FEDERAL HOUSING FINANCE BOARD

FINANCIAL MANAGEMENT POLICY
FOR THE FEDERAL HOME LOAN BANK SYSTEM

I. POLICY OBJECTIVE

The Federal Housing Finance Board (Finance Board) Financial Management Policy (FMP) for the Federal Home Loan Bank System has been established to provide a framework within which the Federal Home Loan Banks (Banks) are allowed to implement prudent and responsible financial management strategies that assist them in accomplishing their housing finance mission, and in generating income sufficient to meet their financial obligations, in a safe, sound, and profitable manner. The specific objectives of each section of the FMP are listed below.

A. Investment Guidelines:

1. Establish policy with respect to the use of funds not required for the Banks' credit programs or operating requirements.

2. Specify permissible investment assets.

3. Establish eligibility standards for investment counterparties.

4. Establish requirements with respect to the characteristics of permissible investments.

5. Establish limits for permissible investment assets.

B. Liquidity Guidelines:

1. Implement the provisions of the Federal Home Loan Bank Act (Act), as amended, with respect to required deposit reserves.

2. Establish additional liquidity requirements.

3. Specify the types and characteristics of investment assets which may be used to satisfy the reserve and liquidity requirements.

C. Funding Guidelines:

1. Identify authorized funding sources.

2. Prescribe the conditions under which the Banks may enter into non-U.S. dollar denominated and other non-standard financing arrangements.

3. Establish individual Bank leverage limits.

D. Hedge Transaction Guidelines:

1. Define authorized hedging transactions and counterparties.

2. Establish requirements and limitations for authorized hedging transactions.

3. Establish a framework for the valuation and collateralization of interest rate swap and option transactions.

4. Establish standards for hedge documentation.

E. Unsecured Credit Guidelines:

1. Establish minimum standards for counterparties receiving extensions of unsecured credit.

2. Establish limits on the amount of unsecured credit a Bank may extend.

3. Establish a method for measuring unsecured credit risk.

F. Interest Rate Risk Guidelines:

1. Establish limits on the aggregate interest rate risk a Bank may incur.

2. Establish a method for measuring interest rate risk.

G. Implementation Guidelines:

1. Define the responsibilities of a Bank's board of directors, management, and internal audit staff.

2. Define the responsibilities of the Federal Housing Finance Board.

II. INVESTMENT GUIDELINES

A. Purpose: To establish policy on the use of funds not required for credit programs or operations, to explicitly permit the purchase of liquid assets, and to provide a safe and sound mechanism for generating income during periods of reduced credit demand to ensure that financial commitments can be met and that dividends can be maintained at levels sufficient to attract and retain members. Each Bank will be responsible for determining the extent to which its investment authority will be used to augment income from advances, consistent with Finance Board regulations and policies.

B. Permissible Investments: To the extent they are specifically authorized under Sections 11(g), 11(h) or 16(a) of the Act, or to the extent a Bank has determined that they are securities in which fiduciary or trust funds may invest under the laws of the state in which the Bank is located, the following investments are permitted:

1. Overnight and term funds, having maturities not exceeding 271 days, placed with eligible financial institutions.[1]

2. Overnight and term resale agreements, having maturities not exceeding 271 days, with eligible counterparties, using for collateral securities which are eligible investments under this section, and Federal Housing Administration (FHA) and Veterans' Administration (VA) mortgages.[2]

3. U.S. dollar and Euro-dollar deposits, having maturities not exceeding 271 days, placed with eligible financial institutions.

4. Commercial paper rated P-l by Moody's or A-l by Standard and Poor's, having a remaining term to maturity of not more than 271 days, traded in U.S. financial markets.[3]

5. Bankers' acceptances, having maturities not exceeding 271 days, drawn on and accepted by eligible financial institutions.[4]

6. Marketable obligations issued or guaranteed by the United States.

7. Marketable direct obligations of U.S. Government Sponsored Agencies and Instrumentalities for which the credit of such institutions is pledged for repayment of both principal and interest.

8. Securities representing an interest in pools of mortgages (MBS) issued, guaranteed or fully insured by the Government National Mortgage Association (GNMA), the Federal Home Loan Mortgage Corporation (FHLMC), or the Federal National Mortgage Association (FNMA), or Collateralized Mortgage Obligations (CMOs), including Real Estate Mortgage Investment Conduits (REMICs), backed by such securities.

