presented for evidentiary purposes (see 28 U.S.C. 1733).

§ 1707.209 Procedure when a decision is not made prior to the time a response is required.

If a response to a demand or request is required before the General Counsel can make the determination referred to in § 1707.201, the General Counsel, when necessary, will provide the court or other competent authority with a copy of this part, inform the court or other competent authority that the demand or request is being reviewed, and seek a stay of the demand or request pending a final determination.

§ 1707.210 Procedure in the event of an adverse ruling.

If the court or other competent authority fails to stay the demand, the employee upon whom the demand is made, unless otherwise advised by the General Counsel, will appear at the stated time and place, produce a copy of this part, state that the employee has been advised by counsel not to provide the requested testimony or produce documents, and respectfully decline to comply with the demand, citing *United States ex rel. Touhy* v. *Ragen,* 340 U.S. 462 (1951). A written response may be offered to a request, or to a demand, if permitted by the court or other competent authority.

Subpart C—Schedule of Fees

§ 1707.301 Fees.

(a) Generally. The General Counsel may condition the production of records or appearance for testimony upon advance payment of a reasonable estimate of the costs to DNFSB.

(b) Fees for records. Fees for producing records will include fees for searching, reviewing, and duplicating records, costs of attorney time spent in reviewing the demand or request, and expenses generated by materials and equipment used to search for, produce, and copy the responsive information. Costs for employee time will be calculated on the basis of the hourly pay of the employee (including all pay, allowance, and benefits). Fees for duplication will be the same as those charged by DNFSB in its Freedom of Information Act fee regulations at 10 CFR part 1703.

(c) Witness fees. Fees for attendance by a witness will include fees, expenses, and allowances prescribed by the court's rules. If no such fees are prescribed, witness fees will be determined based upon the rule of the Federal district court closest to the location where the witness will appear. Such fees will include cost of time spent by the witness to prepare for testimony, in travel, and for attendance in the legal proceeding.

(d) Payment of fees. You must pay witness fees for current DNFSB employees and any records certification fees by submitting to the General Counsel a check or money order for the appropriate amount made payable to the Treasury of the United States. In the case of testimony by former DNFSB employees, you must pay applicable fees directly to the former employee in accordance with 28 U.S.C. 1821 or other applicable statutes.

(e) Certification (authentication) of copies of records. The Defense Nuclear Facilities Safety Board may certify that records are true copies in order to facilitate their use as evidence. If you seek certification, you must request certified copies from DNFSB at least 45 days before the date they will be needed. The request should be sent to the General Counsel. You will be charged a certification fee of $15.00 for each document certified.

(f) Waiver or reduction of fees. The General Counsel, in his or her sole discretion, may, upon a showing of reasonable cause, waive or reduce any fees in connection with the testimony, production, or certification of records.

(g) De minimis fees. Fees will not be assessed if the total charge would be $10.00 or less.

Subpart D—Penalties

§ 1707.401 Penalties.

(a) An employee who discloses official records or information or gives testimony relating to official information, except as expressly authorized by DNFSB or as ordered by a Federal court after DNFSB has had the opportunity to be heard, may face the penalties provided in 18 U.S.C. 641 and other applicable laws. Additionally, former DNFSB employees are subject to the restrictions and penalties of 18 U.S.C. 207 and 216.

(b) A current DNFSB employee who testifies or produces official records and information in violation of this part shall be subject to disciplinary action.

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FEDERAL HOUSING FINANCE BOARD

12 CFR Parts 930 and 932

[No. 2001–28]

RIN 3069–AB11

Unsecured Credit Limits for Federal Home Loan Banks

AGENCY: Federal Housing Finance Board.

ACTION: Final rule.

SUMMARY: The Federal Housing Finance Board (Finance Board) is amending the unsecured credit provision of its rules, which was adopted as part of its capital rule on December 20, 2000 and governs the amount of unsecured credit that a Federal Home Loan Bank (Bank) can extend to a particular counterparty. The unsecured credit limits adopted in December were generally stricter than the limits under which the Banks operated with the Finance Board's Financial Management Policy (FMP). The amendments adopted herein will require the Banks to base the credit limit on the long-term credit rating of the counterparty. They also will set the amount of unsecured credit that a Bank can extend to a government-sponsored enterprise (GSE) at the level allowed under the FMP, and adjust the limits for sales of overnight federal funds and the limits for unsecured credit that can be extended to groups of affiliated counterparties. The amendments also address how the unsecured credit limits should be applied to certain housing finance agency bonds, and clarify how a Bank should calculate its credit exposures from on- and off-balance sheet items and derivative contracts. The Finance Board also is adding to § 932.9 a requirement that a Bank report promptly non-compliance with the unsecured credit limits set forth in the rule as well as making other technical or clarifying changes to the rule.

EFFECTIVE DATE: The final rule is effective on March 27, 2002.

FOR FURTHER INFORMATION CONTACT: James L. Bothwell, Managing Director, (202) 408–2821; Scott L. Smith, Acting Director, (202) 408–2991; or Julie Paller, Senior Financial Analyst, (202) 408–2842, Office of Policy, Research and Analysis; or Thomas E. Joseph, Senior Attorney-Advisor, (202) 408–2512, Office of General Counsel, Federal Housing Finance Board, 1777 F Street, NW., Washington, DC 20006.

SUPPLEMENTARY INFORMATION:

I. Introduction

On December 20, 2000, in accordance with the Gramm-Leach-Bliley Act, Pub.

L. No. 106–102, 133 Stat. 1338 (November 12, 1999) (GLB Act), the Finance Board adopted a final rule to implement the new capital structure that the GLB Act established for the Banks. 66 FR 8262 (January 30, 2001). As part of the final capital rule, the Finance Board adopted § 932.9 of its rules, 12 CFR 932.9, which set new limits on a Bank's unsecured credit exposures to a single counterparty or a group of affiliated counterparties. *Id.* at 8318–19. These new limits represented a revision and codification of the unsecured credit guidelines of section VI of the FMP, Finance Board Res. No. 96–45 (July 3, 1996), as amended by Finance Board Res. No. 96–90 (December 6, 1996), Finance Board Res. No. 97–05 (January 14, 1997), and Finance Board Res. No. 97–86 (December 17, 1997). Given concerns raised by the Banks about the unsecured limits adopted in December 2000, the Finance Board delayed the effective date of these requirements on the condition that the FMP restrictions remained in effect, and, on March 7, 2001, published a proposed rule requesting comment on potential amendments to the unsecured credit requirements. *See* 66 FR 13688 (Mar. 7, 2001).

After considering comments on this rule proposal, the Finance Board believed more changes were needed than those it had previously considered and, as a consequence, published for comment in the **Federal Register** a new set of proposed amendments to § 932.9 on August 8, 2001 (the proposed rule). *See* 66 FR 41474 (Aug. 8, 2001). The Finance Board also again extended the effective date for compliance with § 932.9 subject to the condition that section VI of the FMP remained in effect. *Id.* at 41475. The comment period on the second proposed rule closed on September 7, 2001. After considering the comments received, the Finance Board has made a number of changes to the rule proposed in August 2001, and is adopting an amended version of § 932.9, as discussed below.

II. Discussion of the Comments Received

The Finance Board received seven comment letters on the proposed rule, all of which were from Banks. Two commenters submitted follow-up comment letters to the Finance Board, after the close of the comment period. Nevertheless, these follow-up letters were considered in developing this rule. The comments requested both changes to the proposed rule and amendments and clarifications of how the proposed rule would be applied. The Finance Board agrees with many of the comments made, and as a result has made a number of changes to the proposed rule. The Finance Board addresses the comments received on its proposed changes to § 932.9 below.

Effective Date of Rule

Four of the commenters requested that the Finance Board delay the effective date of § 932.9, which had been scheduled to take effect on October 1, 2001 or on the date the proposed rule was adopted in final form, whichever was earlier. *See* Fin. Brd. Res. No. 2001–11 (June 5, 2001). The commenters suggested that the effective date of the rule be set at various dates that ranged from three to six months after a final rule had been published. The commenters stated that the extension was necessary to give the Banks sufficient time to conform recordkeeping and reporting systems to whatever limits were ultimately adopted by the Finance Board.

The Finance Board generally agrees with these comments. On September 26, 2001, it extended the effective date of § 932.9 until January 28, 2002 to provide sufficient time to complete the rulemaking process. *See* Fin. Brd. Res. No. 2001–20 (Sept. 26, 2001). However, given the date of approval of these final rule amendments, the Banks will have less than ninety days to prepare for implementing the amended version of § 932.9 adopted herein if the January 28, 2002 date for complying with § 932.9 is not changed.[1] Thus, the Finance Board is also adopting separate from these rule amendments, a resolution that delays the date for complying with § 932.9 until the effective date of these final rule amendments. This new effective date will be 90 days from the date this final rule is published in the **Federal Register**.[2] The delay in the effective date is conditioned upon the Banks' continued compliance with the unsecured credit limits in section VI of the FMP. The Finance Board believes that this time frame should be sufficient for the Banks to conform their recordkeeping and reporting systems to the rule as amended.

[1] Further, the Finance Board recognizes that given the large number of amendments adopted by this rulemaking, it would serve no purpose to require the Banks to implement § 932.9, as adopted in December 2000, on January 28, 2002, and then implement this amended version of the rule soon thereafter. It is more reasonable to continue to apply the current unsecured credit restrictions of section VI of the FMP to the Banks until section VI of the FMP is superceded by the amended version § 932.9.

[2] The Finance Board is also extending the effective date for the liquidity requirements set forth in § 932.8 so that both the amended unsecured credit limits and the new liquidity requirements will take effect on the same day.

