

FEDERAL HOUSING FINANCE BOARD

OPEN MEETING

Second Floor  
1777 F Street, N.W.  
Washington, D.C.

Thursday,  
November 30, 2000

The meeting was convened at 10:02 a.m.

ATTENDEES:

WILLIAM C. APGAR, Chairman  
FRANZ S. LEICHTER, Director  
J. TIMOTHY O'NEILL, Director  
JAMES L. BOTHWELL  
CHARLOTTE A. REID  
DEBORAH F. SILBERMAN  
JOSEPH A. MCKENZIE  
GWEN R. GROGAN  
SCOTT L. SMITH  
JONATHAN F. CURTIS  
LORI GOEHRING

P R O C E E D I N G S1  
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(10:02 a.m.)

MR. APGAR: Before we begin, I'd like to just make a brief comment on behalf of the Board.

As most of you know, of course, one of the giants in the housing industry and in housing America, Henry B. Gonzalez, a former House Banking Committee chairman, passed away recently. Even in the most difficult of times, Chairman Gonzalez saw the potential of the Federal Home Loan Bank System. He was obviously chief architect of FIRREA that created this Board. He also invented the Affordable Housing Program.

I can think of no better and more lasting memory than the literally thousands and thousands of families who are benefiting from the program, especially the Affordable Housing Program that he created, so I'm sure my Board member colleagues join me in giving our best sympathies and well wishes to his family and all his many friends in the housing arena.

Without further ado, let's begin with our agenda. The first item on the agenda is the proposed rule on enforcement powers. Jim, would you brief us on the rule and discuss your recommendations?

MR. BOTHWELL: Thank you, Mr. Chairman, and good morning, Director O'Neill and Director Leichter.

1           As you are aware, there are several items on  
2 today's agenda. The first item, as you noticed, Mr.  
3 Chairman, is a proposed rule that would implement the new  
4 enforcement authorities, including cease-and-desist orders,  
5 civil money penalties and subpoena power that were conferred  
6 on the Finance Board by Title 6 of the Gramm-Leach-Bliley  
7 Act.

8           The second and third items both concern the Office  
9 of Finance and involve approval of a waiver request to allow  
10 OF to assume its responsibility for the preparation and  
11 publication of the System's combined financial statements  
12 effective with the first quarter of next year, and the  
13 resolution to allow OF to reopen debt instruments that were  
14 originally issued by the Finance Board under its authority  
15 under Section 11(c) of the Bank Act.

16           The last two items on the agenda are informational  
17 progress reports on the Banks' implementation of the new  
18 collateral authorities provided by the Gramm-Leach-Bliley  
19 legislation and the Banks' operation of their single-family  
20 acquired member asset programs such as Chicago's well-known  
21 MPF program.

22           So without further elaboration, I will ask Deb  
23 Silberman to present the first item.

24           MS. SILBERMAN: Thanks, and I'm going to  
25 immediately let Charlotte describe the proposed rule and

1 give you the opportunity to ask any questions you may have  
2 about it.

3 MS. REID: Good morning, members of the Board.  
4 Staff recommends adoption of this proposed rule, which would  
5 amend the Finance Board regulations to implement the  
6 provisions of the Gramm-Leach-Bliley Act of 1999 that  
7 broadened the Agency's existing supervisory authority over  
8 the Federal Home Loan Banks. If approved by the Board, the  
9 proposed rule will be promptly published in the *Federal*  
10 *Register* for notice and comment for a period of 30 days.

11 The Federal Home Loan Bank Act provides plenary  
12 authority for the Finance Board to insure that the Banks are  
13 operated in a safe and sound manner, its primary statutory  
14 duty under the Act, as well as to supervise the Banks to  
15 insure that they carry out their housing finance mission and  
16 to insure that the Banks remain adequately capitalized and  
17 able to raise funds in the capital market. In particular,  
18 the Act authorizes the Finance Board to issue and enforce  
19 orders and regulations and remove for cause any director,  
20 officer, employee or agent of any Bank or the Office of  
21 Finance.

22 As amended by the Gramm-Leach-Bliley Act, the Act  
23 confers on the Finance Board certain additional  
24 administrative enforcement powers and procedures which are  
25 substantially the same as the enforcement provisions of the

1 Office of Federal Housing Enterprise Oversight with respect  
2 to Fannie Mae and Freddie Mac, pursuant to subtitle C of  
3 Title 13 of the Housing and Community Development Act of  
4 1992, as well as those granted to the appropriate federal  
5 banking agencies with respect to insured depository  
6 institutions under Section 8(b) of the Federal Deposit  
7 Insurance Act. These added enforcement powers broaden and  
8 in no way limit the existing authority of the Finance Board  
9 to supervise the Banks and to insure that the Banks are  
10 operated in a safe and sound manner.

11 Pursuant to the amendments, the Finance Board may  
12 issue cease-and-desist orders, temporary cease-and-desist  
13 orders, corrective-action orders and assess civil money  
14 penalties. The Act, as amended, also sets forth the Finance  
15 Board's authority and procedures for hearings on the record,  
16 judicial review of final orders, the issuance of subpoenas  
17 and subpoenas duces tecum to obtain documents and testimony,  
18 and the enforcement of final orders.

19 Again, nothing in the rule in any way restricts  
20 the authority or the ability of the Finance Board to conduct  
21 an examination or inspection of a Bank or the Office of  
22 Finance or to take other supervisory action. Similarly, the  
23 procedures for administrative challenges to examination  
24 findings or requests for waivers, regulatory interpretations  
25 or approvals, which are set forth in Part 907 of the Finance

1 Board regulations, are independent from and do not serve as  
2 a prerequisite for regulatory action under this part.

3 I'd be happy to answer any questions you may have.

4 MR. LEICHTER: Yes. I have a question. It's  
5 really more in the nature of a comment. It would be my  
6 understanding that no cease-and-desist order would be issued  
7 without action by the Board of Directors.

8 MS. REID: The statute authorizes the Finance  
9 Board to issue cease-and-desist orders and provides a remedy  
10 for the recipient of such an order to challenge the order  
11 and take it to the Finance Board, the Board of Directors,  
12 for final determination.

13 A cease-and-desist order can be issued by the  
14 Finance Board prior to the hearing on the record that would  
15 be conducted by a presiding officer appointed by the Finance  
16 Board, which would then provide all of the information that  
17 is gleaned from the hearing. All of that information would  
18 be provided to the Board of Directors, and the Board of  
19 Directors would make a final determination.

20 Once that order is issued pursuant to the Board's  
21 authorization, the Finance Board, Board of Directors'  
22 authorization, after 30 days it would become a final order.  
23 The recipient of such an order would have that 30 days to  
24 file a challenge petition in the Court of Appeals to have  
25 the cease-and-desist order overturned.

1           MR. LEICHTER: I must say, that somewhat troubles  
2 me. At least at this moment I have difficulty in accepting  
3 that the cease-and-desist order could be issued without  
4 actually having been approved by the members of the Board of  
5 Directors.

6           The procedure that you envisage would have staff  
7 issue a cease-and-desist order, which obviously has some  
8 very serious implications. Maybe many months later, before  
9 the matter comes before the Board of Directors, you've --

10          MR. APGAR: That's a misconception, because the  
11 staff is acting through the authority -- through the  
12 Managing Director, from the Chairman, and so implicitly any  
13 staff action bears the imprint of the Chairman. So I think  
14 that overstates exactly the staff's role. And clearly, as a  
15 matter of process, we need to have some capacity to move  
16 expeditiously, with the involvement of the Chairman, the  
17 Managing Director and other senior staff. This procedure  
18 allows plenty of safeguards for full Board reviews, should  
19 those be needed.

20          MR. LEICHTER: Well, as I indicated, I have some  
21 difficulty in accepting this because it seems to me that the  
22 Agency really acts through the Board of Directors. This  
23 would be a very significant action that would be taken  
24 absent the authority of the Board of Directors.

25          I have no problem with the proposed regulations.

1 We've gone over them, and I very much appreciate the  
2 briefing that I got personally and the briefing today. I  
3 don't see anything in the regulation, as such, that  
4 determines the issue I've raised one way or the other, and I  
5 think it's something that we ought to work out among  
6 ourselves.

7 MR. APGAR: Right. I mean, I think this issue of  
8 exactly what authorities rest with the Chairman and what  
9 authorities rest with the Board -- clearly there are many  
10 administrative duties that couldn't possibly be handled  
11 through full Board action. It's the duty of the Chairman to  
12 identify those which rise to a significant level.

13 In addition, there are many safeguards built in  
14 the system where individuals have the right to appeal to the  
15 full Board before the review, so it seems like this is the  
16 practical way to go. It's certainly consistent with our  
17 tradition of how this Board has operated since its  
18 inception.