9. Non-federal agency MBS, CMOs and REMICs rated Aaa by Moody's or AAA by Standard & Poor's.

C. Limitations on Authorized Investments:

1. Investments in other than U.S. Dollar denominated securities are prohibited.

2. A Bank may enter into agreements to purchase MBS, CMOs, and REMICs, so long as such purchases will not cause the aggregate book value of MBS/CMOs/REMICs held by the Bank to exceed 300 percent of the Bank's capital. A Bank may not increase its holdings of such securities in any one calendar quarter by more than 50 percent of its total capital at the beginning of that quarter. [5]

3. The purchase of Interest Only or Principal Only stripped MBS/CMOs/REMICs is prohibited.

4. The purchase of residual interest or interest accrual classes of CMOs/REMICs is prohibited.

5. The purchase of fixed rate MBS/CMOs/REMICs, or floating rate MBS/CMOs/REMICs that on the trade date are at rates equal to their contractual cap, with average lives that vary more than six years under an assumed instantaneous interest rate change of 300 basis points, is prohibited.

III. LIQUIDITY GUIDELINES

A. Purpose: To implement statutory requirements and to ensure each Bank's ability to meet potential funding needs arising from credit demands, deposit withdrawals, and debt redemptions without incurring material losses.

B. Statutory Deposit Reserve Requirements: Each Bank is required to maintain an amount equal to the total deposits received from its members invested in:

1. Obligations of the United States;

2. Deposits in banks or trust companies which are eligible financial institutions;

3. Advances that mature in 5 years or less to members.

C. Additional Liquidity Requirements:

1. Each Bank is required to maintain a daily average liquidity level each month in an amount not less than:

a. 20 percent of the sum of its daily average demand and overnight deposits and other overnight borrowings during the month, plus

b. 10 percent of the sum of its daily average term deposits, Consolidated Obligations (COs) and other borrowings that mature within one year.

2. Eligible Investments: The following investments, to the extent permitted under subsection II.B, are eligible for compliance with subsection III.C.l liquidity requirements:

a. Overnight funds and overnight deposits, as otherwise described in subsection II.B.l.

b. Resale agreements, which mature in 31 days or less, as otherwise described in subsection II.B.2.

C. Negotiable certificates of deposit, bankers' acceptances and commercial paper as described in subsections II.B.3, 4, and 5.

d. Marketable obligations of the United States as described in subsection II.B.6 which mature in 36 months or less.

e. Marketable direct obligations of U.S. Government Sponsored Agencies and Instrumentalities as described in subsection II.B.7 which mature in 36 months or less.

f. Cash and collected balances held at Federal Reserve Banks and eligible financial institutions, net of member pass-throughs.

3. Limitation: A security that has been pledged under a repurchase agreement cannot be used to satisfy liquidity requirements.

IV. FUNDING GUIDELINES

A. Purpose: To establish parameters for the use of alternative funding sources and structures in order that each Bank may fund its activities in a prudent, cost effective manner.

El. Bank Specific Liabilities

1. Deposits: A Bank may accept deposits from members, from any institution for which it is providing correspondent services, from another Federal Home Loan Bank, and from other instrumentalities of the United States, subject to provisions of the Act and the Finance Board's regulatory and policy requirements.

2. Federal Funds: A Bank may purchase federal funds from any financial institution that participates in the federal funds market.

3. Repurchase Agreements: Repurchase agreements requiring the delivery of collateral by a Bank are permitted with any Federal Reserve Bank, U.S. Government Sponsored Agencies and Instrumentalities, primary dealers recognized by the Federal Reserve Bank of New York, eligible financial institutions, and states and municipalities with a Moody's Investment Grade rating of 1 or 2. Repurchase agreements not requiring the delivery of collateral by the Bank may be entered into with any supplier of funds.

C. Consolidated Obligations: A Bank may participate in COs issued by the Office of Finance, so long as entering into such transactions will not cause the Bank's total unsecured senior liabilities, as defined in Section 910.0 of the Finance Board's regulations (but excluding interBank loans), to exceed 20 times the Bank's total capital. Each Bank shall make every effort to manage its unsecured senior liabilities and capital to ensure compliance with the 2O:l leverage limit.