General Approach

The proposed rule would have required a Bank to determine the applicable maximum capital exposure limits for a particular counterparty based on the long-term credit rating received by that counterparty from an organization regarded as a Nationally Recognized Statistical Rating Organization (NRSRO) by the Securities and Exchange Commission, except in certain limited circumstances. The proposed amendment represented a change from the approach adopted in December 2000 which required a Bank to determine the maximum capital exposure limit for a short-term credit based on an NRSRO's short-term credit rating for the counterparty and to determine the maximum capital exposure limit for a long-term credit based on an NRSRO's long-term credit rating for the counterparty. Under the proposed rule (as under the rule adopted in December 2000), the unsecured credit limit for a particular counterparty (subject to certain exceptions set forth in the rule) would equal the maximum capital exposure limit for that counterparty multiplied by the lesser of the Bank's total capital or the counterparty's Tier 1 or total capital.

Two commenters objected to the reliance on long-term credit ratings, as proposed. The commenters argued that short-term credit exposures presented a markedly different credit risk to a Bank than would a long-term exposure to the same counterparty, and that by disregarding short-term ratings, the Finance Board was ignoring important information about a counterparty embodied in that rating. The commenters also believed that the proposed approach would greatly restrict the amount of unsecured credit a Bank could provide from levels permitted under the FMP or under § 932.9 as adopted in December 2000. One commenter stated that this reduction would force the Banks to seek lower-rated counterparties and increase the term of their lending, thereby raising overall credit risk. The other commenter stated the proposed change, if adopted, would reduce the amount of unsecured credit that a Bank would have available to its members, which may result in membership becoming less attractive to some institutions.

Given these concerns, one commenter urged the Finance Board not to adopt the proposed change and continue to base unsecured credit limits for short-term exposures on short-term credit ratings. The other commenter suggested the Finance Board provide the Banks the option of using short-term credit ratings. The second commenter also urged the Finance Board to develop new short- and long-term limits and a new total limit which would be the sum of the short- and long-term limits plus capacity for additional overnight lending.

A third commenter believed that it was inappropriate to use the counterparty's capital as a basis for setting the unsecured credit limits because this approach could result in unduly large Bank System-wide unsecured credit exposures to a counterparty in relation to that counterparty's total assets. The commenter urged the Finance Board to set the unsecured credit limits at the lesser of a percentage of a Bank's total capital or a counterparty's total assets.

The Finance Board has considered these comments but has decided not to make any changes to the proposed rule in response. In the SUPPLEMENTARY INFORMATION section of the **Federal Register** proposing release for this rule, the Finance Board noted three reasons to require the Banks to determine the applicable maximum capital exposure limit based solely a counterparty's long-term credit rating. First, the Finance Board stated that the reliance on long-term credit ratings was consistent with the approach being suggested by the Basel Committee on Banking Supervision (Basel Committee) for establishing risk-weightings under its standardized approach in the proposed New Capital Accord, which generally proposes using long-term ratings assigned by rating agencies (*i.e.,* NRSROs) and disregarding the maturity of a credit in setting risk weightings. *See* 66 FR at 41479–80 (*citing* Basel Committee, ''A New Capital Adequacy Framework'' 26–36 (June 1999); and Basel Committee, ''Overview of the New Basel Accord'' 13–14 (Jan. 2000)).[3] Second, the Finance Board noted that parties that would be assigned the same short-term credit rating may have markedly different maximum 30-day default rates, depending on a party's long-term credit rating, so that use of long-term ratings would assure more restrictive limits were imposed on borrowers with the higher maximum 30-day default rate. 66 FR at 41480. Finally, the Finance Board stated that exclusive reliance on long-term credit ratings for determining the maximum exposure limits would simplify the Banks' monitoring of their counterparties' ratings. *Id.*

The comments received do not alter the Finance Board's basic reasoning for proposing exclusive use of long-term credit ratings to determine the maximum capital exposure limit applicable to a counterparty. In this regard, the Finance Board emphasizes that its approach is consistent with the standardized approach being proposed by the Basel Committee in the New Capital Accord for establishing risk weightings. The Basel Committee decided generally to ignore maturity of claims in establishing risk weighting in large part because of ''the difficulties in pursuing greater precision in differentiating among the maturities of claims through capital charges'' and the ''broad brush'' nature of the proposed capital requirements. *See* Basel Committee, ''A New Capital Adequacy Framework'' at 33. The same reasoning can be applied to the unsecured credit limits being adopted herein, especially given that the credit limits are designed to provide a broad framework to prevent concentration of credit in single counterparties or groups of affiliated counterparties and not to differentiate with precision the risks of lending to particular counterparties. *See* 66 FR at 8302 (explaining reasoning for adopting § 932.9).

The Finance Board also disagrees with the suggestions of the one commenter that the unsecured credit limits will create more risk by lowering the quality of the Bank's credit portfolios. The unsecured credit limits adopted herein are themselves restrictive as to the amounts of credit that can be lent to lower rated counterparties. At the same time, before undertaking any significant lending or investment activity that was not allowed under the FMP, a Bank will first have to demonstrate pursuant to part 980 of the Finance Board rules, 12 CFR part 980, that it is able to undertake the new lending in a safe and sound manner. In addition, the lending undertaken by a Bank will eventually be subject to the capital requirements of part 932 of the Finance Board rules, helping to assure a Bank holds sufficient capital if it is indeed engaging in lending to lower quality counterparties. Even before the requirements of part 932 become effective, however, a Bank will be subject to the capital requirements set forth in § 956.4 of the Finance Board rules, 12 CFR 956.4, if the Bank undertakes unsecured transactions with any counterparty rated below the second highest credit rating by an NRSRO. Further, with regard to the second commenter's concern about unsecured lending to members, the unsecured credit rules will not in any way limit a Bank's ability to continue to provide liquidity to members using short-term advances.

The Finance Board also continues to believe that it is appropriate to base the unsecured credit limits on the lesser of the capital of the Bank or the capital of the counterparty rather than adopt the commenter's suggestion of using a percentage of a counterparty's assets. The approach adopted herein addresses the Finance Board's concerns with potential concentrations of unsecured credit as a percentage of Bank capital on both the individual Bank and Bank System level. *See* 66 FR at 8302. The approach also is relatively straightforward to implement so the Finance Board sees no reason to alter it in response to the commenter's concerns.

Further, basing the limit on a percentage of counterparty assets rather than counterparty capital would result in higher limits as a percentage of counterparty capital for counterparties with lower capital ratios. For example, two counterparties with the same credit rating and same amount of total assets would be subject to the same limit. If one of the two has a lower capital ratio than the other, however, the Bank's lending to the less capitalized counterparty could equal a higher percentage of that counterparty's capital (*i.e.,* the limit as a percentage of capital would be higher). Because capital serves as a cushion against loss, this methodology suggested by the commenter would allow the Bank a higher exposure relative to capital to the less-capitalized counterparty and provide less protection against potential losses. Thus, the Finance Board believes that limiting extensions of unsecured credit to a percent of capital is the more appropriate methodology.

Overnight Federal Funds Transactions

The proposed rule would have amended § 932.9 to require a Bank to meet two unsecured credit limits for each private counterparty. The first, the term limit, would have applied to all unsecured credit transactions except sales of federal funds with a maturity of one day or less or sales of federal funds subject to a continuing contract (together ''overnight federal funds''). The term limit for a particular counterparty equaled the maximum capital exposure limit times the lesser of the Bank's total capital or the appropriate measure of the counterparty's capital. The second limit, the overall limit, would have applied to all transactions with a particular

[3] *See also,* Basel Committee, ''Consultative Document: The new Basel Capital Accord'' 14–15 (Jan. 2001) (''if there is a long-term issue or issuer assessment [*i.e.,* rating], that assessment should be used not only for long-term claims but also for short-term claims, regardless of the availability of a short-term assessment * * *).

counterparty including any overnight federal funds transactions. The overall limit for a particular counterparty equaled twice the counterparty's term limit.

The Finance Board received two comments on this proposed amendment. One commenter felt that the special treatment afforded overnight Federal Funds transactions by the proposed amendment offered only limited relief to, what the commenter believed were, the unnecessarily restrictive limits of § 932.9. This commenter urged the Finance Board to exclude all overnight federal funds transactions from the unsecured credit limits, or in the alternative, to allow a flat 15 percent of capital add-on to the term limit for overnight federal funds transactions for counterparties with the highest short-term rating and at least the third highest long-term rating. The commenter argued that the ''funding advantage'' that may be enjoyed by the Banks, which the commenters viewed as the reason the Finance Board failed to exclude all overnight federal funds transactions from the rule, was a myth, noting that if such an advantage existed, depository institutions would get most of their funds from the Banks. The commenter also pointed out that given the low spread on advances, the Banks needed to maintain leverage through short-term investments such as selling overnight federal funds. More generally, the commenter believed that the Finance Board's ''conservative'' approach to the unsecured credit limits was inconsistent with the GLB Act because the GLB Act made clear that the Finance Board's responsibility was safety and soundness regulation and not management of the Banks. The other commenter on the proposed amendment recommended that the Finance Board apply the proposed special limits only to overnight investment transactions between a Bank and a member institution, and that the Finance Board include in the overall limit all types of unsecured overnight transactions, not just overnight federal funds transactions.

As the Finance Board has previously stated, it adopted the unsecured credit limits as a safety and soundness regulation to prevent undue concentrations of credit in a single counterparty or groups of affiliated counterparties. *See* 66 FR at 8301–02. Other banking regulators have similar limits in effect.[4] These types of regulations also are consistent with practices for sound management of credit risk as articulated by the Basel Committee. *See* Basel Committee, ''Principles for Management of Credit Risk'' 10 (Sept. 2000). Thus, the Finance Board is confident that these regulations are consistent with its obligations and authority to ensure that the Banks operate in a financially safe and sound manner, and are not inconsistent with the GLB Act or the Bank Act more generally. *See* 12 U.S.C. 1422a(a)3 and 1422b.