19 MR. O'NEILL: It seems like one of the reasons for  
20 the way it's set up -- and tell me if this is not right, but  
21 we want to keep the Board of Directors' hands clean to look  
22 at it after the special -- what's the term for the  
23 special --

24 MS. REID: Presiding officer.

25 MR. O'NEILL: Presiding officer. I think what the



1 staff is saying is that if we get involved early in the  
2 issuance of the cease-and-desist order and then it goes to  
3 the presiding officer and then it comes back to the Board of  
4 Directors for a final decision, we might have unclean hands  
5 because we were the ones that originally voted on the cease-  
6 and-desist order. So how can we objectively view what the  
7 presiding officer says?

8 I think that's why this system -- another reason  
9 why the system was set up the way it is. Is that fair?

10 MS. REID: Yes.

11 MR. APGAR: Yes. That's exactly right.

12 MR. LEICHTER: I understand that's the system  
13 that's envisaged. First of all, I don't think, as the  
14 Chairman described it, you have an absolute firewall between  
15 the issuance of the cease-and-desist order and the eventual  
16 review by the Board of Directors since the Chairman, who is  
17 a member of the Board of Directors, is involved in issuing  
18 the cease-and-desist. So you don't have the, if you will,  
19 untainted appellate process.

20 But I'm not sure that the Board was envisaged  
21 statutorily, as it functions, to play the role of appellate  
22 review in this particular instance. I am concerned that an  
23 action which has such far-reaching effect as a cease-and-  
24 desist order would be issued, as was proposed or stated,  
25 solely on the action of the staff, even with the concurrence

1 of the Chairman. By the way, I --

2 MS. SILBERMAN: Just to clarify one thing, it's  
3 actually only a notice of --

4 MR. LEICHTER: Let me just finish, please.

5 MS. SILBERMAN: It's only a notice of charges  
6 that's issued. The cease-and-desist, the actual order to  
7 cease and desist, is only issued after the hearing which  
8 takes place.

9 MR. LEICHTER: All right. I'm glad you did  
10 interrupt me because that may resolve my concern. Then the  
11 issue that I first raised as to whether a cease-and-desist  
12 order can be issued without action of the Board of  
13 Directors, you're telling me that it cannot and that it's  
14 the cease-and-desist order which follows the action of the  
15 Board of Directors, although the charges can be propounded.  
16 I have no problem with that. In that event, that satisfies  
17 the concern I had.

18 We've looked through the regulation. I have no  
19 problem with the regulation, and maybe we can just fine-tune  
20 some of these issues or add to some of the questions. There  
21 may be misconceptions that I may have, but I have no problem  
22 if you tell me that the actual cease-and-desist order cannot  
23 be issued absent action by the Board of Directors.

24 MR. O'NEILL: I agree with Franz on this. I think  
25 if it's as they say, that the staff can bring up the

1 charges, but the actual cease-and-desist order can only  
2 happen after the Board of Directors has a vote, I think that  
3 that is the way it should be, because I agree that a cease-  
4 and-desist order is rather far-reaching, and I don't want to  
5 use the word "draconian," but it's really a big deal to use  
6 a cease-and-desist order, so I think that it deserves a vote  
7 of the Board of Directors.

8 MR. APGAR: Any other comments?

9 MR. O'NEILL: Just one thing. Obviously this is  
10 something that was spawned by Gramm-Leach-Bliley, so this  
11 one will go for comment.

12 We're voting on the capital reg next month. Are  
13 those the last two things that Gramm-Leach-Bliley says to us  
14 that we have to do, or are there other things still  
15 outstanding?

16 MS. SILBERMAN: I hate to speak in absolutes  
17 because lawyers don't like to do that. I think it's the  
18 last thing, but I reserve the right to be wrong.

19 (Laughter.)

20 MR. BOTHWELL: It's the last thing that I know of.

21 MR. APGAR: Okay. So are there any further  
22 questions before we vote?

23 If not, then all in favor of the proposed rule say  
24 aye.

25 (Chorus of ayes.)

1 MR. APGAR: No opposed. The proposed rule is  
2 adopted.

3 I ask unanimous consent that the staff be  
4 permitted to make technical, conforming changes to the  
5 proposed rule. Without objection, so ordered.

6 They write all these magic words down for me. Did  
7 I do that okay, then? Okay. Good.

8 The second item on our agenda consists of two  
9 issues relating to the Office of Finance. I would change  
10 the cast of characters and let Jim describe the two issues  
11 and then further discussion can proceed in general, I guess.

12 Thank you.

13 MR. BOTHWELL: Thank you, Mr. Chairman. As I  
14 mentioned previously, both of these items involve the Office  
15 of Finance. And I'll just ask Joe McKenzie from the Office  
16 of Policy Research and Analysis to present the items to you.

17 MR. MCKENZIE: Good morning. Staff is requesting  
18 the Finance Board approval of two resolutions dealing with  
19 the Office of Finance. The first resolution deals with the  
20 timing of the transfer of the responsibility for preparing  
21 the System's combined financial statements, and the second  
22 resolution deals with the authority of the Office of Finance  
23 to reopen bond issues.

24 Turning to the question of preparing financial  
25 statements, on June 2 the Finance Board adopted a final rule

1 dealing with the Office of Finance. Among other provisions,  
2 the rule requires that the Office of Finance prepare the  
3 combined financial statements of the Bank System.

4 The Finance Board has been in the practice of  
5 preparing the combined financial statements, because the  
6 Finance Board has been the issuer of the consolidated  
7 obligations for the Federal Home Loan Banks under the  
8 authority of Section 11(c) of the Federal Home Loan Bank  
9 Act.

10 The new Office of Finance rules authorize the  
11 Federal Home Loan Banks to issue consolidated obligations in  
12 their own names through the Office of Finance under the  
13 authority of Section 11(a) of the Bank Act. It was the  
14 expectation of the Banks, the Finance Board and the Office  
15 of Finance that after December 31 of this year, the Finance  
16 Board would no longer issue any consolidated obligations  
17 except for the reopening of certain previously issued  
18 consolidated obligations, which was the subject of the  
19 second resolution.

20 While the requirement for the preparation of  
21 combined financial statements by the Office of Finance  
22 became effective on July 1 of this year, the transfer is  
23 actually being phased in over time to allow for appropriate  
24 staffing, the completion and adoption of appropriate  
25 policies and procedures by the Office of Finance and

1 sufficient opportunity for the Office of Finance to  
2 institutionalize its process for the external audit of the  
3 combined financial statements.

4 In its waiver request, the Office of Finance has  
5 argued that it still requires more time to complete these  
6 tasks. I would note that the preparation of the year-end  
7 2000 combined financial statements will require  
8 collaborative efforts of both the Finance Board staff and  
9 the Office of Finance staff because this is a very complex  
10 undertaking. However, these collaborative efforts will  
11 provide for a seamless transition in the process.

12 The resolution for your consideration would grant  
13 the waiver requested by the Office of Finance and require  
14 that the Office of Finance be responsible for preparing  
15 combined financial statements for the System beginning with  
16 the first quarter of 2001.

17 Turning to the second issue of reopening  
18 previously issued consolidated obligations, as previously  
19 noted the Finance Board recently adopted a rule authorizing  
20 the Banks to issue consolidated obligations through the  
21 Office of Finance under Section 11(a) of the Bank Act.

22 Before the adoption of that rule, all consolidated  
23 obligations had been issued by the Finance Board through the  
24 Office of Finance under the authority of Section 11(c) of  
25 the Bank Act. The expectation has been that all

1 consolidated obligations issued after December 31 of this  
2 year will be issued by the Banks under Section 11(a) of the  
3 Bank Act, and the Finance Board will no longer issue any  
4 consolidated obligations.

5           The Office of Finance often finds it convenient  
6 and economical to reopen certain previously issued  
7 consolidated obligations. For example, if the interest  
8 rate, terms, maturity date and other conditions of a  
9 prospective bond issue are very similar to an existing bond  
10 issue, the Office of Finance may elect to cumulate the new  
11 prospective bond issue on top of the existing bond issue.

12           The benefits of reopening a previously issued bond  
13 issue is that it results in a larger and somewhat more  
14 liquid bond issue, and the added liquidity may marginally  
15 lower the interest rate on the bond. Because the current  
16 debt issuance authorization to the Office of Finance expires  
17 by its own terms on December 31 of this year, the Office of  
18 Finance, without explicit authorization, will not be able to  
19 reopen any bond issues in 2001.

20           There are a number of practical limitations to the  
21 extent to which the Office of Finance can reopen bond  
22 issues. First, reopening generally only works with fixed  
23 rate, noncallable bonds, and this category of bonds is only  
24 about 40 percent of outstanding bond issues.

25           The second practical limitation is that the

1 Treasury Department has very complex rules on original issue  
2 discount and effectively requires that the interest rate on  
3 the new bond and the reopened bond be very, very close.

4 Thirdly, most of the consolidated obligations  
5 issued by the Finance Board under the authority of Section  
6 11(c) of the Bank Act will roll off in several years as  
7 there are relatively few long-term bonds.

8 So the second resolution for reconsideration would  
9 allow the Office of Finance to reopen consolidated  
10 obligations previously issued by the Finance Board under the  
11 authority of Section 11(c) of the Bank Act, and the  
12 resolution places no limitation on this reopening.