1. A Bank may participate in the following types of standard debt issues:

   a. Debt with a fixed rate and fixed maturity, in either coupon or discount form.

   b. Debt with a fixed maturity whose coupon rate may vary in predetermined increments or based upon the movement of U.S. Treasury securities, U.S. Dollar LIBOR, the 11th District Cost of Funds Index or FHLBank COs.

   C. Debt whose principal may be called or redeemed in whole or in part at the discretion of the Bank.

   d. Debt whose principal amortizes according to a predetermined schedule.

2. A Bank may also participate in non-standard debt issues, some examples of which are:

   a. Debt whose coupon may vary based upon the movement of an eligible financial index (other than those identified in subsection C.1.b. above).[6]

   b. Debt whose principal is subject to redemption in whole or in part, based upon the movement of one or more eligible financial index or indices (e.g., indexed amortizing bonds).

c. Debt whose principal balance may increase based upon the movement of one or more eligible financial index or indices.

d. Debt whose coupon may vary based upon the movement of two or more eligible financial indices, including transactions which multiply the effect of rate changes.

e. Debt denominated in a currency other than U.S. Dollars whose exchange rate risk relative to the U.S. Dollar can be effectively hedged.

If a Bank participates in a debt issue other than the standard transactions described in subsection C.l above, the Bank will be required to enter into a contemporaneous hedging arrangement that allows the interest rate and/or basis risk to be passed through to the hedge counterparty, unless the Bank is able to document that the debt will: (a) be used to fund mirror-image assets in an amount equal to the debt; or (b) offset or reduce interest rate or basis risk in the Bank's portfolio, or otherwise assist the Bank in achieving its interest rate and/or basis risk management objectives. If a Bank participates in debt denominated in a currency other than U.S. Dollars, the currency exchange risk must be hedged.

V. HEDGE TRANSACTION GUIDELINES

A. Purpose: To allow the implementation of hedging programs that control the interest rate and basis risk which arises in the ordinary course of business.

B. Permitted Instruments and Strategies: Long and short positions in the cash, forward, futures, and option markets (including caps and floors), and the purchase and sale of interest rate exchange agreements (swaps) are permitted if they assist a Bank in achieving its interest rate and/or basis risk management objectives. Hedging strategies must be explicitly stated at the time of execution and adequate documentation must be maintained during the life of the hedge. A Bank may also enter into swaps as intermediary between a member and a non-member counterparty to facilitate the member's asset/liability management strategies. Speculative use of permitted hedging instruments is prohibited.[7]

C. Hedging With Interest Rate Swaps and Options (Including Caps and Floors):

1. All swaps entered into by a Bank shall be governed by the FMP.

2. Unsecured risk exposure associated with interest rate swaps and options is governed by the FMP's Unsecured Credit Guidelines.

3. Collateral Requirements: A Bank shall require collateral for interest rate swaps and options from those counterparties (or guarantors) that, on the trade date of the transaction, do not qualify for unsecured extensions of credit, and for risk exposure that, on the trade date of the transaction, exceeds the limits for unsecured extensions of credit established in the FMP. (Each Bank's board of directors may identify a level of exposure it deems material before a collateral call will be required, either at the initiation, or throughout the life, of a hedge agreement. If a Bank chooses to identify a minimum collateral call level, that level or the method for calculating it must be included in the Bank's policy, as required in subsection VIII.A.l.f. of the FMP.)

   a. The dollar amount of collateral shall be determined by the Bank commensurate with the risk undertaken and shall be maintained in accordance with the requirements of the Bank's agreement with the counterparty.

   b. Collateral required during the life of the transaction shall be no less than the market value of the swap, as determined by the Bank, plus net accrued interest due to the Bank.

   C. For option transactions in which the Bank is a potential receiver of payments, a minimum initial collateral maintenance level must be established that is no less than the market value of the contract, plus amounts due to the Bank under the contract.

   d. Collateral agreements entered into by a Bank that are not required by the FMP will not be subject to FMP collateral requirements.