Further, as noted in the **SUPPLEMENTARY INFORMATION** section of the preamble of the proposed rule, the Finance Board considered excluding overnight federal funds transactions from its unsecured credit limits because other banking regulators excluded these transactions from their lending limits. *See* 66 FR at 41476. The Finance Board also noted that the Banks have different incentives than commercial depository institutions to lend into the federal funds markets. The differing incentives include both the funding advantage enjoyed by GSEs in borrowing and the more varied lending and investment opportunities available to commercial banking enterprises which reduces these institutions' incentives to engage in federal funds lending. *Id.* The Finance Board also emphasized that overnight federal funds transactions are currently subject to the unsecured credit limits of the FMP and that completely excluding overnight federal funds transactions from the restrictions of § 932.9 would have represented a significant loosening of its restrictions, which was not the purpose of adopting these limits. Given these considerations, the Finance Board concluded that it was not appropriate to completely exclude overnight federal funds transactions from the unsecured credit limits, and instead, proposed the overall limit discussed above.

The Finance Board continues to believe that its initial reasoning remains sound. In particular, the Finance Board believes there is a basis for concluding that Banks have a financial incentive to lend to the federal funds markets, and that to permit such lending without limits would be imprudent. The Finance Board also believes that the rule as adopted provides the Banks with sufficient flexibility to invest funds to both meet their liquidity needs and to counter cyclical fluctuations in their business. Based on the same reasoning discussed above, the Finance Board also sees no compelling reasons to extend the treatment offered to overnight federal funds transactions to other types of overnight transactions in which a Bank may engage or to limit the additional lending capacity for overnight federal funds transactions just to transactions with members. Such restrictions would unnecessarily limit a Bank's investment opportunities with little apparent gain from a safety and soundness perspective. Moreover, nothing would prevent a Bank from implementing internal policies that would achieve this goal so long as the policies were consistent with § 932.9 and other Finance Board regulations.

Affiliated Counterparties

In response to concerns that the unsecured credit limits were too restrictive, the Finance Board proposed to amend § 932.9 so that the unsecured credit limit applicable to groups of affiliated counterparties would equal 30 percent of the Banks total capital. 66 FR at 41482. The Finance Board explained that the proposed aggregate limit on extensions of unsecured credit to affiliated counterparties would have allowed the Banks to extend somewhat larger amounts of credit to large financial conglomerates than did the provisions in § 932.9 as adopted in December 2000. *Id.* at 41480.

The Finance Board also proposed amending the definition of ''affiliated counterparty.'' *Id.* at 41481. The Finance Board believed that new definition was more understandable and was more consistent with the meaning of the phrase ''corporate group'' as used in regulations issued by the Office of the Comptroller of the Currency (OCC), which addressed lending to affiliated counterparties. *Id.* at 41480. The effects of the proposed definition would have generally been to raise the threshold for control when defining an affiliate from (either direct or indirect) ownership of 25 percent of the voting securities or interests of an entity to 50 percent of such securities or interests. The Finance Board did not believe the change would generally alter the number or groupings of affiliated counterparties covered by the restrictions in § 932.9. *Id.*

The Finance Board received only one comment on the proposed changes to the unsecured credit limits applicable to extensions to a Bank's unsecured lending to groups of affiliated counterparties. The commenter urged the Finance Board to raise the limit from 30 percent of a Bank's total capital to 50 percent of a Bank's total capital because, as the commenter believed, there was only an indirect link between affiliates related by a common holding company and failure of one affiliate would seldom cause another affiliate to fail. The commenter also recommended that counterparties related by a common holding company and special bankruptcy-remote subsidiaries should

[4] The Office of the Comptroller of the Currency sets forth its lending limits at 12 CFR part 32.

not be considered affiliates for purposes of § 932.9.

The Finance Board considered this comment but has not altered the proposed unsecured lending limits for groups of affiliated counterparties or the proposed definition of affiliated counterparty as a result. The Finance Board disagrees with the commenter's suggestion that there is only minimal risk that the failure of one affiliated counterparty would affect the financial standing of other affiliates. As the Finance Board previously pointed out, applying credit exposure limits to groups of affiliated counterparties is consistent with sound principles of risk management and with practices of other regulators. *See* 66 FR at 41477. The Finance Board believes that the new limit suggested by the commenter would be too lenient and allow Banks too great an exposure to groups of affiliated counterparties. The limit adopted herein on extensions of credit to groups of affiliated counterparties, however, is consistent with limits adopted by other bank regulators.[5] *See* 12 CFR 932.5(d) and 12 CFR 560.93(c). As already stated, the Finance Board also believes that the definition of ''affiliated counterparty,'' as proposed and as adopted herein, is consistent with similar terms used by other banking regulators.

GSE Limits

The Finance Board proposed raising the limit on extensions of unsecured credit to a GSE to 100 percent of the lesser of a Bank's or GSE's total capital. *Id.* at 41482. This change basically would have re-instituted the limit on extensions of unsecured credit to GSEs that had been in effect under the FMP.[6] *Id.* at 41475–76. As the Finance Board explained, the proposal resulted from Banks' concerns that the limits as adopted in December 2000 may have disrupted the Banks' investment strategies. At the same time, the Finance Board did not believe the proposal raised any safety and soundness concerns. *Id.* The proposed amendment also would have required a Bank to treat a GSE like other private counterparties should any NRSRO have assigned a credit rating to, or downgraded a credit rating of, any long-term senior unsecured credit obligation issued by a GSE to below the highest investment grade or placed a GSE on a credit watch for such a downgrade. *Id.* at 41482. This trigger provision was proposed to assure the preferential GSE limit was not applied to an entity undergoing obvious financial difficulty. *Id.* at 41475.

The Finance Board received two comments on this proposed rule. The first commenter believed the trigger provision would have resulted in too drastic a cut in future credit to a troubled GSE and recommended that the deadline for applying the lower limits applied to a GSE after a downgrade in its credit rating be keyed to the extent of the downgrade (*e.g.,* six months if downgraded to the second highest investment grade credit rating, three months if downgraded to the third highest investment grade credit rating, etc.). The commenter argued that reducing future extensions of credit to a GSE in times of financial difficulty could increase the risk of default by that entity. The second commenter requested that the Finance Board clarify that the preferential unsecured lending limit for GSEs would not be applied to subordinated debt issued by the GSE.

The Finance Board does not believe that any change in the proposed trigger provision is necessary in response to the comment and is adopting it as proposed. The commenter's suggestion, if adopted, could leave the Banks with the risk of maintaining the liquidity of other GSEs in the unlikely occurrence that another GSE experienced severe financial difficulties. More importantly, to the extent that special action were needed to help a GSE, or any other large financial institution, such action would have to be coordinated with other financial regulators, and the Finance Board would have to take appropriate action at that time (*e.g.,* waiver of the trigger provision) to allow the Banks to adjust their lending positions accordingly. At the same time, the Finance Board would expect that a Bank would take steps to reduce its exposure to a GSE (or any other counterparty) as soon as the GSE's potential financial difficulties became apparent. Thus, the reduction in extensions of unsecured credit may be spread over time, and the reduction in unsecured credit triggered when the credit rating downgrade actually occurs may not be as drastic as the commenter suggested.

The Finance Board agrees with the second commenter, however, and has altered the final rule to make clear that the special unsecured credit limits applicable to GSEs do not apply to subordinated debt. GSE subordinated debt is generally perceived as providing an indication of the entity's financial standing, independent of any implied government guarantee. As such, the risk of holding GSE subordinated debt would be similar to the risks associated with holding non-GSE debt. The amendments to § 932.9 adopted by the Finance Board will restrict a Bank's holding of GSE debt to the level calculated using the maximum capital exposure limit associated with the credit rating assigned to the GSE's subordinated debt. This rule would apply even if the GSE's subordinated debt received the highest investment grade rating from an NRSRO. Further, a Bank's holdings of a GSE's subordinated debt would be included in the total amount of unsecured credit extended to that GSE for purposes of applying the preferential lending limit for GSEs (*i.e.,* 100 percent of the lesser of the Bank's or the GSE's total capital).

The Finance Board also recognizes that the commenter's concerns with regard to GSE subordinated debt would also apply to the subordinated debt of any other counterparty. Thus, the Finance Board is also adopting new § 932.9(a)(4)(iii) as part of these final rule amendments. This provision imposes a special sub-limit on any debt issued by a counterparty if that debt obligation received an issue rating from an NRSRO that is lower than the counterparty's long-term credit rating. This sub-limit would be calculated using the rating assigned to the lower-rated debt obligation for purposes of determining the maximum capital exposure limit. Because the lower credit rating assigned to a particular obligation would indicate that holding that obligation is more risky than holding other obligations of the issuer-counterparty, it is appropriate to limit the Bank's holdings of that specific obligation. Generally, the Finance Board believes that an issue rating will be lower than the issuer's long-term rating only in cases where the issue in question is subordinated debt.