13 MR. APGAR: Very good. Since we have two items  
14 that are interrelated, perhaps we should start with a  
15 discussion on the first item. Any questions concerning the  
16 first item?

17 MR. O'NEILL: I just want to compliment the staff.  
18 Obviously the Office of Finance thought that it needed more  
19 time, and I'm happy that any accommodation could be worked  
20 out between the Office of Finance and the staff here, so  
21 thank you for doing that.

22 MR. APGAR: Yes. It seems like getting a seamless  
23 transfer of this function is very important, and this will  
24 accommodate that. It seems like a smart thing to do.

25 Any further comment?



1           If there are no further comments, the vote occurs  
2 on the first Board resolution of waiving the regulatory  
3 requirement that the Office of Finance prepare the combined  
4 financial reports for the year 2000. All in favor say aye.

5           (Chorus of ayes.)

6           MR. APGAR: The ayes have it. The proposed  
7 resolution is adopted.

8           The second issue? Any comments on the second  
9 issue relating to the opening of the bond issues? Again, it  
10 seems like a relatively limited need for this, but in  
11 certain instances it may prove useful and cost effective to  
12 have this.

13          MR. MCKENZIE: This is particularly important for  
14 the tax bond program that the Office of Finance has issued.

15          MR. APGAR: There are some certain categories of a  
16 limited variety where this makes a significant difference.

17          MR. O'NEILL: I always was a little bit uneasy  
18 that the bonds that were being issued, even though they were  
19 done by the Office of Finance, they were being done in our  
20 names. So this relieves that burden.

21          The only other thing -- right now what the Finance  
22 Board always did was issue them under 11(c). In the future,  
23 the Banks are going to issue them under 11(a). Did we ever  
24 issue any bonds under 11(a)?

25          MR. MCKENZIE: No. Eleven (a) deals with the

1 issuance of bonds by the private banks.

2 MR. O'NEILL: So we only issued them under 11(c)?

3 MR. MCKENZIE: Correct.

4 MR. O'NEILL: And in the future is it that the  
5 Office of Finance will only do them under 11(a)? They will  
6 not be able to do new bond issues under 11(c)?

7 MR. MCKENZIE: They will be able to reopen  
8 existing bond issues that were originally issued under  
9 11(c). Next year they can reopen them under the authority  
10 of 11(c), so --

11 MR. APGAR: -- view.

12 MR. BOTHWELL: Yes. As Joe said, the amount of  
13 these types of debt instruments is about 40 percent.

14 MR. MCKENZIE: Yes.

15 MR. BOTHWELL: And they will roll off over time,  
16 so eventually you're going to get to a point where all the  
17 new consolidated obligations are issued under 11(a).

18 MR. O'NEILL: Although in time any of those can be  
19 reopened, so right now, say, it's three or four years before  
20 they all might run off. That might end up being a longer  
21 period of time if any of them are reopened, but there are no  
22 new 11(c) bonds that can be issued by the Office of Finance.  
23 Is that right?

24 MR. BOTHWELL: Correct. After the first of the  
25 year, yes.

1 MR. O'NEILL: Okay.

2 MR. APGAR: Any new questions? Okay. The vote  
3 occurs on the second Board resolution authorizing the Office  
4 of Finance to reopen any consolidated obligations previously  
5 issued by the Finance Board. All in favor of the proposed  
6 resolution say aye.

7 (Chorus of ayes.)

8 MR. APGAR: The ayes have it. The resolution is  
9 adopted.

10 The third item on the agenda is a report on AMA  
11 activities.

12 MR. BOTHWELL: This is the first of the two  
13 informational items. Joe will again present this item.

14 MR. MCKENZIE: Staff is currently preparing a  
15 progress report on the new business activities of the Banks  
16 and changes to their collateral policies.

17 As you know, just over one year ago the Gramm-  
18 Leach-Bliley Act was signed into law, enabling smaller  
19 lenders to have greater access to the Bank System, both in  
20 terms of membership and advances. It authorizes the Banks  
21 to make long-term advances to community financial  
22 institution members for the purpose of providing funds for  
23 small businesses, small farms and small agribusinesses. The  
24 Act also expanded the types of collateral acceptable from  
25 all members to secure advances, by removing the 30 percent

1 limit of member capital on the so-called other real-estate-  
2 related collateral.

3 The Finance Board adopted a final rule on June 29  
4 of this year that amended its regulations to allow the Banks  
5 to accept from CFI members the new categories of collateral  
6 to secure advances. The rule also implemented the Gramm-  
7 Leach-Bliley Act provision that removed the limitation for  
8 all members on the amount of advances that may be secured by  
9 other real estate-related collateral.

10 Under the amended advances regulations, each of  
11 the Banks must file a notice with the Finance Board for any  
12 expansion of their business activities and the acceptance of  
13 new types of collateral eligible to secure advances. Among  
14 other requirements of the new business activity rule, the  
15 Banks must file a notice to maintain or expand the use of  
16 other real estate-related collateral and document their  
17 plans to allow CFI members to pledge newly eligible types of  
18 collateral to support advances.

19 In connection with the new business activities  
20 filings, each Bank must also adopt a member products policy  
21 by November 15 of this year, so as you can see this is very,  
22 very early in the process. The rules only became effective  
23 in July. These new business requirement submissions were  
24 only due several weeks ago.

25 There are three key developments. The Federal

1 Home Loan Banks of Dallas, Topeka, Des Moines and Seattle  
2 have submitted new business activity notices to the Finance  
3 Board that would allow CFIs to pledge new types of  
4 collateral for advances. There are many small, rural banks  
5 in these districts that can benefit from these liberalized  
6 collateral rules.

7 Five of the Banks, New York, Pittsburgh, Atlanta,  
8 Indianapolis and Chicago, will retain their 30 percent cap  
9 on other real estate-related collateral. However, six of  
10 the Banks, Boston, Des Moines, Dallas, San Francisco, Topeka  
11 and Seattle, have proposed to raise their 30 percent cap on  
12 other real estate-related collateral to as high as 200  
13 percent of member capital.

14 Most of the new business activity proposals center  
15 around collateral. The majority of Bank System members  
16 pledge one to four family mortgages as collateral. This is  
17 a function of the fact that most members pledge collateral  
18 under the blanket lien, and five of the 12 Banks lend only  
19 against single-family mortgages under the blanket lien.

20 The blanket lien is somewhat of a difficult  
21 concept to understand. Basically a member pledges blocks of  
22 assets as collateral without either specifying in detail  
23 which of the individual assets or delivering the assets.  
24 Systemwide, 62 percent of all collateral-securing advances  
25 is under the blanket lien, 30 percent is in a listing

1 status, and eight percent is in delivery status.

2 All of the Banks currently accept multi-family  
3 mortgage collateral, but the policies vary from Bank to Bank  
4 on the amount of mortgage, the types of multi-family  
5 mortgage collateral they will accept and the amount of  
6 advances that multi-family mortgages can secure.

7 All of the Banks accept securities as collateral,  
8 but again the policies of the Banks differ in terms of the  
9 amounts of collateral, the amount and types of securities  
10 they will take and the extent to which those securities may  
11 secure advances.

12 Other real estate-related collateral accepted by  
13 some of the Banks includes commercial mortgages, second  
14 mortgages, lines of credit and participation loans. Seven  
15 of the Banks in their collateral policies don't specify  
16 exactly the types of other real estate-related collateral  
17 they'll accept, but rather the decisions are made on a case  
18 by case basis.

19 Looking at the total amount of collateral pledged  
20 in the System, 80 percent of the total collateral is  
21 mortgage loans, 12 percent is mortgage-backed securities,  
22 four percent is other securities, and three percent is other  
23 real estate-related collateral. The Banks have varying  
24 collateral security procedures as determined by their boards  
25 of directors and memberships.

1           During the last two years, the Banks have made  
2 changes to their collateral policies, but most of these  
3 collateral policy changes have been incremental and not  
4 major except for the acceptance of the new types of  
5 collateral from CFI members at several of the Banks.

6           All of the Banks use blanket liens to secure  
7 advances, but the Banks differ among themselves as to what  
8 types of collateral counts under the standard blanket lien.  
9 Although the majority of members remain under the blanket  
10 lien, many commercial Bank members have been reluctant to  
11 provide the Home Loan Banks with a lien on all their assets,  
12 so some of the Banks are developing specialized blanket  
13 liens where a commercial bank or other member will only  
14 pledge portions of their assets.

15           The Banks discount collateral-securing advances.  
16 That is, the market value of the collateral must exceed the  
17 amount of advance. The fact is that determining the amount  
18 of discount or the so-called haircut on the collateral  
19 includes the market risk, the ease with which you could  
20 liquidate the collateral if the Bank had to, the cost of  
21 liquidation and the financial strength of the member.

22           Because of the prevalent use of the blanket lien,  
23 the amount of collateral pledged to secure advances greatly  
24 exceeds the total amount of advances. At September 30, the  
25 Banks had collateral of \$965 billion to secure advances of

1 about \$429 billion.

