOR O'NEILL: Aye.

MS. GOTTLIEB: Director Mendelowitz?

DIRECTOR MENDELOWITZ: Yes.

MS. GOTTLIEB: Director Weicher?

DIRECTOR WEICHER: Aye.

MS. GOTTLIEB: Chairman Korsmo?

CHAIRMAN KORSMO: Yes, the motion is adopted and the resolution is adopted designating seats. My assumption is now we notify the banks. Arnie, is that the process as to the appropriate number and they would proceed with their elections?

Before we close today, because I had raised expectations to some level on the one particular issue, just let me give everyone a very quick update on where we stand with the so-called modern membership issue. I will remind everyone, that late last year after the Board received the Morrison & Foerster opinion, banks were invited to submit a second round of comments on the modern membership question. At that time, I announced a goal of bringing a recommendation on this long studied issue to my colleagues in June. We've obviously missed that target due to the complexity of the numerous issues involved and the many different views we've taken into account in considering how to proceed. Everyone acknowledges that today's world of financial services is organized on a fundamentally different basis than the one Congress responded to 70 years ago when it created the Federal Home Loan Banks. The question still remains, however: How should the banks, their member institutions and their regulator, the Federal Housing Finance Board react to this changing world? How should we react to a changing industry reality?

Well, so, too, we should also ask the ques--answer the question, or ask the question, at least, whether

institutions should be able to access Federal Home Loan Bank services everywhere they do business? And also, the question of whether the bank should be able to compete for the business of all institutions that actually finance housing in their regions. I was interested the other day, to learn that the four largest mortgage lenders in the Dallas district, none of them are members of the Dallas bank; it's Wells Fargo and the three regional banks all headquartered in Alabama that, by virtue of that, are members of the Atlanta Bank.

As we've said many times, it's probably time to begin to answer these questions one way or another. Accordingly, I've asked the Office of Supervision and the Office of General Counsel to provide the Board with a proposed regulation for our consideration at our next meeting. The process I envision will ensure that the public, the banks, and the members have full opportunities for notice and comment on any proposal. And let me emphasize this, any regulation will be designed to respect the strength of the regional and cooperative nature of the Federal Home Loan Banks and will be designed to enhance the safety and soundness and business viability of each bank.

Let me also assure my colleagues that we intend to, while I want to bring something to our next Board meeting, we intend to move this process very deliberately by making sure that each of you is intricately involved in the process of developing any proposal. I know this is an issue that raises a lot of emotion, both pro and con. It's one that's complicated by the fact that there doesn't seem to be any obvious methodology for responding to it. And there doesn't seem to be any particular consensus among the 12 banks on not only on how to proceed, but, indeed, on the question of whether to proceed.

Because, however, we had requested, you will recall, a year and a half ago that the four banks who were petitioning the Board for relief on this issue, because we asked them to defer and allow us to proceed in some well-organized and deliberate process, I feel it incumbent upon us to engage in that process. And now is probably the time to do so.

So I did want to at least acknowledge that this issue is on the table because, as I mentioned, I had said at any number of forums that we would be addressing it sometime this year. Again, let me assure my colleagues that, as the

Office of Supervision and the Office of General Counsel move forward, we will keep you apprised of the direction we're moving. I would like to be able to give you some indication of what that direction is but, frankly, I don't know what it is at this point. So that's my announcement.

Are there any other comments, any other business, anything else to bring before--

DIRECTOR LEICHTER: Yes, Mr. Chairman. I'm pleased that in your comments on what we used to call multidistrict now called modernization maybe there'll be another name along the way--

CHAIRMAN KORSMO: The Leichter Plan is what I'm anticipating.

DIRECTOR LEICHTER: Well, I doubt that you're going to see a Leichter Plan, but I'd be certainly happy to participate and in making my recommendation, as I have to you and others, in informal discussions we've had as we've explored the issue. But what I think is important in what you said is that we have a very deliberative process here. It isn't just that this reason raises emotion, this issue raises some extremely complex, difficult issues, including some very tough legal issues that we all need to address

together. So I just want to urge that any recommendation that the staff puts forth in a proposed rule that we have at least two weeks prior to a Board meeting so that we have sufficient time to look at it, understand it, discuss it with the staff, discuss among the various directors and then leading to a Board meeting where there could be a full discussion.

CHAIRMAN KORSMO: I appreciate that, Director Leichter, that's why we did this with the AMA regulation, as well, trying to have a longer period in anticipation of responses from individual directors before we had to deal with it on a formal basis in an open meeting. We will do the same with this process. I anticipate we will also do the same with the activity reg because I know that is of particular interest to several of you and, indeed, to me. So I appreciate your comments, Director Leichter. Any other comments?

DIRECTOR MENDELOWITZ: Mr. Chairman, I was just mulling over Commissioner Weicher's observations about appropriate comment periods.

CHAIRMAN KORSMO: Right.

DIRECTOR MENDELOWITZ: Given we don't know what this is going to be, but we know that no matter what it is- it's going to be--

CHAIRMAN KORSMO: Make somebody unhappy.

DIRECTOR MENDELOWITZ: Yeah, it is going to be, I think, no matter what we come forward with, it's going to be controversial in terms of legal issues; it's going to be controversial in terms of structure and the future of the system. And I think it probably is something that justifies a 90-day comment period, given the significance of it. And I'd like to suggest that we agree on that now.

CHAIRMAN KORSMO: Why don't we keep our powder dry until we see how the process is going. Obviously, that will be part of the discussion in adopting any proposal, but I appreciate your comment on that regard and we'll certainly take that into consideration when the proposal's being adopted.

Any other comments? Any other discussion, questions, comments, criticisms? Hearing none, thank you, this was a good meeting and record time for this long of an agenda for us. This meeting is adjourned. Thank you very much.

[Whereupon, at 10:54 a.m., the meeting was  
adjourned.]