4. A Bank may enter into an unsecured interest rate swap or option agreement with a counterparty that does not meet the minimum credit standards as long as the transaction results in a net reduction of credit risk arising from previously existing swap or option agreements with that counterparty, and a master agreement executed by the Bank and the counterparty provides for such netting.

5. A Bank may, for hedging purposes, enter into interest rate swap agreements in which the notional principal balance amortizes based upon the prepayment experience of a specified group of MBS or the behavior of an interest rate index (Indexed Principal Swaps), or swap agreements which may be terminated or extended at the option of the Bank or its counterparty (swaptions).

   a. Interest rate swaps that amortize according to the behavior of Interest Only or Principal Only stripped MBS/CMOs/REMICs are prohibited.

   b. Interest rate swaps that amortize according to the behavior of residual interest or interest accrual classes of CMOs or REMICs are prohibited.

   C. Indexed principal swaps that have average lives that vary by more than six years under an assumed instantaneous change in interest rates of 300 basis points are prohibited, unless they are entered into in conjunction with the issuance of COs in which the interest rate risk is passed through to the investor.

6. In addition to interest rate caps and floors, a Bank may take long and short hedge positions in any options contract provided that:

   a. The underlying instrument is an investment or a futures contract permissible under this policy.

   b. The hedge is constructed such that the price volatility of the option position is consistent with the price volatility of the cash instrument being hedged or with the option component of that instrument.

   C. The option contract is traded on an organized exchange regulated by the Commodity Futures Trading Commission or the Securities and Exchange Commission; or through a recognized securities dealer which reports its position regularly to the Federal Reserve Bank of New York.

7. Documentation:

   a. Market value determinations and subsequent collateral adjustments should be made, at a minimum, on a monthly basis.

   b. Failure of a counterparty to meet a collateral call will result in an early termination event.

c. Early termination pricing and methodology shall be detailed in all interest rate swap and option contracts in which a Bank is involved as principal. This methodology must reflect a reasonable estimate of the market value of the swap or option at termination. Standard International Swap and Derivatives Association, Inc. language relative to early termination pricing/methodology may be used to satisfy this requirement.

d. The transfer of an agreement or contract by a counterparty shall be made only with the consent of the Bank.

e. Transactions with a single counterparty shall be governed by a single master agreement when practicable.

8. Non-U.S. Dollar denominated swaps are authorized only to convert matching non-U.S. Dollar denominated debt to U.S. Dollar denominated debt, or to offset another non-U.S. Dollar denominated swap.

D. Hedging in the Financial Futures Markets:

1. Long and short positions in financial futures may be used for hedging provided that:

a. The underlying instrument is an investment or other transaction permissible under this policy.

b. The price of the futures contract has a high correlation with the price of the cash instrument being hedged.

C. The futures contract is traded on an organized exchange regulated by the Commodity Futures Trading Commission.

2. If delivery of the underlying security will cause a Bank to exceed any investment limitation of the FMP, the Bank must close out its position prior to taking delivery.

3. Any Bank with a position which exceeds 5 percent of the open interest in any specific futures contract month shall report that position to the investment desks of the other Banks and to the Finance Board's District Banks' Directorate within one business day of the initiation of the position. Notification shall also be provided when such a position declines below 5 percent.

E. Hedging in the Cash or Forward Markets:

1. The purchase or sale of cash market securities for either regular (cash) or forward delivery is permitted, provided that:

   a. Only securities that are permissible investments under this policy are used.

   b. The price of the cash or forward instrument has a high correlation with the price of the instrument being hedged.

   C. Any security purchased in the cash market for hedging purposes is subject to the investment limits of the FMP.

2. Short positions in instruments authorized in the FMP, the purchase of securities under resale agreements, and the borrowing of securities in connection with short sales is authorized for hedging purposes.

VI. UNSECURED CREDIT GUIDELINES

A. Purpose: To set prudent limits on unsecured credit risk arising from authorized investment and hedging strategies.

B. Scope: All on- and off-balance sheet extensions of credit in which the value of collateral pledged to the Bank by a counterparty is less than the credit the Bank has extended to that counterparty. (InterBank loans and obligations of, or guaranteed by, the United States[8] are not subject to the requirements of this section.)