2 I'd be happy to answer any questions you may have.

3 MR. APGAR: I just have a couple of comments.

4 First of all, I noticed in your presentation the time line  
5 and the date of November 15, 2000, which was the time the  
6 Banks were required to submit their plans, one year and  
7 three days after the enactment of the Gramm-Leach-Bliley  
8 legislation. I think nobody can say that the Finance Board  
9 didn't enable the Banks to move forward with this  
10 particularly important new set of business activities.

11 Now, of course, the ball is squarely in the Banks'  
12 court to develop the capacity and the programs to use these  
13 new authorities, and I'd just like to ask you. Do you think  
14 we're on a reasonable time line for moving forward with this  
15 and have the Banks done the difficult process, or where are  
16 they in the difficult process of staffing up in order to  
17 make sure they have sufficient resources and expertise to  
18 prudently handle these new business lines?

19 MR. MCKENZIE: The Banks are on different stages  
20 of this. Several of the Banks that have been in the  
21 practice of accepting other real estate-related collateral  
22 and have the institutional capacity at those Banks in terms  
23 of appraisers, collateral experts, they're ahead of the  
24 game.

25 There are other Banks that have not been in the



1 process of actively soliciting other real estate-related  
2 collateral. Therefore, they're behind. They're going to  
3 have a different staffing need. It will take, you know,  
4 maybe a year or more to get the Banks fully staffed in this  
5 issue.

6 MR. APGAR: Thanks. It seems now that there are  
7 different levels of expertise. How would you comment on the  
8 just general, overall sense of the kind of haircuts they're  
9 putting on the CFI collateral?

10 MR. MCKENZIE: Well, the Banks are very prudent,  
11 and we would expect that the collateral coverage initially  
12 on the other real estate collateral may be as high as 200  
13 percent. You know, that gradually would come down through  
14 time as the Banks become more familiar in dealing with these  
15 types of collateral.

16 MR. APGAR: So we're in the early stages of a  
17 learning curve?

18 MR. MCKENZIE: Oh, yes.

19 MR. APGAR: Learning a new business, developing  
20 expertise, transferring expertise that already exists to  
21 these new activities --

22 MR. MCKENZIE: That's right.

23 MR. APGAR: -- and getting comfortable with these  
24 new business?

25 MR. MCKENZIE: It's going to be particularly

1 important because the reason a member is pledging other real  
2 estate-related collateral is that they probably don't have  
3 enough sort of plain vanilla collateral to pledge, so it  
4 becomes particularly critical that the Bank ascertain the  
5 value of this collateral because there's basically nothing  
6 else.

7 MR. APGAR: Right.

8 Franz, any questions on this report?

9 MR. LEICHTER: Yes. Just to follow up what you  
10 asked, Mr. Chairman, I first wanted to thank very much Joe  
11 McKenzie for his presentation and really always being  
12 available to provide needed data and information. I'm  
13 grateful.

14 I guess my follow-up to the Chairman's question is  
15 have we seen yet any of these programs in operation? Do we  
16 know how well they're working? Under this new policy and  
17 new powers, have they made advances to member institutions,  
18 particularly CFIs who are making monies available in their  
19 community for community investment and development?

20 MR. MCKENZIE: I think we're still a little too  
21 early.

22 MR. O'NEILL: One thing. There was an article  
23 that was in this month's ABA *Banking Journal* talking about  
24 the North American agricultural finance conference that was  
25 sponsored by the ABA and the American Bankers Association.

1 Pat Conway spoke to that and about what the Des Moines Bank  
2 is doing, so I think Des Moines is probably in the forefront  
3 of this, so slowly but surely things are moving.

4 MR. BOTHWELL: I do believe it's going to be a  
5 matter of emphasis from the Office of Supervision's  
6 standpoint next year as they go and do the Bank examinations  
7 to look at their collateral policies and credit policies, so  
8 this is going to be an area of particular emphasis next  
9 year.

10 MR. APGAR: They're going to want to make sure  
11 that things are in place --

12 MR. BOTHWELL: Exactly.

13 MR. APGAR: -- before we go down.

14 MR. BOTHWELL: Exactly.

15 MR. APGAR: Any other questions or comments on  
16 this report?

17 MR. O'NEILL: I was struck by something that you  
18 said. I note the limit is 30 percent of other than real  
19 estate collateral, but didn't you say that only three  
20 percent is in fact that kind of collateral?

21 MR. MCKENZIE: That's correct.

22 MR. O'NEILL: That seems extraordinarily low.  
23 Which is the highest Bank? Is there any Bank that is close  
24 to the 30 percent?

25 MR. APGAR: A test of memory here.

1 MR. MCKENZIE: We have those numbers. We recently  
2 collected those numbers, and we can give you those numbers  
3 as soon as I have the report with me. It's a number I  
4 haven't committed to memory.

5 MR. O'NEILL: I was just struck. I would have  
6 said it would be like 15 or 20 percent --

7 MR. APGAR: With some bumping up against the  
8 ceiling.

9 MR. O'NEILL: -- with a few bumping up against the  
10 ceiling, but if it's three percent even if there's one Bank  
11 that's up at 20 or 25 percent, you know, there are a lot of  
12 Banks then that would be near zero.

13 MR. APGAR: It doesn't sound like it. It sounds  
14 like they're all pretty low would be my guess on this  
15 number.

16 MR. O'NEILL: Another thing, and this is kind of a  
17 question for not only this discussion, but what we're doing  
18 on capital. Basically now we have twice as much collateral  
19 as we need for advances. When we do what we do on capital,  
20 will that shrink the amount of collateral so that the amount  
21 of collateral will be more in line with the advances or not?

22 MR. BOTHWELL: Our capital should have no impact  
23 on the amount of the collateral that the members hold.  
24 That's on their balance sheets, not on the Home Loan Bank  
25 balance sheets, so there shouldn't be any impact of our

1 collateral rule on -- of our capital rule on the collateral  
2 availability that the members hold to take down advances.

3 MR. O'NEILL: Don't you think that that's a lot of  
4 collateral under such a --

5 MR. MCKENZIE: Well, the reason why there's twice  
6 as much collateral as there is advances, suppose you had a  
7 member that had lots and lots of single-family mortgages  
8 that was pledged under the blanket lien and only had five or  
9 six percent of its liabilities as advances. That particular  
10 member may have 700 percent collateral ratio, so it's really  
11 an artifact of the blanket lien.

12 MR. O'NEILL: And obviously we don't want to do  
13 away with the blanket lien, so I guess we just have to  
14 accept that there will be much more collateral than there is  
15 to fund the advances.

16 MR. APGAR: The options are highly structured,  
17 so --

18 MR. O'NEILL: True.

19 MR. APGAR: -- presumably it was their choice to  
20 engage in a blanket lien as the most effective way to do it.  
21 If there are other less onerous ways to do it presumably  
22 within our guidelines, they could do that as well. You  
23 know, presumably it's a matter -- to some degree a matter of  
24 choice by the members as to how they --

25 MR. O'NEILL: Is there anything in this new

1 collateral rule that will shrink the excess collateral?

2 MR. MCKENZIE: The collateral coverage ratios are  
3 determined by the Banks' boards of directors.

4 MR. O'NEILL: That's certainly as it should be.

5 With regard to the new collateral for small farm  
6 or small agribusiness loans, which of the Federal Home Loan  
7 Banks have been the leaders in that area of small farm or  
8 agribusiness?

9 MR. MCKENZIE: I think the Banks of Des Moines and  
10 Topeka because they have so many members, so many small  
11 agricultural members in both districts. That's the natural  
12 place to look for that development to start taking hold.

13 MR. O'NEILL: Any other Banks other than those two  
14 that has been --

15 MR. BOTHWELL: Dallas.

16 MR. MCKENZIE: Dallas, yes.

17 MR. O'NEILL: And for accepting small business  
18 collateral, which Banks are the leaders in that area?

19 MR. MCKENZIE: Well, I don't think we've had  
20 enough experience. I mean, we did a very extensive  
21 collateral survey effective September 30, and none of the  
22 Banks reported having new types of collateral-securing  
23 advances as of September 30 of this year.

24 Again, the process has been so compressed. Those  
25 rules only became effective -- they became effective in

1 August, so it's very, very early in the process.

2 MR. MCKENZIE: Okay. Thank you.

3 MR. APGAR: Any questions?

4 Okay. Maybe we can turn to our next report then  
5 on acquired member assets and mortgage partnership finance  
6 products.

7 MR. BOTHWELL: Yes, Mr. Chairman. To present this  
8 item, I would ask Scott Smith, the acting director of the  
9 Policy Office.

10 MR. SMITH: Good morning, Directors Apgar,  
11 Leichter and O'Neill. Staff is presenting an update on the  
12 progress of the acquired member assets or AMA programs of  
13 the Federal Home Loan Banks. This update is limited to  
14 single-family mortgage purchase programs that are now active  
15 or specifically the mortgage purchase finance program or MPF  
16 and the mortgage purchase program or MPP.