Measurement of Derivatives Exposure

The Finance Board proposed amending § 932.9 to require a Bank to measure the unsecured credit exposure arising from a derivative contract in accordance with §§ 932.4(g) and 932.4(h) of the Finance Board rules. 12 CFR 932.4(g) and 932.4(h). As adopted in December 2000, § 932.9 contained no provision indicating how a Bank should measure its unsecured credit exposure to a counterparty, and this change would have conformed the

[5] The cited regulations generally restrict an institution's aggregate extension of credit, including any lending that is fully secured by readily marketable financial instruments or bullion in which the lender holds a perfected security interest, to a corporate group to an amount not to exceed 50 percent of a bank's capital and surplus. The Finance Board's limit, though lower, would not apply to extensions of credit which are backed by collateral held by a Bank in accordance with the requirements of § 932.9.

[6] Mortgage-backed securities issued by other federal housing GSEs and purchased by the Banks were previously, and are not now, considered a form of unsecured credit by the Finance Board.

measurement for derivative contracts with that undertaken when calculating a Bank's credit risk capital charges for derivative contracts under § 932.4 of the Finance Board rules.

Four commenters pointed out that when read strictly this provision as proposed would not take account of collateral held against derivative exposure. These commenters pointed out that the proper measure of the unsecured credit exposure from a derivative contract should be the net marked-to-market value of the contract less the collateral posted by the counterparty. Two of these commenters also specifically stated that it was inappropriate to include the potential future credit exposure (PFE) of a contract in the calculation of the Bank's extension of unsecured credit to a counterparty. The two commenters pointed out that the exposure of a Bank upon default of a counterparty would be the marked-to-market value of the contract at the time of default. Further, these commenters stated risk management techniques, such as the right to value derivatives and call for additional collateral at any time, mitigate the need to include PFE in exposure calculations. One of these two commenters also requested that the Finance Board specify the frequency with which a Bank must measure its credit exposure from a derivative contract and recommended a frequency of once a month, which would coincide with minimum requirements in agreements for measuring exposure and settling collateral.

The Finance Board did not intend that derivative exposure against which collateral is properly held be included in the amount of unsecured credit extended to a counterparty, but agrees that the proposed wording in § 932.9(f) did not make this clear. Thus, this provision, as adopted, has been reworded to make clear that any portion of a derivative exposure against which the Bank holds collateral shall not be counted toward the total amount of unsecured credit extended to a counterparty. To be counted, however, this collateral must be held in accordance with § 932.4(e)(2)(ii)(B) of the Finance Board's rules, which among other things requires the value of the collateral to be appropriately discounted to protect the Bank against a price decline during the holding period and to account for the potential cost of liquidation of the collateral.

The Finance Board, however, believes that it is appropriate to continue to include a derivative contract's PFE in the calculation of extension of unsecured credit. Such practice appears to be standard for derivative dealers when setting counterparty credit limits. *See e.g.,* Bank for International Settlements, ''OTC Derivatives: Settlement Procedures and Counterparty Risk Management'' 15–16 (Sept. 1998). The Finance Board believes that it is also appropriate here since the value of certain derivative contracts may be fast changing and the use of collateral may reduce losses but generally does not eliminate credit risk. *Id.* at 4. Thus, as adopted, § 932.9(f) requires a Bank to include both the current credit exposure and the PFE in its calculation of the amount of unsecured credit extended to a counterparty. This provision, both as proposed and as adopted, allows a Bank, however, to calculate its exposure on a net basis for derivative contracts subject to a qualifying bilateral netting contract, as that phrase is defined under § 932.4(h)(3).

The Finance Board has also decided not to place in the rule a minimum frequency for calculating exposures under a derivative contract. Instead, Banks should establish clear policies to govern such calculations, and these policies will be reviewed by the Finance Board in the course of Bank examinations. In setting this policy, a Bank should consider the complexity of its derivative holdings and the volatility of the value of those holdings as well as other relevant factors. The Finance Board generally believes, however, that a Bank should value its derivative contracts more frequently than once a month for purposes of applying § 932.9.

Requests for Additions to the Rule

Two commenters asked that the Finance Board add a provision to the rule to clarify the status of bonds issued by state and local housing finance agencies (HFAs). Both commenters pointed out that investment in HFA bonds helped Banks achieve their housing finance missions and provided Banks with investment flexibility and that treating HFAs like other counterparties severely restricts the Banks' investment in HFA bonds because HFAs often have low capital. These commenters also noted that HFA bonds were considered outside the scope of the unsecured credit limits of section VI of the FMP. As a follow up to its comment letter, one commenter sent an additional letter stating that they believe that most HFA bonds were secured by mortgage collateral and therefore should have been exempt from the unsecured credit limits, but provided no justification or legal rationale to support such a conclusion. Another commenter requested that the Finance Board add a provision that if a third-party guaranteed repayment by the counterparty, the unsecured credit limits should be applied to the guarantor and not to the counterparty itself, as has been required under the FMP.

The Finance Board has considered these comments and has made changes in the final rule as a result. With regard to the HFA obligations, the Finance Board believes that generally these obligations should be subject to the unsecured credit limitations. While the structure of the HFA obligations held by the Banks may vary widely, it does not appear that these obligations are usually secured in the sense that the HFA provides the Bank with collateral that the Bank holds in accordance with the principles set forth in § 932.4(e)(2)(ii)(B) or in the same sense that a Bank secures an advance. Nevertheless, given that the structure of these transactions may vary, the Finance Board is willing to consider on a case-by-case basis that a specific HFA transaction may be considered secured and therefore should be excluded from the limits of § 932.9.

The Finance Board agrees with the commenters, however, that application of the proposed limits in § 932.9 may restrict the Banks' ability to purchase the HFA obligation and be detrimental to the Banks' housing finance mission. Investments in HFA obligations are also subject to other Finance Board regulations. Thus, the Finance Board is adopting new § 932.9(a)(3) which sets a special limit for certain HFA obligations. As is explained more fully in the next section of this preamble, this special limit for qualified HFA obligations will be calculated based upon the Bank's total capital and the maximum capital exposure limit associated with the rating of the instrument purchased by the Bank. To qualify for treatment under § 932.9(a)(3), the HFA obligation must either be an acquired member asset, as defined in § 955.2 of the Finance Board rules, or be the type of obligation excluded by § 956.3(a)(4)(iii) from the general prohibition against the Banks' investing in whole mortgages or loans (or interests therein). The Finance Board believes that the approach adopted in these amendments will provide the Banks with sufficient capacity to invest in HFA obligations in support of their housing finance mission while still preventing undue concentrations of these instruments on the Banks' books.

More generally, the Finance Board recognizes that, given the comment concerning the status of HFA bonds, there may be some confusion concerning the intended scope of this rule. This is especially true where a bond or other debt securities may be backed by a pledge of specific property or by revenues, such as may occur with certain HFA bonds, so that the debt security may be considered secured in some context. In developing this rule, however, the Finance Board has viewed the purchase of a debt security or other debt obligation generally to be an unsecured extension of credit, unless the Bank, itself, holds or controls collateral against its exposure from the debt obligation, in accordance with the requirements of § 932.4(e)(2)(ii)(B). To make this view clear, the Finance Board has adopted new § 932.9(f)(2). New § 932.9(f) also makes clear that the Finance Board continues to exempt mortgage-backed securities from the unsecured credit limits and that loans purchased as acquired member assets (AMA) and identified in §§ 955.2(a)(1) and (2), 12 CFR 955.2(a)(1) and (2), are also exempt.

The AMA exemption under new § 932.9(f)(2) does not extend to HFA bonds purchased under the AMA. Generally, a member or housing associate does not need to provide added credit enhancements and collateralize that credit enhancement for HFA bonds as it would for mortgages purchased under the AMA program. *See* 12 CFR 955.3(b)(3). This is because the HFA bonds purchased under the AMA program are already enhanced by collateral (not held by the Bank) and rated sufficiently high that additional enhancement or collateral is not required. Further, the unsecured credit provision for HFA bonds already takes account of this higher rating by allowing the maximum capital exposure limits to be determined based on the issue rating of the HFA bond itself rather than on the rating of the HFA. The new provision also makes clear that the Finance Board is willing to consider on a case-by-case basis that any debt obligation or debt security purchased by the Bank should not be subject to the limits of § 932.9 because the Bank's credit exposure is adequately secured.

The Finance Board also agrees with the commenter that where a third-party has provided an unconditional and irrevocable guarantee covering a credit extended by the Bank, the Bank's exposure will ultimately be to the guarantor. Given this fact, the Finance Board has modified proposed § 932.9(a) to make clear that if repayment of a credit is guaranteed unconditionally and irrevocably by a third-party, the resulting unsecured credit exposure would be treated as if it were to the third-party guarantor. This means that in calculating the unsecured credit limits for these guaranteed transactions, a Bank would consider the credit rating and capital of the third-party guarantor and would aggregate the credit exposure arising from the guarantee with any other unsecured credit extended to the third-party guarantor. The Finance Board recognizes that for regulatory or other reasons, a third-party may not provide, or be able to provide, an irrevocable guarantee, but may provide some other form of support or credit enhancement. While the rule as adopted only allows unconditional, irrevocable guarantees to be attributed to the third-party guarantor, the Finance Board would be willing to consider allowing this treatment to be extended on a case-by-case basis to other specific support arrangements, if a Bank can demonstrate that the support or credit enhancement provided by the third-party provides a level of protection equivalent to an irrevocable guarantee.

Requests for Clarification

One commenter requested clarification as to whether the phrase ''affiliated counterparties' combined * * * capital'' as used in the reporting requirements of proposed § 932.9(e)(1)(ii) meant the consolidated capital of the affiliated group or the combined capital of only those affiliated counterparties' to which a Bank had actually extended credit. The Finance Board believes that the phrase ''affiliated counterparties' combined * * * capital'' should be interpreted to mean the consolidated capital of the holding company for the affiliated group. Use of this figure would help avoid double counting of capital of affiliated members of a group.