C. Eligibility for Unsecured Extensions of Credit:

1. The amount of unsecured credit that may be extended to individual counterparties shall be commensurate with the counterparty's credit quality. A counterparty's credit quality shall be determined by credit ratings of the counterparty's debt, debt securities, or deposits.

2. Acceptable Credit Ratings: A Bank may extend unsecured credit to counterparties assigned the following credit ratings at the transaction trade date:

	Thomson Bankwatch	IBCA	Moody's		Standard & Poor's		IDC
Level I	A A/B	A A/B	P-1	Aaa	A-1		above 190
Level II	B B/C	B B/C		Aa		AA	165-190
Level III	C	C		A		A	140-164

a. Thomson Bankwatch shall be the primary short-term rater. Only Moody's and S&P long-term ratings may be used. The use of short- or long-term credit ratings shall be appropriate to the term of the transaction: i.e., short-term ratings for transactions with a maturity equal to 1 year or less; long-term ratings for transactions with a maturity greater than 1 year.

b. Single-A and double-A ratings from Moody's and Standard & Poor's shall be interpreted to include the full range of the generic rating category (e.g., single-A will include A- and A3).

c. Rating downgrades of counterparties shall not require the liquidation of existing positions.

d. A Bank will have discretion to choose the rating it will use if the rating agencies disagree. on a counterparty's credit rating. In the event of a split rating (i.e., a counterparty receiving different ratings on its short- and long-term liabilities), the higher of the two ratings will dictate the total amount of unsecured credit the Bank may extend to the counterparty; however, the lower of the two ratings will limit the allowable credit exposure to the counterparty for investments/hedges with maturities governed by the lower of the two ratings to the maximum allowed in the FMP for counterparties with that rating.

3. Acceptable Country Risk Rating: Unsecured credit may be extended only to foreign counterparties subject to minimum risk of political and economic instability as represented by a country risk rating of I by Thomson Bankwatch.

4. Limitations on Unsecured Credit Extensions

a. Unsecured extensions of credit to a single U.S. Government Sponsored Agency or Instrumentality shall not exceed 100 percent of a Bank's capital.

b. Unsecured extensions of credit to a single Level I counterparty shall not exceed 50 percent of a Bank's capital.

c. Unsecured extensions of credit to a single Level II counterparty shall not exceed 25 percent of a Bank's capital.

d. Unsecured extensions of credit to a single Level III counterparty shall not exceed 10 percent of a Bank's capital.

e. The maximum amount of unsecured credit that may be extended to any counterparty shall not exceed 50 percent of that counterparty's Tier I capital (or tangible capital if Tier I is not available).

f. Limitations on extensions of unsecured credit apply only to the specific counterparty receiving the credit. However, each Bank is expected to evaluate its unsecured credit exposure to related counterparties and impose limits on such extensions of credit if necessary.

g. Unsecured extensions of credit (except those that result from a Bank entering into swaps and other hedging arrangements) to Level III counterparties may not be made for terms in excess of one (1) business day,

h. Maximum Effective Maturities for Unsecured Extensions of Credit Arising from Interest Rate Swap Agreements and Similar Transactions:[9]

Counterparty Credit Rating	--Maximum Effective Maturity of Agreements--
Long Term	
Aaa, AAA	No maturity limit
Aa, AA	7 years
A, A	5 years
Short Term	
Al, Pl, A, B	1 year

Contingent Collateralization of Agreements: Contracts for interest rate exchange agreements or similar transactions with effective maturities longer than 10 years shall require full collateralization of the agreement value plus accrued interest (maintenance margin) in the event of a counterparty downgrade below Level III.

VII. INTEREST RATE RISK GUIDELINES

A. Purpose: To set prudent limits on the extent to which each Bank may be exposed to interest rate risk.

B. Interest Rate Risk Limitation:

1. Each Bank is required to maintain the duration of its equity (at current interest rate levels using the CO cost curve) within a range of +5 years to -5 years.

2. Each Bank is required to maintain its duration of equity, under an assumed 200 basis point change in interest rates, within a range of +7 years to -7 years.

3. Duration of equity calculations shall be performed by the Finance Board based upon data supplied by the Banks at intervals prescribed by the Finance Board. Banks which have internal duration models may submit their results, if different from those calculated by the Finance Board, to evidence compliance with this policy. Determination of compliance will ultimately rest with the Finance Board.