17 Part 955 of the Federal Housing Finance Board  
18 regulations authorizes the Banks to require member assets, a  
19 category of assets that derives from changes contained in  
20 the Financial Services Modernization Act and from  
21 refinements to the Finance Board requirements for mortgage  
22 purchase programs.

23 Specifically, member assets of a Bank must (1) be  
24 acquired from members or housing associates; (2) be whole  
25 loans that qualify as collateral for Federal Home Loan

1 advances; and (3), be acquired subject to meeting the risk-  
2 sharing requirement where the member credit enhances the  
3 loans or loan pools to at least investment grade. Currently  
4 the member assets required by the Banks are all single-  
5 family home mortgage loans, and it is likely that home  
6 mortgage loans will continue to be the primary type of  
7 assets acquired.

8           If I may now direct your attention to Exhibit 1 in  
9 the Board book? This is also a handout available to the  
10 audience. The broad, upward sloping line shows the volume  
11 in billions of dollars of single-family loans acquired by  
12 the Banks from mid-1997 through October 2000. AMA volume is  
13 now about \$16 billion, most of which was acquired during the  
14 last 12 months.

15           The four wide arrows along the bottom of the  
16 exhibit identify important regulatory actions affecting the  
17 scope and development of today's AMA programs. I'll go  
18 through those four wide arrows in turn. The first arrow to  
19 the left marks the moment the first loans were acquired by  
20 the Chicago Federal Home Loan Bank after they received  
21 approval to proceed with the MPF program as a pilot program  
22 and subject to a \$750 million cap.

23           Resolution 98-41, identified by the second wide  
24 arrow, authorized the expansion of the MPF program to the  
25 other 11 Banks and also a corresponding increase in the cap



1 to \$9 billion. Note that Dallas was approved to participate  
2 shortly thereafter with seven more Banks also receiving  
3 approval to participate in MPF over the next two years.

4 With Resolution 99-50, identified by the third  
5 arrow, the mortgage purchase authority of the Banks was  
6 extended beyond the MPF program to any member mortgage asset  
7 or MMA program that would be approved by the Finance Board.  
8 That is, any program meeting the number nexus and the risk-  
9 sharing requirement specified in the resolution.

10 Resolution 99-50 also liberalized the risk-sharing  
11 requirement in two important ways. First, members could  
12 satisfy a portion of their risk-sharing responsibility  
13 through the purchase of supplemental or deep coverage  
14 mortgage insurance. Second, government-insured or  
15 guaranteed mortgages, specifically FHA, VA and RHS loans,  
16 were for the first time deemed to meet the risk-sharing  
17 requirement. As a result of these changes to the risk-  
18 sharing requirement and following a few months of product  
19 development, member asset volume began to increase sharply.

20 The fourth and final wide arrow identifies Finance  
21 Board approval of the final rule on core mission assets and  
22 acquired member assets. This rule authorized the AMA  
23 programs and as a consequence moved AMA programs from pilot  
24 to permanent status, thus eliminating the \$9 billion cap on  
25 volume. Please note also that the last entry on this time

1 line, final approval of a new AMA program, the mortgage  
2 purchase program, for three Banks, Seattle, Cincinnati and  
3 Indianapolis.

4           However, given that the MPP product is somewhat  
5 different than the MPF product, it involves different  
6 administrative procedures, the Finance Board has imposed a  
7 \$300 million cap per Bank until such time as actual MPP  
8 purchases under the new procedures can be examined to ensure  
9 the safety and soundness of the program operations.

10           MR. O'NEILL: Can I just ask --

11           MR. SMITH: Sure.

12           MR. O'NEILL: -- one question? When the CMA/AMA  
13 rule was done in July, June or July, that was when the cap,  
14 this \$9 billion cap, was off? Is that right?

15           MR. SMITH: Yes. I'm trying to remember now, Jim.  
16 Didn't we have a preliminary relief of the cap for a couple  
17 of weeks there?

18           MR. BOTHWELL: Well, I'm not so sure of that, but  
19 that is when the \$9 billion cap was lifted.

20           MR. SMITH: Yes.

21           MR. O'NEILL: If you look up --

22           MR. SMITH: There was no action, though, for three  
23 weeks.

24           MR. O'NEILL: If you look up at the time that the  
25 \$9 billion cap is removed, we were probably around between

1 \$10 billion and \$11 billion. I think that's why maybe there  
2 was a waiver of --

3 MR. SMITH: There was no action --

4 MR. BOTHWELL: There was no action.

5 MR. SMITH: -- enforced for three weeks in  
6 anticipation of the rule.

7 MR. O'NEILL: Okay. I'm sorry. Okay.

8 MR. APGAR: Let's be clear. The rule was passed  
9 by the Board of Directors on the 26th or 27th of June and  
10 appeared in the Federal Register on --

11 MR. SMITH: I think the 18th of July.

12 MR. APGAR: -- the 18th of July. Yes.

13 MR. BOTHWELL: I think during that time there was  
14 a no action letter.

15 MR. O'NEILL: Okay. I'm sorry for the  
16 interruption.

17 MR. SMITH: It's all right. Figure 2 or Exhibit 2  
18 rather shows the distribution of the current volume of MPF  
19 loans among the different Federal Home Loan Banks. This  
20 distribution reflects the different participation  
21 arrangements among the Banks.

22 In other words, it doesn't reflect what the Banks  
23 have acquired in loans. It reflects that after they  
24 acquired them, they then participate some of them to the  
25 other Banks to sort of spread the loan pools around a bit.

1 I note in particular the Chicago Bank participates in many  
2 of the loan pools, and that helps explain why their volume  
3 is so much greater, as well as the fact that they were the  
4 first Bank in the business.

5 MR. O'NEILL: Glancing at Chart No. 2, is the  
6 reason that the one district is so high, is that because  
7 Norwest, all of those loans came through the Des Moines  
8 district, and that's why that is so high than all the  
9 others?

10 MR. SMITH: For proprietary reasons, I don't think  
11 the Banks like to explain exactly where the -- what the  
12 members are that have contributed to that.

13 MR. O'NEILL: Okay. That's fine.

14 MR. SMITH: Figure 3 shows a rather steady  
15 increase, in fact a 200 percent increase, over the last year  
16 and a half in the number of member institutions that  
17 participate in the MPF program. That number is now  
18 approaching 180 member institutions as PFIs.

19 Finally, Figure 4 shows the master commitments for  
20 the MPF program. The first bar measures the total volume of  
21 all master commitments from the beginning of the program  
22 until now. That number is slightly above \$110 billion. The  
23 second bar shows the volume of master commitments that is  
24 now open and is less than the first bar by the volume of  
25 master commitments that are closed, so that number is now

1 roughly about \$103 billion or \$104 billion.

2 The last bar shows the volume of currently open  
3 master commitments that are available to be filled over the  
4 next year or so. It is less than the second bar by the  
5 volume of current commitments already filled, and so we can  
6 see that there's roughly \$10 billion or \$11 billion of the  
7 currently open commitments that have been filled.

8 Ordinarily the height of that third bar, which is  
9 about \$92 billion, would be an indicator of expected volume  
10 growth during the next year, but the Bank staff, the Chicago  
11 Bank staff in particular, now anticipates that only about  
12 half of that available volume is likely to be filled on the  
13 master commitments. This is no reason other than there were  
14 some overanxious master commitments made.

15 MR. O'NEILL: Is this both the normal program, as  
16 well as FHA?

17 MR. SMITH: FHA, yes. It covers both.

18 MR. O'NEILL: So maybe some of the third one is  
19 because we had a deadline for FHA?

20 MR. SMITH: Right. There was a rush in to build  
21 up some of the FHA master commitments ahead of what a real  
22 analysis of anticipated volumes would be, so they  
23 overestimated.

24 MR. O'NEILL: Okay.

25 MR. SMITH: Finally, the Banks will be subject to

1 new loan data reporting requirements starting in 2001. This  
2 data will be used to monitor the proportion of AMA loans  
3 that represent loans to targeted populations or areas.

4 As we reported to the Board previously, the staff  
5 analysis of MPF data through 1999 indicated that MPF loans  
6 have contributed among these targeted populations and areas  
7 as defined by the GSC housing goals in similar proportions  
8 to the distributions achieved by Fannie Mae and Freddie Mac.

9 With that, I'd be happy to answer any questions.

10 MR. APGAR: Now that the pools are starting to  
11 build obviously the credit enhancements provided by the  
12 members effectively raise the credit quality or rating of  
13 the proposals that appear on the balance sheets of the  
14 Banks, could you talk a little bit about the credit quality  
15 of these, of these pools?

16 MR. SMITH: Yes. Under I believe it was 99-50,  
17 for the first time we allowed their credit-quality pools to  
18 be at a minimum of investment grade. Previous to that they  
19 had to be AA or better, an equivalent of AA or better, the  
20 second highest credit rating category.

21 However, under the current operating guidelines  
22 for MPF and MPP, both programs expect to acquire loan pools  
23 that are rated at least AA, so that's where the pools are  
24 that have been acquired so far and where they expect to be  
25 going forward.