This commenter also requested clarification whether the Finance Board expected data as of the month-end or some other date under the ''monthly'' reporting that would be required under § 932.9(e). This requirement applies to extensions of credit outstanding at any time during the month, not just at month-end, although the Bank does not have to submit its report to the Finance Board until after the last business day of the month. Such report should be provided promptly after that date.

Another commenter asked for clarification of the meaning of the phrase ''net payments due a Bank'' as used in proposed § 932.9(f)(1), a provision which addresses the measurement of unsecured credit exposures from on-balance sheet transactions. The Finance Board notes that this phrase was used in section VI of the FMP, and the Finance Board intends that it has the same meaning as under the FMP. Thus, the phrase indicates an amount due to or accrued by the Bank as of a point in time (i.e., the time a Bank measures its exposure from the on-balance sheet transaction) and not the future amounts due over the life of the transaction.

Status of FMP Provisions

One commenter requested that the Finance Board specifically rescind in the final version of § 932.9 provisions in section VI of the FMP concerning maximum maturities for derivative contracts and contingent collateralization of interest rate exchange agreements. The Finance Board does not believe a specific provision needs to be added to § 932.9 as requested by the commenter. Upon the effective date of § 932.9, the unsecured credit limitations of section VI of the FMP will be superseded and replaced by the rule. Any provision of section VI of the FMP which has not been adopted as part of § 932.9, such as the two cited by the commenter, will no longer apply to the Banks.

Another commenter asked the Finance Board to clarify whether restrictions contained in certain parts of the FMP would still be applicable after the effective date of § 932.9. Specifically, the commenter requested clarification of the applicability of: footnote 1 which defines ''eligible financial institutions'' and effectively limits the counterparties to which a Bank may lend overnight and term funds; footnote 3 which sets forth qualifications for issuers of commercial paper, bank notes and thrift notes that a Bank may buy; and footnote 6 which sets forth the criteria for eligible non-member counterparties for hedging transactions. Footnotes 1 and 3 appear in section II.B of the FMP, and footnote 6 is found in section V of the FMP. The Finance Board believes that because these provisions restrict, based on credit ratings, the counterparties to which the Bank may extend credit or with which a Bank may transact business which would create a credit exposure, these restrictions should be superseded upon the effective date of § 932.9. Section 932.9 is intended to address concerns about the credit rating of the Banks' counterparties. It does so, however, by limiting the amount of credit a Bank can extend to parties rated at these various levels and not by restricting the counterparties with which the Bank can transact. The new business activity requirements of Part 980 of the Finance Board's rules would apply to any investments involving counterparties the Bank intends to transact with that were not permitted under the FMP. *See* 66 FR at 41477–78.

III. The Final Rule

Except as noted below, the Finance Board is adopting the amendments to § 930.1 and § 932.9 of its rules, generally as proposed. The notices of proposed rulemaking published in the **Federal Register** on March 7, 2001, 66 FR 13688, and August 8, 2001, 66 FR 41474, contain additional explanatory information about the changes being adopted herein, and interested parties should review these document for a more complete understanding of the rule provisions discussed below.

Definitions

The Finance Board is amending § 930.1 of its rules, as proposed, to change the definition for ''affiliated counterparty'' and to add a new definition for the phrase ''sales of federal funds subject to a continuing contract.'' The definition of ''affiliated counterparty'' being adopted herein reads as follows:

Affiliated counterparty means a counterparty of a Bank that controls, is controlled by or is under common control with another counterparty of the Bank. For the purposes of this definition only, direct or indirect ownership (including beneficial ownership) of more than 50 percent of the voting securities or voting interests of an entity constitutes control.

The amended definition will generally raise the threshold for control from direct or indirect ownership of 25 percent of the voting securities or voting interests of an entity to ownership of 50 percent of such interests, but is not likely to alter significantly the number or groupings of counterparties that would be covered by the affiliated counterparty limitations. *See,* 66 FR at 41480.

In addition, the Finance Board is defining the phrase ''sales of federal funds subject to a continuing contract'' as an overnight federal funds loan that is automatically renewed each day unless terminated by either the lender or the borrower. This definition is consistent with the generally understood meaning of this phrase, and makes clear the types of federal funds transactions that will benefit from treatment under the overall limit of § 932.9(a)(2) of the Finance Board rules. *See Id.* at 41478.

Unsecured Extensions of Credit to a Single Counterparty

The Finance Board is adopting proposed § 932.9(a) with additional provisions designed primarily to address subordinated debt issued by a counterparty and a Banks' purchases of certain obligations issued by HFAs. In addition, the Finance Board has adopted a change to the proposed rule that requires a Bank to attribute the unsecured credit exposure arising from a transaction for which repayment is irrevocably and unconditionally guaranteed by a third-party to the guarantor. The Finance Board also has restructured § 932.9(a) slightly to accommodate the new provisions.

As adopted, § 932.9(a) of the Finance Board rules sets forth the limits on a Bank's extensions of unsecured credit to a single, non-GSE counterparty. Specifically, a Bank must always meet two limits. Under the first limit, all unsecured extensions of credit, except sales of overnight federal funds, by a Bank to single non-GSE counterparty can not exceed the term limit set forth in § 932.9(a)(1). Under the second limit, which is twice the term limit, all unsecured extensions of credit including overnight federal funds transactions by a Bank to a single counterparty can not exceed the overall limit set forth in § 932.9(a)(2). *See Id.* The effect of these limits is to allow the Banks to increase their lending of overnight federal funds to non-GSE counterparties beyond the term limit applicable to other types of unsecured lending.

Section 932.9(a) also sets out the criteria for calculating the term limit and the overall limit applicable to non-GSE counterparties. Under the rule, the term limit equals the product of the maximum capital exposure limit multiplied by the lesser of: (i) The Bank's total capital or (ii) the counterparty's Tier 1 capital, or, if Tier 1 capital is not available total capital (as defined by the counterparty's principal regulator), or some comparable measure identified by the Bank. This approach is the same approach adopted in § 932.9 in December 2000. *See* 66 FR at 8301–02. The overall limit is twice the term limit calculated for the counterparty.

Further, as adopted, § 932.9(a) clarifies how a Bank attributes the credit exposure arising from a transaction that is subject to an unconditional and irrevocable guarantee by a third-party. Under the rule, if repayment of any unsecured credit is irrevocably and unconditionally guaranteed by a third party, the third-party guarantor shall be considered the counterparty. The Bank would therefore attribute the credit exposure to the third-party guarantor and calculate the applicable unsecured credit limits based upon the long-term credit rating of the third-party guarantor and the lesser of the Bank's total capital or the relevant capital measure for the third-party guarantor. If the third-party only guarantees a portion of the repayment of the credit, only that portion of the credit exposure so guaranteed shall be attributable to the third party guarantor, and the remainder of the exposure shall be attributable to the direct counterparty and subject to the limits applicable to the direct counterparty. As discussed above, the Finance Board is willing to consider requests from the Bank on a case-by-case basis that it apply this approach to other forms of credit enhancement that may not clearly constitute an irrevocable unconditional guarantee, but may nonetheless offer a equivalent level of support.

As previously discussed, the limits for qualifying obligations issued by an HFA also are calculated somewhat differently, and, as set forth in § 932.9(a)(3), the limit for these HFA obligations will always equal the product of the applicable maximum capital exposure limit and the Bank's total capital. Furthermore, the maximum capital exposure limit will be determined based on the credit rating assigned to the particular obligation purchased by the Bank. This approach could conceivably result in different limits applying to different classes or series of obligations issued by the same HFA (if each class or series received different issue ratings from the NRSROs). In such a case, however, the rule makes clear that limits will not be separately and independently applied so that the total amount of unsecured credit extended to a HFA by a Bank could never exceed the limit associated with the highest rated qualifying obligation purchased by the Bank. For example, if a Bank purchased two classes of qualifying obligations from a HFA with different structures such that one class was rated in the highest investment grade category and the other was rated in the second highest investment grade category by an NRSRO, the Bank's combined total purchase of both classes of instruments could not exceed 15 percent of the Bank's total capital. At the same time, the Bank's purchase of the instrument rated in the second highest investment grade category could not exceed 14 percent of the Bank's total capital.

To qualify for treatment under § 932.9(a)(3), the HFA obligation must either be an acquired member asset, as defined in § 955.2 of the Finance Board rules, or be the type of obligation excluded by § 956.3(a)(4)(iii) from the general prohibition against the Banks' investing in whole mortgages or loans (or interests therein). Any other type of obligation issued by an HFA or any other form of unsecured extension of credit to the HFA would not qualify for treatment under § 932.9(a)(3), and the limit for that investment would be calculated under § 932.9(a)(1). Of course, the Bank would also have to be authorized to invest in or provide such other form of unsecured credit under part 956 of the Finance Board rules or some other applicable Finance Board regulation or order.

The maximum capital exposure limits are set forth in Table 4. Each maximum capital exposure limit corresponds to a different investment grade rating so that more restrictive maximum capital exposure limits are imposed on lower-rated, and therefore potentially riskier, counterparties. The applicable maximum capital exposure limit for a counterparty rated at the highest investment grade by an NRSRO is set at 15 percent. This level is broadly consistent with federal lending limits pertaining to commercial banks as set forth by statute and regulation. The maximum capital exposure limits corresponding to credit ratings below the highest investment grade, however, are calibrated to the 15 percent maximum capital exposure limit based upon the ratio of the average credit risk percentage requirement (over all maturity bucket groupings) for the highest investment grade to the average credit risk percentage requirement for each investment grade.[7] A more complete explanation of the derivation of the maximum capital exposure limits is found in the SUPPLEMENTARY INFORMATION section of the **Federal Register** release proposing this rule. *See* 66 FR at 41478–80.