4. Each Bank is required to report its cash flows and calculate its duration of equity both with and without projected cashflows which represent the Bank's share of the System's REFCorp and ABP obligations.

VIII. IMPLEMENTATION GUIDELINES

A. The Board of Directors of each Bank shall:

1. Adopt and forward to the Finance Board a Bank financial management policy consistent with the FMP within 90 calendar days of the effective date of the FMP. The Bank's policy will address:

a. the role of the investment portfolio in maintaining liquidity and generating earnings;

b. limits on changes in net market value resulting from interest rate risk and convexity;

c. the impact of the mark to market accounting requirements of SFAS 115;

d. the cash flow implications of the FIRREA obligations and their impact on the Bank's measurement and control of interest rate risk;

e. a commitment to attain and maintain a stand-alone triple-A rating on long-term deposits or other unsecured long-term liabilities; and

f. any minimum collateral call levels approved by the Bank's board or the methods by which such levels are determined.

2. To the extent that the Bank enters into investment transactions not specifically permitted under Sections 11(g), 11(h), or 16(a) of the Act, ensure that such investments are securities in which fiduciary and trust funds may invest under the laws of the state in which the Bank is located.

3. Identify the tolerable risk limits for MBS/CMOs/REMICs, including the amount of capital (market value) the Bank is willing to expose under a 200 basis point movement in interest rates.

4. Evaluate modeling and management expertise available to measure and control the credit, interest rate, basis, and other risk involved in non-standard financing arrangements entered into by the Bank.

5. Establish policies that ensure diversity in the Bank's funding sources and investments.

6. Authorize specific individuals to develop financial strategies and to execute financial transactions governed by the FMP. (Duties and responsibilities shall be appropriately divided so that no one individual has sole responsibility for any two of the following functions: trading; funds and security transfer; and portfolio accounting.)

7. Approve the opening of any unsecured checking or settlement accounts with counterparties that do not meet the credit standards established in the FMP.

Decide whether to maintain any existing unsecured checking or settlement accounts with counterparties that have been downgraded below credit standards established in the FMP. The justification for such approvals shall be forwarded to the Finance Board for review. (Unsecured checking or settlement accounts with counterparties that do not meet the credit standards of the FMP but that are covered by deposit insurance or are otherwise guaranteed are exempt from this requirement).

8. Approve a list of brokers, reporting dealers, and futures commission merchants with whom the Bank may purchase and sell securities and contracts.

B. Management of each Bank shall:

1. Establish internal control systems to ensure compliance with the FMP.

2. Submit a monthly report to its board of directors and to the Finance Board regarding the activities governed by the FMP. At a minimum, the report shall cover the areas of investments, liquidity, funding, hedging, unsecured counterparty risk, and interest rate risk. It will also discuss compliance with the limitations in the FMP and the Bank's internal policies. Any exceptions to the FMP shall be highlighted and explained in the compliance report submitted to the Finance Board; such report shall be in a format defined by the Finance Board.

3. Provide periodic data, as requested by the Finance Board, to facilitate its oversight of FMP implementation,

4. Establish one or more securities safekeeping agents and notify the Finance Board accordingly. (Authorized agents include Federal Reserve Banks, Federal Home Loan Banks, and other eligible financial institutions domiciled in the U.S.)

5 . Account for financial transactions executed under the FMP in accordance with Generally Accepted Accounting Principles.

C. The Internal Auditor of each Bank shall establish internal auditing programs that test for compliance with the FMP.

D. The Federal Housing Finance Board shall:

1. Monitor each Bank's compliance with the FMP.

2. Interpret any questions related to the FMP.

3. Consider requests for exceptions to the FMP.

E. The FMP shall:

1. Become effective on January 1, 1994.

2. Amend and replace the Financial Management Policy dated July 1, 1991 and the Interim Funding Guidelines dated December 23, 1992. Financial transactions and contracts that were authorized for, and entered into by, the Banks under these and any relevant preceding policies, and that remain outstanding on the effective date of the FMP, are grandfathered for purposes of compliance with the amended policy guidelines.