1           MR. APGAR: What about the minimum requirement and  
2 the very solid in the overall safety and soundness  
3 viewpoint?

4           Just picking up on an FHA point, there has been  
5 lots of discussion about the effect of the MPF program on  
6 FHA and a lot of discussion about the fact that the biggest  
7 potential, of course, for these programs is in the  
8 conforming market. Could you talk through that a bit?

9           What share of the growth is reasonably believed  
10 coming out of the FHA, and has there been any recent  
11 changes?

12           MR. SMITH: Well, a great deal of volume, the bulk  
13 of the volume, in the last calendar year has been the FHA  
14 loans, but that's not to suggest that the conventional loan  
15 acquisitions haven't been proceeding and growing at a steady  
16 rate. Again, the Banks would prefer me not to divulge  
17 specific numbers so I'll stay clear of that.

18           I think there was a rush in when the FHA loan  
19 acquisitions were first allowed. There was a very brisk  
20 business in that initially for the program. I think it has  
21 leveled off somewhat as the market for Ginnie Mae's has  
22 adjusted somewhat to the presence of the Federal Home Loan  
23 Banks in that market.

24           MR. APGAR: It does appear that some of the  
25 initial predictions of the significant drain off from Ginnie

1 Mae as a result of this were overstated at best.

2 MR. SMITH: That's right.

3 MR. APGAR: That has launched a bit of a comeback  
4 in spite of the comments that they were doomed. Is that a  
5 fair statement?

6 MR. SMITH: I think that's a fair statement.

7 MR. APGAR: A little bit easier than he might have  
8 in the spring or summer of the year.

9 Do you anticipate the volume to become more evenly  
10 distributed as more Banks get involved? How do you think  
11 that's going to shake out? Now, of course, there are a  
12 couple Banks who are doing the bulk of the business.

13 MR. SMITH: Well, even though a half dozen or so  
14 Banks have been in for six or more months at least, I think  
15 it takes a while for them to build up the number of  
16 participating financial institutions in their district.

17 Each potential PFI has to go through an approval  
18 process where they evaluate the loan quality provided by  
19 that PFI and so on, so it takes a little while for that to  
20 build up, and I think that's starting to happen now. The  
21 volume will be growing at the other districts.

22 In addition, when you look at these volume numbers  
23 by Bank there's another factor involved here, which is that  
24 the Banks that are using the Chicago Federal Home Loan  
25 Bank's back office have to pay a fee to Chicago for that



1 service, and in lieu of paying such a fee they can  
2 participate some of the loans they acquire to Chicago.

3 Many of the Banks have gone down that route, so  
4 early on a fair percentage of their acquisitions are  
5 participated to Chicago. Over time, their fee requirement  
6 goes down and so the participations will start diminishing.  
7 Participations in Chicago will diminish, and you'll see the  
8 volumes grow with the other Banks.

9 MR. O'NEILL: Of the \$7.731 billion in Chicago, do  
10 you have a sense of how much of that came from other Banks  
11 that gave it to them in lieu of a fee?

12 MR. SMITH: That's a good question. I don't  
13 really have that figure. My guess is -- our guess is it's  
14 about half.

15 MR. O'NEILL: About half?

16 MR. SMITH: Don't hold me to that.

17 MR. O'NEILL: You reserve the right to be wrong?

18 MR. APGAR: Okay. That's part of my basic  
19 charter, so I guess it's okay.

20 Just another question. Now we have this MPP out  
21 there, you know, just starting a little bit different  
22 variance on a theme. I guess one Bank is actually  
23 positioned to have both programs operating. Is that  
24 correct?

25 MR. SMITH: That's correct.

1           MR. APGAR: How do you think it's going to play  
2 out? Will it be like the battle of the bands, or different  
3 Banks do you think specialize in one or the other product?

4           MR. SMITH: Well, certainly it presents an  
5 interesting opportunity for there to be such a complication.  
6 I don't know whether it's going to play out that way. I  
7 think the intention of this is the Indianapolis Bank --

8           MR. APGAR: Right.

9           MR. SMITH: -- that's approved under both MPP and  
10 MPF. I think it's the intention of the Indianapolis Bank to  
11 proceed with MPP for their conventional business.

12           Initially their approval for MPF as they conveyed  
13 it to us was really designed for the FHA business, so we'll  
14 see. They have the authority to do FHA business under MPP  
15 as well, so we'll have to wait and see what they do.

16           MR. APGAR: It really struck me that the hallmark  
17 of all of this was although MPF was first out of the gate  
18 and obviously built up some degree of momentum that there  
19 are a lot of other ways you could potentially structure  
20 products under these broad goals only limited by the Bank's  
21 innovation and our capacity to make sure that these new  
22 activities are safe and sound and so we'll see a lot of  
23 experimentation and trial in the marketplace to see which  
24 products best work.

25           Maybe one of these new MPP or something else, will

1 emerge as a significant rival in terms of activity levels to  
2 the MPF program.

3 MR. SMITH: Well, as time goes on the Banks learn  
4 what works for the membership and what doesn't. As you say,  
5 there are new ideas that evolve so we'll see. I think the  
6 products are only going to get better.

7 MR. APGAR: Now, you didn't mention or I didn't  
8 hear you mention in your report any activity relating to  
9 multi-family, although I know some Banks are experimenting  
10 with programs in the multi-family arena. Could you speak a  
11 little bit about that?

12 MR. SMITH: The multi-family programs we have  
13 underway currently are not structured the same way as the  
14 AMA with the risk sharing. It's different, and they  
15 basically qualify under the target investment authority that  
16 we now have.

17 MR. APGAR: There's no reason why they couldn't  
18 be?

19 MR. SMITH: The Banks have been exploring trying  
20 to set them up as AMA programs. There is difficulty in  
21 terms of data available to do the -- calculate what credit  
22 enhancement is necessary to raise those multi-family --

23 MR. O'NEILL: Didn't we grandfather all of the  
24 existing pilots at the time that we did the CMA/AMA? All of  
25 the existing pilots were grandfathered so they did count for

1 AMA. Isn't that right?

2 MR. SMITH: Well, they count. The question is do  
3 they count as core mission assets. That's the question, and  
4 the answer is yes, they're grandfathered in.

5 MR. O'NEILL: But they're not grandfathered to be  
6 part of these charts?

7 MR. BOTHWELL: Well, there's a distinction there  
8 between an acquired member asset and a core mission asset.  
9 Some of those problems that we're talking about in multi-  
10 family didn't meet the credit risk sharing requirements of  
11 the AMA assets, so they're not included in these AMA  
12 figures. They were, however, grandfathered to count as the  
13 core mission assets in our definition of what a core mission  
14 asset is.

15 As Scott said and as the Chairman said, our rule  
16 provides a great deal of flexibility to create more AMA type  
17 of products, and hopefully the Banks will continue to be  
18 innovative in this area and design a multi-family product  
19 that meets the AMA risk sharing requirements and number  
20 nexus requirements.

21 In fact, with our new business activity  
22 requirement now all they'd need to do if they're going to  
23 present us with a different product is give us 60 days  
24 notice. During that time we'll look at their product and  
25 assure ourselves that this product can be -- is safe and

1 sound and that they have the necessary expertise and  
2 procedures and so on, and then they can go ahead after the  
3 end of that 60 day period.

4 MR. O'NEILL: For example, the pilots that were  
5 there originally. Do the Atlanta pilot, the CICNC pilot,  
6 and -- well, now it's in the whole district. Originally it  
7 was just in North Carolina. Does that count as AMA or not?

8 MR. SMITH: No, but it does count as a core  
9 mission asset.

10 MR. O'NEILL: How about New York's --

11 MR. SMITH: CMA?

12 MR. O'NEILL: -- CMA, and then after that it was  
13 the sequential participation?

14 MR. SMITH: Sequential is a separate product under  
15 CMA that would count as AMA because the risk sharing  
16 structure is different than the rest of the CMA program.  
17 The original CMA program would not count as AMA.

18 MR. O'NEILL: And my personal favorite -- when I  
19 was young, it took me a while to get a down payment -- is  
20 Seattle's rent to own. Is that counted under AMA or not?

21 MR. SMITH: I believe that counts under CMA again.  
22 I don't think the -- the risk sharing is not set up the  
23 same.

24 MR. O'NEILL: Okay.

25 MR. APGAR: Scott?

1 MR. LEICHTER: Did I understand you to say that we  
2 don't know what percentage of the MPF program is in FHA?

3 MR. SMITH: I'm saying we know. I'm not --

4 MR. BOTHWELL: He doesn't have the number with  
5 him.

6 MR. SMITH: I don't have the number with me, and  
7 the Banks would prefer if I don't hand out specific numbers  
8 on that for proprietary reasons. I can tell you later.

9 MR. LEICHTER: Yes. No. I'm just -- I won't  
10 press the issue. I'm just a little surprised. I kind of  
11 know why it shouldn't be a public figure.