As set forth in § 932.9(a)(4)(i), a Bank will determine the maximum capital exposure limit applicable to a counterparty based on the counterparty's long-term credit rating, subject to two exceptions.[8] Under the first exception, a short-term credit rating will be used to determine the applicable maximum credit exposure limit if NRSROs have provided a short-term credit rating for a counterparty but have not provided a long-term rating for that counterparty. *See Infra* § 932.9(a)(4)(ii). If a short-term credit rating for a counterparty is used, however, the highest short-term investment grade rating is deemed to correspond to the maximum capital exposure limit assigned to the third highest long-term investment grade rating in Table 4 (*i.e.,* nine percent), and the second and third highest short-term investment grade ratings would correspond to the maximum capital exposure limit assigned to the fourth highest long-term investment grade rating in Table 4 (*i.e.,* 3 percent). This treatment of the short-term investment grade credit ratings is more fully discussed in the proposing release. 66 FR at 41480.

The second exception to exclusive use of long-term credit ratings is set forth in § 932.9(a)(4)(iii), and has been added by the Finance Board in adopting this final rule. This provision states that if a Bank purchases a debt obligation from a counterparty that has an investment rating from an NRSRO that is lower than the counterparty's long-term rating, the amount of the lower-rated obligation held by the Bank can not exceed a special sub-limit. Specifically, this sub-limit equals the maximum capital exposure limit from Table 4 corresponding to the rating assigned the lower-rated debt obligation multiplied by the lesser of the Bank's total capital or the counterparty's applicable capital measurement. While the Bank's purchases of the lower-rate obligation could not exceed the sub-limit, the total amount of unsecured credit extended by the Bank to the counterparty (including amounts of the lower rated obligation) would be restricted by the term limit and overall limit calculated using the counterparty's long-term credit rating. As already noted, the Finance Board recognized the need to adopt this provision when considering comments that the special unsecured credit limits for GSEs should not be applied to subordinated debt issued by the GSE because the same concerns arise whether a GSE or a non-GSE counterparty issues subordinated debt.[9]

Section 932.9(a)(5) establishes the criteria that a Bank will use to determine a counterparty's long-term credit rating. The same criteria should be used whenever § 932.9 requires a Bank to determine the short-term rating of a counterparty or the issue rating of a specific obligation. This criteria is generally the same as that adopted in § 932.9 in December 2000, and has been altered only to remove provisions that are no longer necessary given other changes adopted in this final rule. *See Id.* at 41481. In determining a counterparty's long-term credit rating, the rule requires a Bank to use the most recent rating issued by an NRSRO, and if more than one NRSRO has rated the counterparty, to use the lowest rating from among those ratings. A Bank should also ignore modifiers (*e.g.,* +, −, or 1, 2, 3), so that, for example, ratings of A+ or A− would both correspond to the same maximum capital exposure limit in Table 4 (*i.e.,* third highest investment grade or 9 percent). Further, if a counterparty is placed on a credit watch by an NRSRO, the rule states that the credit rating from that NRSRO at the next lower grade shall be used. In cases where a counterparty is not rated by an NRSRO, the rule allows a Bank to determine the applicable credit rating using standards available from an NRSRO or similar standards.

Affiliated Counterparties

The Finance Board is adopting the unsecured credit limit on groups of affiliated counterparties in § 932.9(b), as proposed. *See Id.* at 41480 (discussing proposed affiliated counterparty limit). Under § 932.9(b), the aggregate limit on the extension of unsecured credit to a group of affiliated counterparties would equal 30 percent of the FHLBank's total capital. In calculating the amounts of unsecured credit extended to a group of affiliated counterparties, a Bank should include the amounts of sales of overnight federal funds to those affiliated counterparties. The rule also makes clear that unsecured credit limitations on individual counterparties continue to apply to each counterparty within a group of affiliated counterparties.

GSE Limits

The Finance Board is adopting the special limit for GSEs generally as proposed, *see id.* at 41475–76, 41478, but, as already explained above, has added a provision to establish a lower, sub-limit for GSE subordinated debt held by a Bank. In adopting the final version of § 932.9(c), the Finance Board also has made some technical and conforming changes to the proposed rule.

Section 932.9(c) establishes the credit limits that a Bank should impose on its unsecured lending to GSEs. Under § 932.9(c)(1), a Bank's unsecured credit exposure to a GSE may not exceed 100 percent of the lesser of either the Bank's total capital or the GSE's total capital (as defined by the GSE's principal regulator, or some similar measure of the GSE's capital identified by the Bank). In applying this limit, a Bank must include in its calculation of the total amount of unsecured credit extended to a GSE all forms of

[7] The credit risk percentage requirements are set forth in § 932.4, Table 1.3 of Part 932 of the Finance Board rules, 12 CFR 932.4, and are used to calculate the credit risk component of the Bank's risk-based capital requirement.

[8] The Finance Board addressed its reasons for relying on long-term credit rating in its response to comments in Section II above as well as in the preamble of the August 2001 proposing release for this rule. *See* 66 FR at 41479.

[9] By contrast, a review of Moody's September 2001 Rating Lists for Banks and Securities Firms found that the issuer rating (i.e., the long-term counterparty rating) seldom if every differed from issue ratings for long-term senior debt. This is especially true under the rule because the rule ignores modifiers when determining credit ratings.

unsecured lending, including sales of overnight federal funds and a Bank's purchases of the GSE's subordinated debt. In addition, § 932.9(c)(2) requires that a Bank's total purchase of a GSE's subordinated debt not exceed a special sub-limit, which equals the maximum capital exposure limit corresponding to the credit rating assigned to the subordinated debt multiplied by the lesser of the Bank's total capital or the applicable capital measurement of the GSE. For example, if a GSE's subordinated debt were rated AA and the GSE's total capital were larger than the Bank's total capital, the sub-limit on purchases of the GSE's subordinated debt would equal 14 percent of the Bank's total capital. A Bank must calculate and apply the sub-limit on subordinated debt even if the subordinated debt is rated at the highest investment grade.

Section 932.9(c)(3) requires a Bank to treat GSEs like private counterparties in the event any NRSRO assigns a credit rating to, or downgrades the credit rating of, any long-term, senior debt obligation issued by a GSE to below the highest investment grade, or places the GSE on a credit watch for a potential downgrade. In this case, the Bank must calculate the maximum amount of its unsecured extensions of credit to that GSE in accordance with paragraph (a)(1) of the proposed rule. After a GSE's credit rating is downgraded or the GSE is placed on a watch list for a potential downgrade, § 932.9(d) applies to a Bank's extensions of unsecured credit to that GSE.

Section 932.9(c)(4) exempts a Bank's unsecured lending to another Bank from all the unsecured credit limits of this rule, although a Bank still must report its credit exposure to another Bank to the extent required by § 932.9(e). In adopting § 932.9(c)(4), the Finance Board is incorporating into the unsecured credit rule a similar inter-Bank exclusion that was contained in the FMP's unsecured credit provision. *See Id.* at 41476, 41478.

Transition Provision for Downgrades

The Finance Board has adopted the transition provision of § 932.9(d), as proposed. *See Id.* at 41480–81. This provision provides that in the event a lower maximum credit limit is imposed on a counterparty (including on a GSE) because an NRSRO has downgraded the credit rating applicable to a counterparty or has placed a counterparty on a credit watch for a potential downgrade, a Bank is not required to unwind or liquidate any transaction or position that was entered into prior to the date of the downgrade or the placement on credit watch so long as the transaction or position complied with the limits at the time it was entered.[10] However, any new unsecured extensions of credit to the counterparty would have to comply with the new lower maximum exposure limit. The rule makes clear that a renewal of an existing unsecured extension of credit, including any decision not to terminate a sale of federal funds subject to a continuing contract, would be considered a new extension of unsecured credit.

Reporting Requirements

The Finance Board is adopting the reporting requirements contained in § 932.9(e), generally as proposed. These requirements are in substance the same as those that were contained in § 932.9(c) of the version of the unsecured credit rule adopted by the Finance Board in December 2000. However, in adopting the final version of § 932.9, the Finance Board has added new provision to § 932.9(e) which requires the Banks promptly to report any positions in excess of the term limit, the overall limit or the special GSE limit set forth in the rule.

Under this provision, the Banks must report monthly to the Finance Board the amount of unsecured credit to a single counterparty, or group of affiliated counterparty, that exceeds five percent of either a Bank's total capital or the counterparty's, or the affiliated counterparties' combined, Tier 1 capital, or if Tier 1 capital is not available the counterparty's total capital (as defined by the counterparty's principal regulator) or some other comparable measure identified by the Bank. As discussed above, the consolidated capital of the holding company of the group of affiliated counterparties would be considered the combined capital of that affiliated group. In addition, the Banks must report monthly to the Finance Board the amount of the Bank's total combined secured and unsecured extensions of credit to a single counterparty or group of affiliated counterparties that exceed five percent of a Bank's total assets.

These reporting obligations apply to all extensions of credit by a Bank (including extensions of credit to other Banks), except those arising from a Bank's purchase of obligations of, or guaranteed by, the United States. As discussed above Banks must report promptly after the last business day of the month any extensions of credit in excess of the limits set forth in §§ 932.9(e)(1) and (e)(2) that occurred during that month.