FOOTNOTES

1. The term "eligible financial institutions" includes:

   a. Federal Home Loan Banks;

   b. FDIC-insured financial institutions whose most recently published financial statements exhibit Tier I (or tangible) capital of not less than $100 million, and which have been rated not lower than C by Thomson Bankwatch or single A by Standard & Poor's or Moody's.

   c. The head office of foreign commercial banks whose most recently published financial statements exhibit Tier I (Or tangible) capital of not less than $100 million, and which have been rated at least C (company rating) by Thomson Bankwatch or C (individual rating) by IBCA and I country risk by' Thomson Bankwatch.

   d. Branches or agency offices of eligible financial institutions located in the United States or in other countries receiving a country risk rating of I from Thomson Bankwatch.

2. Eligible counterparties for resale agreements include the. Federal Reserve Bank of New York, primary dealers in government securities recognized by the Federal Reserve whose capital exceeds $100 million or which are guaranteed by parent firms whose capital exceeds $100 million, and U.S. Government Sponsored Enterprises for which the credit of such institution is pledged for repayment. Members that are eligible financial institutions are eligible counterparties for the Bank in which they are a member.

   Resale agreements may be consummated using a designated custodian, provided the custodian is a domestic eligible financial institution and documentation is provided which evidences the Bank's security interest in the collateral held by the custodian.

3. Commercial paper issuers must exhibit at least $100 million of tangible capital on their most recently published audited financial statements and be included in Moody's Global Short-Term Market Record under the industry classifications of banking, finance, or securities. If the issue receives its Al/P1 rating by virtue of 'a guarantee or other credit enhancement, the minimum capital requirement shall apply to the guarantor. If the issue receives its Al/P1 rating by virtue of the credit standing of a non-U.S. issuer or guarantor, the foreign issuer/guarantor must be domiciled in a country with a country risk rating of I.

4. Investments of the type described in subsections II.B.1 through II.B.5, that have a term to maturity greater than 271 days are authorized, provided they contain a "put" option that a Bank may exercise either continuously or at discrete intervals equal to or less than the 271 day maturity limit during the life of the investments. For purposes of determining compliance with the stated maturity limits, settlement date will be deemed the initiation of a transaction.

5. For purposes of determining compliance with the MBS limit, investment levels will be measured as of the transaction trade date and capital levels will be based on the Bank's most recently available monthly financial statement. A Bank will not be required to divest securities solely to bring the absolute level of its holdings into compliance with the limit. A Bank's dollar roll financing activity will not be circumscribed by the MBS investment authority limits.

6. An "eligible financial index" is an index that is recognized by the International Swap and Derivatives Association, Inc., publicly available, and verifiable independent of the dealers underwriting the debt issue or acting as counterparties in transactions related to these issues. For an index that pertains to a foreign country, that country must be assigned a Country Risk Rating no lower than II by Thomson Bankwatch.

7. Eligible non-member counterparties for hedging transactions include:

   a. Eligible financial institutions;

   b. Foreign financial institutions domiciled in countries receiving a country risk rating of I from Thomson Bankwatch;

   c. Domestic corporations or partnerships, foreign corporations, domestic subsidiaries of foreign corporations, international organizations, and foreign governments or their agencies, rated at least single-A by Moody's or S&P; and

   d. U.S. Government Sponsored Agencies.

8. For purposes of the FMP, unsecured extensions of credit will be measured as follows:

   il. For on-balance sheet transactions, an amount equal to the sum of the book value of the item plus net payments due the Bank.

b. For standard off-balance sheet transactions, an amount equal to the sum of the net market value of the agreement, as determined by the Bank, plus net payments due the Bank, plus 0.5 percent of the notional amount.

c. For off-balance sheet transactions where the net market value is dependent upon the interrelationship between or among two or more indices, an amount equal to the sum of the net market value of the agreement, plus net payments due the Bank, plus 1 percent of the notional amount.

d. For off-balance sheet transactions in which the effect of interest rate movements is multiplied (leveraged transactions), an amount equal to the sum of the net market value of the agreement, plus net payments due the Bank, plus 2 percent of the notional amount.

9. For Indexed Principal Swaps, the effective maturity shall be the weighted average maturity using consensus prepayment speed estimates for current interest rate levels, unless an appropriate alternative methodology is applied.