12 It's something we can assess not only as Board  
13 members if confidentially given the information, but, I  
14 mean, in looking at the program and seeing how it works and  
15 the benefits it provides, certainly a degree or the  
16 percentage that's FHA I think is a significant indicator.

17 MR. SMITH: It's common knowledge. I'll suggest  
18 it's more than half. I mean, it's common knowledge.

19 MR. BOTHWELL: I would add that the fear that I  
20 think existed was that the FHA business was easier to do  
21 and, therefore, would drive out any of the conventional loan  
22 business. That was, I think, a primary reason why the Board  
23 acted to place a ceiling on the amount of FHA loans that  
24 could be counted as core mission.

25 That really hasn't been realized, and in fact the

1 volumes of incremental volumes of the conventional loans if  
2 anything have been increasing in terms of percentage, you  
3 know, of conventional/FHA. That fear I don't think has been  
4 actually realized.

5 MR. SMITH: I think there were adjustments made in  
6 the FHA market in part because of our presence, but because  
7 of other things going on that I think really slowed down the  
8 concerns and the rush of trying to do that sort of business.

9 If I could return for a moment to your question  
10 about the multi-family, what I was trying to say before is  
11 that in the single family marketplace there's a great more  
12 understanding and data available to work with to develop  
13 models that are used to assess the credit quality of the  
14 pools that are purchased. This has not happened in the  
15 multi-family market as yet, and that's what largely is  
16 holding the Banks back from developing.

17 As that research moves forward and models are  
18 developed for multi-family, I think the Banks will be fairly  
19 quick to move into that business.

20 MR. APGAR: As critical as it is to provide new  
21 sources of funding for the single-family market, it's even  
22 more so in the multi-family market, and that's an area  
23 certainly in need. One can hope that as new flexibility is  
24 granted to the Banks, we'll reap the payoff in extra funding  
25 of multi-family development, which, of course, would support

1 the national needs.

2 MR. LEICHTER: Atlanta has a program, right,  
3 that --

4 MR. SMITH: Yes.

5 MR. LEICHTER: -- is for multi-family?

6 MR. SMITH: They have a program. The risk sharing  
7 again is different --

8 MR. LEICHTER: Yes.

9 MR. SMITH: -- than it is for the AMA program.  
10 The volume on that program is very small at the moment.  
11 It's under \$20 million. That's been in place for a couple  
12 years.

13 MR. O'NEILL: Doesn't Boston also have a multi-  
14 family program?

15 MR. SMITH: They have authority to proceed on one.  
16 I don't believe they have done very much business.

17 MR. APGAR: They were working on another, I don't  
18 know if it's called pilot or not, but an arrangement to try  
19 to figure out how to make better use of FHA small loan  
20 processing. Many of their members would like to have  
21 engaged in FHA business, but the size of the loans made it  
22 difficult to work under the conventional program.

23 They were working jointly with our offices, our  
24 HUD Office of Multi-Family Finance, to see if they could  
25 come up with an arrangement where the Bank could work with



1 members and our FHA staff to make that program more flexible  
2 and usable. They've made some progress on that, though it's  
3 a tricky business. Financing of these small, multi-family  
4 developments is one of the big challenges facing the  
5 industry still.

6 MR. LEICHTER: Is there anything that we can do  
7 which would make or facilitate the Banks being more involved  
8 in multi-family activities? I think we've certainly seen  
9 the need that we ought to urge the Banks to become more  
10 involved in this area.

11 MR. BOTHWELL: Well, the question, you know, is we  
12 always have our job to do, but in addition to that I think  
13 next year when we come back to the Board to present and  
14 discuss and further this issue about assessing goals for the  
15 AMA program that there you might want to consider, as HUD  
16 has done for Fannie and Freddie, maybe some multiplier for  
17 the multi-family type of loans so we have an incentive in  
18 that way. I think that's very much something that the Board  
19 might consider at that time.

20 MR. LEICHTER: You say this is something that  
21 we'll be doing next year?

22 MR. APGAR: Well, as you know, -- by  
23 administrating the data collection --

24 MR. LEICHTER: Yes.

25 MR. APGAR: -- and other things. We just can't

1 launch into a goal setting operation without, you know,  
2 fundamental information.

3           There was a two stage process, I imagine, where we  
4 begin to collect more detailed data on AMA activity and then  
5 based on that see what would be prudent. Obviously the  
6 analog between Fannie and Freddie is only culled so far  
7 obviously.

8           All of us are operating in discovering a  
9 responsive enterprise environment, so, therefore, some  
10 public responsibilities are appropriate, but they're  
11 fundamentally different organizations, Fannie and Freddie,  
12 versus the Banks, so you can't just take the regime --

13           MR. LEICHTER: Right.

14           MR. APGAR: -- from goal setting and do it over  
15 whole cloth, but, you know, I think the goal that we passed  
16 sets up a way of moving in that direction, and I think that  
17 that will be an important activity to look at in the future.

18           MR. O'NEILL: Can I ask a question about the MPP  
19 program? Right now there's a \$300 million cap for each of  
20 the three Banks. Are any of the Banks near that cap? Where  
21 are the three Banks?

22           MR. SMITH: I don't think any of the Banks have  
23 done their first deal yet.

24           MR. BOTHWELL: They're at zero right now. They  
25 have the authority, and they're talking with the members

1 that are --

2 MR. APGAR: I think the announcement that they  
3 were approved to do this was October 30.

4 MR. SMITH: Yes. Yes, so they're very early on.  
5 They're all I'm sure anxious to get their first deal done,  
6 and it may happen in the next couple of weeks.

7 MR. O'NEILL: Do you think that when they finally  
8 do the first deal would they -- how long do you think before  
9 they will have a problem with the \$300 million cap?

10 MR. SMITH: We don't anticipate they'll ever have  
11 a problem with it in that the purpose of the cap is just to  
12 guarantee some time for the Office of Supervision to go in  
13 to evaluate their operations after they've actually done  
14 some deals, so as long as their first deals are small in  
15 volume, which the Banks anticipate anyway, then there should  
16 be more than sufficient time for the Office of Supervision  
17 to go in and review the operation and if everything is fine  
18 grant them approval effectively lifting the -- to go beyond  
19 the \$300 million.

20 MR. O'NEILL: To go beyond the \$300 million, will  
21 that have to come to the Board of Directors, or is that  
22 something that the Office of Supervision can lift on their  
23 own?

24 MR. SMITH: I believe that's Office of  
25 Supervision's --

1           MR. BOTHWELL: Right. Yes. It is the condition  
2 of the program that the Finance Board granted, and so the  
3 Finance Board can take off the \$300 million once the Office  
4 of Supervision gets in there and there's enough activity and  
5 enough experience that, you know, they can look at the  
6 Banks' operation and they get comfortable. We can just  
7 remove that. No one anticipates this being an impediment to  
8 business.

9           MR. O'NEILL: I just want to make sure. I mean, I  
10 don't know. To me, \$300 million is a fairly low cap. I  
11 don't know what kind of volume the first couple of projects  
12 will be, but I just want to make sure that we don't strangle  
13 that one.

14           MR. APGAR: I would just submit it's exactly the  
15 opposite. By going this route and giving them permission to  
16 start with a test actually accelerated their capacity to  
17 move into the marketplace. Absent that, the Office of  
18 Supervision would have had to have done significant  
19 additional reviews, would have required sufficient  
20 additional documentation so they could have been sure that  
21 this was okay.

22           So this is kind of a compromise between getting it  
23 all buttoned down on day one and turning them loose and  
24 saying hey, during this provisional period while we're  
25 watching how this thing is working in practice we'll have a

1 cap in place with the full expectation because we wouldn't  
2 have gone down this route if there wasn't a full expectation  
3 that the additional reviews of the Office of Supervision  
4 will find and support their initial sense that this was a  
5 worthy activity.

6 Modifications would only be on the margins and  
7 not, you know, basic in that, in fact, in due course the  
8 program will be approved for full operation.

9 MR. O'NEILL: Well, I just want to make sure that  
10 the staff is acceptive of that and that we don't get into a  
11 situation where any of the Banks get close to the cap and  
12 the Office of Supervision is still kind of hemming and  
13 hawing around.

14 I assume that that will not be the case, but I  
15 just want to make sure that we, just as we did -- I mean, in  
16 one case there was a no action letter to make sure that the  
17 Chicago Pilot didn't bump up against the \$9 billion cap;  
18 that we are sensitive that we don't strangle this program  
19 similarly.

20 MR. APGAR: I guess if, you know, we look at the  
21 growth lines of the MPF program since December, which is  
22 when the critical date was, the 99-50 letter, it's as pretty  
23 much a straight line up as you can get. It's hard to see  
24 where anybody was strangled over that period, but we take  
25 your point, and I'm sure the Office of Supervision takes

1 your point now, too.