New § 932.9(e)(3) requires that a Bank report promptly to the Finance Board any time its extensions of unsecured credit exceed any one or more of the limits set forth in §§ 932.9(a), (b) or (c). The Banks should report the name of the counterparty or group of affiliated counterparties involved, the date or dates for which the Bank was not in compliance, the level of the limit calculated in accordance with the rule and the amount by which the Bank's extension of unsecured credit exceeded the limit. The Bank may also include a brief statement describing any extenuating circumstances or other factors that may have led to non-compliance with the limits. The Finance Board believes that the initial report by the Bank need only be brief. If additional information is needed, the Finance Board will request it from the Bank depending on the particular circumstances of the situation. The Finance Board has not set a specific deadline for submitting a report required under § 932.9(e)(3) to provide some flexibility in this area. By way of guidance, however, the Finance Board believes that a report would be prompt if it occurred within two business days of when the Bank recognizes that a limit had been breached.

The Finance Board is adopting this new provision to help it closely monitor the effectiveness of these unsecured credit limits, and the Banks' concentration of credit. The Finance Board also believes that it is more effective and provides an opportunity for quick action (if needed) to require that reports be made to the Finance Board as soon as a Bank finds that it is not in compliance with the unsecured credit limits rather than seek such information on an *ad hoc* basis or wait for the monthly credit reporting required under the rule. The requirement also closes gaps in the reporting provision in that a Bank could be in violation of the unsecured credit limits with regard to a lower-rated counterparty but not necessarily be required to report the credit concentration under §§ 932.9(e)(1) or (2).

Calculating Extensions of Credit

The Finance Board has adopted proposed § 932.9(f) as § 932.9(f)(1) with one change to make clear that any credit exposure from a derivative contract against which the Bank holds collateral is not counted as unsecured credit. The

[10] The finance Board has already stated that § 932.9 will not require a Bank to unwind existing positions that do not conform to its new limits, provided that the credit was extended in accordance with the FMP prior to the effective date of this rule. *See* 66 FR at 41477–78.

provision, as adopted, also makes clear that the Bank must hold this collateral in accordance with § 932.4(e)(2)(ii)(B) in order for the value of the collateral to be subtracted from the credit exposure arising from the derivative contract. As discussed in Section II of this preamble, the Finance Board has also adopted new § 932.9(f)(2) to clarify the status of certain debt securities and debt obligations purchased by the Bank. Section 932.9(f) also has been restructured to accommodate the new provision. Other parts of § 932.4(f)(1) are adopted as proposed. *See Id.* at 41481. Thus, the amount of unsecured credit arising from on-balance sheet transactions will equal the sum of the book value of the item plus any amounts accrued by the Bank but not yet paid with respect to that item. The rule also requires a Bank to measure exposures from off-balance sheet and derivative transactions in accordance with § 932.4 of the Finance Board rules, which sets forth the requirements for calculating a Bank's credit risk-based capital charge. Thus, unsecured credit exposures arising from off-balance sheet transactions should be measured in accordance with § 932.4(f); unsecured credit exposures from single derivatives contracts should be measured in accordance with § 932.4(g); and unsecured credit exposures for derivative contracts subject to a qualifying bilateral netting contract should be measured in accordance with § 932.4(h). The Banks should include both the current credit exposure and the PFE in calculations of exposures arising from derivative contracts.

As previously discussed, § 932.9(f)(2) has been adopted to clarify the Finance Board's view that any debt obligation or debt security purchased by the Bank will be subject to the unsecured credit limits unless the Bank's credit exposure arising from these instruments is collateralized in accordance with § 932.4(e)(2)(ii)(B) or the Finance Board has made a determination on a case-by-case basis that the debt obligation should not be subject to the unsecured credit limits. The new provision specifically states that MBS are not subject to the unsecured credit limits nor are loans identified in §§ 955.2(a)(1) and (2) and purchased by the Bank as AMA under authority granted in part 955. HFA bonds purchased under a Bank's AMA authority, however, would be subject to the unsecured credit limits unless the Finance Board determines otherwise. Further, § 932.9(f)(2) only addresses debt obligations or debt securities purchased by the Bank. Thus, transactions with members originated by the Bank such as advances or letters of credit would be considered secured and not subject to the rules as long as collateral is posted and held in accordance with any applicable Finance Board rules and Bank policies.

United States Obligations

The Finance Board is adopting § 932.9(g), as proposed. *See Id.* at 41481. This provision makes clear that obligations of, or guaranteed by, the United States are not subject to the any of requirements of § 932.9 (including the reporting requirements that are contained in § 932.9(e)).

IV. Regulatory Flexibility Act

The final rule applies only to the Banks, which do not come within the meaning of small entities as defined in the Regulatory Flexibility Act (RFA). *See* 5 U.S.C. 601(6). Therefore, in accordance with section 605(b) of the RFA, 5 U.S.C. 605(b), the Finance Board hereby certifies that this final rule, will not have a significant economic effect on a substantial number of small entities.

V. Paperwork Reduction Act

The final rule does not contain any collections of information pursuant to the Paperwork Reduction Act of 1995. *See* 44 U.S.C. 3501 *et seq.* Therefore, the Finance Board has not submitted any information to the Office of Management and Budget for review.

List of Subjects in 12 CFR Parts 930 and 932

Capital, Credit, Federal home loan banks, Investments, Reporting and recordkeeping requirements.

Accordingly, the Federal Housing Finance Board amends title 12, chapter IX, Code of Federal Regulations as follows:

PART 930—DEFINITIONS APPLYING TO RISK MANAGEMENT AND CAPITAL REGULATIONS

1. The authority citation for part 930 continues to read as follows:

Authority: 12 U.S.C. 1422a(a)(3), 1422b(a), 1426, 1440, 1443, 1446.

2. In § 930.1 revise the definition of *Affiliated counterparty,* and add, in correct alphabetical order the definition for *Sales of federal funds subject to a continuing contract,* to read as follows:

§ 930.1 Definitions.

* * * * *

Affiliated counterparty means a counterparty of a Bank that controls, is controlled by or is under common control with another counterparty of the Bank. For the purposes of this definition only, direct or indirect ownership (including beneficial ownership) of more than 50 percent of the voting securities or voting interests of an entity constitutes control.

* * * * *

Sales of federal funds subject to a continuing contract means an overnight federal funds loan that is automatically renewed each day unless terminated by either the lender or the borrower.

* * * * *

PART 932—FEDERAL HOME LOAN BANK CAPITAL REQUIREMENTS

3. The authority citation for part 932 continues to read as follows:

Authority: 12 U.S.C. 1422a(a)(3), 1422b(a), 1426, 1440, 1443, 1446.

4. Revise § 932.9 to read as follows:

§ 932.9 Limits on unsecured extensions of credit to one counterparty or affiliated counterparties; reporting requirements for total extensions of credit to one counterparty or affiliated counterparties.

(a) *Unsecured extensions of credit to a single counterparty.* A Bank shall not extend unsecured credit to any single counterparty (other than a GSE) in an amount that would exceed the limits of this paragraph. A Bank shall not extend unsecured credit to a GSE in an amount that would exceed the limits set forth in paragraph (c) of this section. If a third-party provides an irrevocable, unconditional guarantee of repayment of a credit (or any part thereof), the third-party guarantor shall be considered the counterparty for purposes of calculating and applying the unsecured credit limits of this section with respect the to guaranteed portion of the transaction.

(1) *Term limits.* All unsecured extensions of credit by a Bank to a single counterparty that arise from the Bank's on- and off-balance sheet and derivative transactions (but excluding the amount of sales of federal funds with a maturity of one day or less and sales of federal funds subject to a continuing contract) shall not exceed the product of the maximum capital exposure limit applicable to such counterparty, as determined in accordance with paragraph (a)(4) of this section and Table 4 of this part, multiplied by the lesser of:

(i) The Bank's total capital; or

(ii) The counterparty's Tier 1 capital, or if Tier 1capital is not available, total capital (as defined by the counterparty's principal regulator) or some similar comparable measure identified by the Bank.

(2) *Overall limits including sales of overnight federal funds.* All unsecured extensions of credit by a Bank to a single counterparty that arise from the Bank's on- and off-balance sheet and derivative transactions, including the amounts of sales of federal funds with a maturity of one day or less and sales of federal funds subject to a continuing contract, shall not exceed twice the limit calculated pursuant to paragraph (a)(1) of this section.

(3) *Limits for certain obligations issued by state, local or tribal governmental agencies.* The term limit set forth in paragraph (a)(1) of this section when applied to the marketable direct obligations of state, local or tribal government unit or agencies that are acquired member assets identified in § 955.2(a)(3) of this chapter or are otherwise excluded from the prohibition against investments in whole mortgages or whole loan or interests in such mortgages or loans by § 956.3(a)(4)(iii) of this chapter shall be calculated based on the Bank's total capital and the credit rating assigned to the particular obligation as determined in accordance with paragraph (a)(5) of this section. If a Bank owns series or classes of obligations issued by a particular state, local or tribal government unit or agency or has extended other forms of unsecured credit to such entity falling into different rating categories, the total amount of unsecured credit extended by the Bank to that government unit or agency shall not exceed the term limit associated with the highest-rated obligation issued by the entity and actually purchased by the Bank.

(4) *Bank determination of applicable maximum capital exposure limits.* (i) Except as set forth in paragraph (a)(4)(ii) or (a)(4)(iii) of this section, the applicable maximum capital exposure limits are assigned to each counterparty based upon the long-term credit rating of the counterparty, as determined in accordance with paragraph (a)(5) of this section, and are provided in the following Table 4 of this part:

TABLE 4.—MAXIMUM LIMITS ON UNSECURED EXTENSIONS OF CREDIT TO A SINGLE COUNTERPARTY BY COUNTERPARTY LONG-TERM CREDIT RATING CATEGORY

Long-term credit rating of counterparty category	Maximum capital exposure limit (in percent)
Highest Investment Grade	15
Second Highest Investment Grade	14
Third Highest Investment Grade	9
Fourth Highest Investment Grade	3
Below Investment Grade or Other	1

(ii) If a counterparty does not have a long-term credit rating but has received a short-term credit rating from an NRSRO, the maximum capital exposure limit applicable to that counterparty shall be based upon the short-term credit rating, as determined in accordance with paragraph (a)(5) of this section, as follows:

(A) The highest short-term investment grade credit rating shall correspond to the maximum capital exposure limit provided in Table 4 of this part for the third highest long-term investment grade rating;

(B) The second highest short-term investment grade rating shall correspond to the maximum capital exposure limit provided in Table 4 of this part for the fourth highest long-term investment grade rating; and

(C) The third highest short-term investment grade rating shall correspond to the maximum capital exposure limit provided in Table 4 of this part for the fourth highest long-term investment grade rating.

(iii) If a specific debt obligation issued by a counterparty receives a credit rating from an NRSRO that is lower than the counterparty's long-term credit rating, the total amount of the lower-rated obligation held by the Bank may not exceed a sub-limit calculated in accordance with paragraph (a)(1) of this section, except that the Bank shall use the credit rating associated with the specific obligation to determine the applicable maximum capital exposure limit. For purposes of this paragraph, the credit rating of the debt obligation shall be determined in accordance with paragraph (a)(5) of this section.

(5) *Bank determination of applicable credit ratings.* The following criteria shall be applied to determine a counterparty's credit rating:

(i) The counterparty's most recent credit rating from a given NRSRO shall be considered;

(ii) If only one NRSRO has rated the counterparty, that NRSRO's rating shall be used. If a counterparty has received credit ratings from more than one NRSRO, the lowest credit rating from among those NRSROs shall be used;

(iii) Where a credit rating has a modifier, the credit rating is deemed to be the credit rating without the modifier;

(iv) If a counterparty is placed on a credit watch for a potential downgrade by an NRSRO, the credit rating from that NRSRO at the next lower grade shall be used; and

(v) If a counterparty is not rated by an NRSRO, the Bank shall determine the applicable credit rating by using credit rating standards available from an NRSRO or other similar standards.

(b) *Unsecured extensions of credit to affiliated counterparties.* (1) *In general.* The total amount of unsecured extensions of credit by a Bank to a group of affiliated counterparties that arise from the Bank's on- and off-balance sheet and derivative transactions, including sales of federal funds with a maturity of one day or less and sales of federal funds subject to a continuing contract, shall not exceed thirty percent of the Bank's total capital.

(2) *Relation to individual limits.* The aggregate limits calculated under this paragraph shall apply in addition to the limits on extensions of unsecured credit to a single counterparty imposed by paragraph (a) of this section.

(c) *Special limits for GSEs.* (1) *In general.* Unsecured extensions of credit by a Bank to a GSE that arise from the Bank's on- and off-balance sheet and derivative transactions, including from the purchase of any subordinated debt subject to the sub-limit set forth in paragraph (c)(2) of this section, from any sales of federal funds with a maturity of one day or less and from sales of federal funds subject to a continuing contract, shall not exceed the lesser of:

(i) The Bank's total capital; or

(ii) The GSE's total capital (as defined by the GSE's principal regulator) or some similar comparable measure identified by the Bank.

(2) *Sub-limit for subordinated debt.* The maximum amount of subordinated debt issued by a GSE and held by a Bank shall not exceed the term limit calculated under paragraph (a)(1) of this section, except that a Bank shall use the credit rating of the GSE's subordinated debt to determine the applicable maximum capital exposure limit. The credit rating of the subordinated debt shall be determined in accordance with paragraph (a)(5) of this section.

(3) *Limits applying to a GSE after a downgrade.* If any NRSRO assigns a credit rating to any senior debt obligation issued (or to be issued) by a

GSE that is below the highest investment grade or downgrades, or places on a credit watch for a potential downgrade of the credit rating on any senior unsecured obligation issued by a GSE to below the highest investment grade, the special limits on unsecured extensions of credit under paragraph (c)(1) of this section shall cease to apply, and instead, the Bank shall calculate the maximum amount of its unsecured extensions of credit to that GSE in accordance with paragraphs (a)(1) and (a)(2) of this section.

(4) *Extensions of unsecured credit to other Banks.* The limits of this section do not apply to unsecured credit extended by one Bank to another Bank.

(d) *Extensions of unsecured credit after downgrade or placement on credit watch.* If an NRSRO downgrades the credit rating applicable to any counterparty or places any counterparty on a credit watch for a potential downgrade, a Bank need not unwind or liquidate any existing transaction or position with that counterparty that complied with the limits of this section at the time it was entered. In such a case, however, a Bank may extend any additional unsecured credit to such a counterparty only in compliance with the limitations that are calculated using the lower maximum exposure limits. For the purposes of this section, the renewal of an existing unsecured extension of credit, including any decision not to terminate any sales of federal funds subject to a continuing contract, shall be considered an additional extension of unsecured credit that can be undertaken only in accordance with the lower limit.

(e) *Reporting requirements.* (1) *Total unsecured extensions of credit.* Each Bank shall report monthly to the Finance Board the amount of the Bank's total unsecured extensions of credit arising from on- and off-balance sheet and derivative transactions to any single counterparty or group of affiliated counterparties that exceeds 5 percent of:

(i) The Bank's total capital; or

(ii) The counterparty's, or affiliated counterparties' combined, Tier 1 capital, or if Tier 1 capital is not available, total capital (as defined by each counterparty's principal regulator) or some similar comparable measure identified by the Bank.

(2) *Total secured and unsecured extensions of credit.* Each Bank shall report monthly to the Finance Board the amount of the Bank's total secured and unsecured extensions of credit arising from on- and off-balance sheet and derivative transactions to any single counterparty or group of affiliated counterparties that exceeds 5 percent of the Bank's total assets.

(3) *Extensions of credit in excess of limits.* A Bank shall report promptly to the Finance Board any extensions of unsecured credit that exceeds any limit set forth in paragraphs (a), (b) or (c) of this section. In making this report, a Bank shall provide the name of the counterparty or group of affiliated counterparties to which the excess unsecured credit has been extended, the dollar amount of the applicable limit which has been exceeded, the dollar amount by which the Bank's extension of unsecured credit exceeds such limit, the dates for which the Bank was not in compliance with the limit, and, if applicable, a brief explanation of any extenuating circumstances which caused the limit to be exceeded.

(f) *Measurement of unsecured extensions of credit.* (1) *In general.* For purposes of this section, unsecured extensions of credit will be measured as follows:

(i) For on-balance sheet transactions, an amount equal to the sum of the book value of the item plus net payments due the Bank;

(ii) For off-balance sheet transactions, an amount equal to the credit equivalent amount of such item, calculated in accordance with § 932.4(f) of this part; and

(iii) For derivative transactions, an amount equal to the sum of the current and potential future credit exposures for the derivative contract, where those values are calculated in accordance with §§ 932.4(g) or 932.4(h) of this part, as applicable, less the amount of any collateral that is held in accordance with the requirements of § 932.4(e)(2)(ii)(B) of this part against the credit exposure from the derivative contract.

(2) *Status of debt obligations purchased by the Bank.* Any debt obligation or debt security (other than mortgage-backed securities or acquired member assets that are identified in §§ 955.2(a)(1) and (2) of this chapter) purchased by a Bank shall be considered an unsecured extension of credit for the purposes of this section, except:

(i) Any amount owed the Bank against which the Bank holds collateral in accordance with § 932.4(e)(2)(ii)(B) of this part; or

(ii) Any amount which the Finance Board has determined on a case-by-case basis shall not be considered an unsecured extension of credit.

(g) *Obligations of the United States.* Obligations of, or guaranteed by, the United States are not subject to the requirements of this section.

Dated: December 11, 2001.

By the Board of Directors of the Federal Housing Finance Board.

J. Timothy O'Neill,

Chairman.

[FR Doc. 01–31570 Filed 12–26–01; 8:45 am]

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DEPARTMENT OF TRANSPORTATION

Federal Aviation Administration

14 CFR Part 39

[Docket No. 2001–CE–29–AD; Amendment 39–12562; AD 2001–25–09]

RIN 2120–AA64

Airworthiness Directives; Dornier Luftfahrt GmbH Model 228–212 Airplanes

AGENCY: Federal Aviation Administration, DOT.

ACTION: Final rule.

SUMMARY: This amendment adopts a new airworthiness directive (AD) that applies to all Dornier Luftfahrt GmbH (Dornier) Model 228–212 airplanes that have a certain brake assembly installed. This AD requires you to inspect the brake housing subassembly for cracks, nicks, or corrosion (referred to as damage). This AD also requires you to replace damaged brake housing assemblies and modify the torque take-out cavity. This AD is the result of mandatory continuing airworthiness information (MCAI) issued by the airworthiness authority for Germany. The actions specified by this AD are intended to detect and correct damage to the brake housing assembly, which could result in failure of this assembly. Such failure could lead to loss of braking action on landing and possible loss of control of the airplane.

DATES: This AD becomes effective on January 18, 2002.

The Director of the Federal Register approved the incorporation by reference of certain publications listed in the regulations as of January 18, 2002.

ADDRESSES: You may get the service information referenced in this AD from Dornier Luftfahrt GmbH, Customer Support, P.O. Box 1103, D–82230 Wessling, Federal Republic of Germany; telephone: (08153) 300; facsimile: (08153) 304463. You may view this information at the Federal Aviation Administration (FAA), Central Region, Office of the Regional Counsel, Attention: Rules Docket No. 2001–CE–29–AD, 901 Locust, Room 506, Kansas City, Missouri 64106; or at the Office of