2 MR. BOTHWELL: I assure you that --

3 MR. O'NEILL: You know, obviously if for some  
4 reason the Office of Supervision isn't yet satisfied, I  
5 guess we could always as a Board --

6 MR. APGAR: Intervene.

7 MR. O'NEILL: -- intervene with a no action letter  
8 and whatever else to make sure that that doesn't happen.

9 MR. APGAR: Any other comments? Great.

10 Before we adjourn, I have just one matter I wanted  
11 to bring up. As you all know, there are a lot of financial  
12 institutions and holding companies, over 100 I guess, with  
13 financial institution subsidiaries that are located in and  
14 doing business in more than one Federal Home Loan Bank  
15 district and, of course, more and more this is the trend.  
16 Holding companies have a natural presence, and continuous  
17 consolidation of the industry makes this just more and more  
18 significant.

19 It's critical for the Finance Board to address the  
20 effects of this industry bound consolidation on the Home  
21 Loan Bank System, the impact that continued consolidation  
22 will have on the cooperative nature of the System, on the  
23 economics of the System, especially as all this plays out  
24 under the new Capital Rule.

25 Therefore, it seemed prudent at this stage when

1 we're on the edge of putting a new Capital Rule into place  
2 that we begin a serious review, and I've asked the staff to  
3 begin a review to research and study and analyze the issues  
4 that relate to this growing national consolidation of the  
5 banking industry and prepare to make a preliminary report  
6 back to the Board in the new year on these important issues.

7 With respect to this issue, it's come to our  
8 attention that some members may be interested in exploring  
9 their ability to seek membership in adjoining Federal Home  
10 Loan Bank districts or even a multiple Federal Home Loan  
11 Bank membership. On that matter I just want to point out  
12 that we already have provisions in place for handling any  
13 requests of that nature that would come forward.

14 The Board has a public process whereby Federal  
15 Home Loan Banks and their members may explore such issues of  
16 membership with the Finance Board, and those procedures are  
17 present in our regulations. I note here that interested  
18 folks could look at 12 CFR, Part 907, subpart (c), so while  
19 we research and analyze and prepare ourselves for this broad  
20 set of global issues, we're also well positioned to handle  
21 any particular matter that may come before the Board that  
22 can be well handled under our existing procedures.

23 I just wanted to make that note. I know that both  
24 my colleagues have been interested in this topic as well.  
25 I've had conversations with both of them.

1 Franz, do you have any further comments on this  
2 general topic?

3 MR. LEICHTER: No. I very much appreciate your  
4 comments, Chairman. I think this is an incredibly important  
5 issue for the System. Obviously when the System was  
6 established and as it evolved with the 12 Banks we certainly  
7 didn't have in mind that we would have these national banks  
8 and banks that would have activity in the multi districts.

9 I think the structure we have is not well suited  
10 for the changes that have occurred in the industry. As you  
11 rightly point out, there's been much consolidation of late,  
12 and this is obviously going to continue. As these mergers  
13 or acquisitions or consolidations occur, it could create  
14 imbalances in one or more Banks. It could really create  
15 some destabilization.

16 So I think it's very important that we address  
17 this, and it may well be that we will want to even at some  
18 point soon announce that we're going to have is it ANPR,  
19 announced proposed -- wait a second. Announced --

20 MR. BOTHWELL: Announced notice of public rule  
21 making.

22 MR. LEICHTER: Advanced notice of proposed rule  
23 and establish a formal procedure because I think that is  
24 really one of the most important issues that we need to  
25 address.



1           I just want to say that while we study this, and  
2 obviously we need to come up with a System-wide resolution,  
3 that there may be individual cases in the interim that we  
4 will need to address. I just want to say that speaking for  
5 myself that if an appropriate case is made and an  
6 application is submitted to the Board to try to deal with  
7 the effects of an acquisition where we might feel that there  
8 will be an imbalance created in one or more Banks that we  
9 will need to deal with that promptly.

10           I'm not sure on the procedures because there's I  
11 think different approaches. I think we need to look and to  
12 see how we proceed. You mentioned one way, Mr. Chairman.  
13 There may be other ways, interpretive regulations and so on.

14           The statute, the regulations, do maybe somewhat  
15 obliquely, but they do address the issue of a bank having a  
16 membership that is not in the district of its principal  
17 place of office, so I think there are tools available for us  
18 to deal with it. I just want to say, speaking for myself,  
19 and I'm sure I speak for the Board and the staff, this is  
20 something that we will address very promptly and very  
21 readily if we feel that there's a situation that requires  
22 administrative relief.

23           MR. APGAR: Yes. With respect to the effects of  
24 bank members to as a convenience join other Banks, we've  
25 handled cases like that in the past. As I mentioned, there

1 are procedures in place. Clearly these are significant  
2 matters, and they will need to be handled in a full and open  
3 manner.

4 Like I said, I think we are well positioned to  
5 handle any immediate situation that may arise, and we also  
6 are building capacity in understanding to deal with the more  
7 fundamental issues over the near term.

8 MR. O'NEILL: Both of your remarks I strongly  
9 second, and I agree that there really are two things going  
10 on here. There is the more national issue that we need to  
11 get a handle on as soon as we can, so thank you for asking  
12 the staff to start looking at that, but then there probably  
13 are some more immediate examples of that that we have to  
14 deal with more promptly than maybe the overall issue gets  
15 resolved.

16 I think all of us agree that we should do this as  
17 a regulatory matter rather than any kind of legislation in  
18 this area, so I think that it's good that we are talking  
19 about it now and that if something comes up that we will  
20 look at it and look at it promptly, so I think that -- I  
21 hope that the people on Capitol Hill will take note that  
22 we're going to be dealing with this ourselves and that we  
23 will not go down the lane of more legislation because I  
24 think that that is fraught with uncertainty if we go down  
25 that path.

1 I really thank both of you for all that you've  
2 said, and I think that this is a very important issue for  
3 the next year, but even something more immediately than that  
4 if things come up.

5 MR. APGAR: Right. With respect to the last  
6 comment, obviously these matters are significant. They go  
7 to the heart of the nature of the System.

8 My interest is having a full and open discussion  
9 of this, and I also share your view that our House and  
10 Senate, with oversight of these activities, will share our  
11 understanding of the important nature of this and also  
12 choose to move in a deliberate fashion following a full and  
13 open airing of any matters that may arise in the near  
14 future.

15 Any comment on this matter? Okay.

16 Just one note. I arrived in the office this  
17 morning, and I had the opportunity to read a reasonably --  
18 although the article wasn't so sensational, the headline  
19 appeared to be in American Banker. I just wanted to comment  
20 because there seemed to be a couple of items that were mis-  
21 stated.

22 The American Banker reviewed the comments received  
23 from our proposed rule making and noted that many Banks  
24 objected to what we were doing. The obvious point, of  
25 course, is that's why you have proposed rule making.

1           We have been very open, I believe. As a matter of  
2 fact, I don't think there's any issue that was raised in the  
3 article that wasn't fully discussed at our last Board  
4 meeting where we identified the ten or 12 or maybe it's up  
5 to 15 key issues that we needed to work on in response to  
6 the proposed rule.

7           I think it's safe to say that as a result of those  
8 dialogues with our banking colleagues, both Banks and  
9 members, that we are well along to identifying resolutions  
10 to most of the issues raised by those comments, and we  
11 perceive that the rule as it's put in final form will  
12 satisfy most of the concerns raised in that.

13           My central issue was they also hinted at the idea  
14 that the Housing Finance Board was about to be quorumless,  
15 and so I quickly checked Franz's and Tim's heart rates and  
16 found out they were healthy. I noted that they are still  
17 two important nominations before the Senate, Al Memdelowitz,  
18 who has joined us here today, Doug Miller, and so we have  
19 plenty of talent in the wings. Then we start with the HUD  
20 Secretary's representatives.

21           The only thing I can say that I'm sure of in all  
22 of this, even though I took the heart rates and Senate  
23 confirmation, is that there will be a HUD representative on  
24 this Board no matter who is the President of the United  
25 States. Therefore, we will have a quorum on January 21

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24 this Board no matter who is the President of the United  
25 States. Therefore, we will have a quorum on January 21

1 because that automatically is vested in HUD to assign a  
2 representative to the Board.

3 We have a lot of work before us between now and  
4 January. We have a lot of work before this Board between  
5 now and the next year to take on these important matters.  
6 Lack of a quorum will not be one of our problems. I think  
7 that's safe to say.

8 With that, I also think we could end the meeting  
9 where we began. In the tradition of many bodies of this  
10 type, we'll adjourn the meeting in the memory of Henry B.  
11 Gonzalez, who ultimately got us all here in the first place.

12 Thank you very much.

13 (Whereupon, at 11:28 a.m. the meeting in the  
14 above-entitled matter was concluded.)

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REPORTER'S CERTIFICATE

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DOCKET NO.: --  
CASE TITLE: Federal Housing Finance Board Open Meeting  
HEARING DATE: November 30, 2000  
LOCATION: Washington, D.C.

I hereby certify that the proceedings and evidence are contained fully and accurately on the tapes and notes reported by me at the meeting in the above case of the Federal Housing Finance Board.

Date: November 30, 2000



Gabriel Thomas

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