2010 PERFORMANCE and ACCOUNTABILITY REPORT

MANAGING THROUGH THE HOUSING CRISIS
PREPARING FOR THE FUTURE

FEDERAL HOUSING FINANCE AGENCY

FHFA'S MISSION

Provide effective supervision, regulation, and housing mission oversight of Fannie Mae, Freddie Mac, and the Federal Home Loan Banks to promote their safety and soundness, support housing finance and affordable housing, and support a stable and liquid mortgage market.

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Federal Housing Finance Agency Key Management Officials . . . inside back cover

Message from the FHFA Acting Director

I am pleased to present the Federal Housing Finance Agency's (FHFA's) *FY 2010 Performance and Accountability Report*. During FY 2010, FHFA supervised the 14 housing-related government-sponsored enterprises (GSEs) to promote their safety and soundness and their fulfillment of their housing finance mission. FHFA regulates the Federal National Mortgage Association (Fannie Mae), the Federal Home Loan Mortgage Corporation (Freddie Mac), and the Federal Home Loan Bank System – the 12 Federal Home Loan Banks (FHLBanks) and the FHLBanks' fiscal agent, the Office of Finance.

During the past two years, FHFA has been at the center of many of the federal government's efforts to respond to the crisis in the nation's housing and housing finance markets. FHFA continues to work with the Administration and Congress to respond to the problems for borrowers, communities, and investors posed by seriously delinquent mortgages, to develop alternatives for restructuring the housing finance system, and to find long-term solutions to the many challenges facing the housing market.

Each year FHFA produces an Annual Performance Plan that outlines FHFA's strategic goals and performance measures to track the agency's progress toward achieving its mission. This report describes the agency's record against its FY 2010 goals and performance measures as set forth in the FY 2010 Annual Performance Plan.

Managing Through the Financial Crisis

Enterprises

In September 2008, FHFA placed Fannie Mae and Freddie Mac (the Enterprises) into conservatorships—actions designed to stabilize the financially-troubled institutions. In conjunction with that action, the Treasury Department, exercising authority granted by Congress in the Housing and Economic Recovery Act of 2008, agreed to provide financial support to the Enterprises through the Senior Preferred Stock Purchase Agreements. The agreements ensure the Enterprises maintain a positive net worth so they may continue to be active suppliers of housing finance. The agreements are ongoing, explicit, and irreversible contractual commitments of the federal government ensuring that Fannie Mae and Freddie Mac can meet their obligations and maintain a positive net worth.

While in conservatorship, the Enterprises have continued to fulfill their mission of providing liquidity and stability in the secondary mortgage market. The Enterprises serve a vital role by linking local lenders with international capital markets. In FY 2010, the Enterprises purchased 60 percent of single-family originations, which was down from 65 percent in 2009, but still the dominant share of the market.

As conservator and safety and soundness regulator, FHFA acts to ensure that Fannie Mae and Freddie Mac minimize losses and undertake only activities tied to their core responsibilities. With continuing uncertainty about economic conditions, employment, housing prices, and mortgage delinquency rates, the outlook for the Enterprises remains unclear, and they are likely to require additional draws under the Senior Preferred Stock Agreements.

Federal Home Loan Banks

The FHLBank System also faces challenges stemming from weakness in domestic housing markets. Banks that invested in residential private-label mortgage-backed securities (private-label MBS) in 2005-2008 have generally experienced other than temporary impairment (OTTI) on those investments, which has reduced income and in one case contributed to the particular FHLBank being characterized by FHFA as "undercapitalized" pursuant to the agency's prompt corrective action regulation.

The FHLBanks have also experienced a decline in core mission assets, particularly loans to member institutions, known as "advances." Advances grew rapidly in 2007 and 2008 in response to liquidity strains in financial markets, topping $1 trillion by October 2008. After peaking in 2008, advances have declined steadily as liquidity pressures in the markets eased, member deposits increased, and loan demand slowed. Advances dropped to $631 billion by year-end 2009 and $500 billion by the end of the fourth quarter of FY 2010.

Against a backdrop of falling housing prices and rising mortgage delinquencies and foreclosures, FHLBank investments in private-label MBS were a source of concern at several FHLBanks as severe and widespread economic weakness caused significant deterioration in these securities. As of September 30, 2010, the FHLBanks held private-label MBS equivalent to 4.5 percent of assets. To date, shortfalls of principal or interest have occurred on only 1 percent of private-label MBS held by the FHLBanks, but collectively the FHLBanks have recognized $3.3 billion in credit-related impairments and an additional $10.8 billion in noncredit-related, other-than-temporary-impairments on these investments.

FHFA urged the FHLBanks to focus on returning to more traditional operations and activities, particularly their core mission of making advances. FHFA also encouraged the FHLBanks to reduce investment portfolios not needed to support core business activities and safe and sound operations. FHFA made major changes to its regulations governing the FHLBanks' funding arm, the Office of Finance, expanding its board of directors from 3 to 17 members. The new board of directors is comprised of the 12 FHLBank presidents and 5 independent directors.

Preparing for the Future

Although the Enterprises have been operating in conservatorships for two years, they have continued to support the housing finance system and have played a key role in housing finance. However, the Enterprises have relied on support from the Treasury Department in order to maintain a positive net worth and to carry out their responsibilities to support housing finance. FHFA will continue to focus the Enterprises on foreclosure alternatives designed to reduce credit losses on delinquent mortgages. FHFA will also focus on ensuring the Enterprises continue their core business activities of providing stability and liquidity to the secondary mortgage market while ensuring prudent underwriting of new business.

Under the Dodd-Frank Wall Street Reform and Consumer Protection Act, enacted on July 21, 2010, FHFA became a member of the Financial Stability and Oversight Council (FSOC). FSOC will coordinate regulatory activities to address systemic risk issues, designate systemically important non-bank financial institutions and financial market utilities for regulation by the Federal Reserve System, and recommend prudential measures to the Federal Reserve and other regulators to head off threats. The Dodd-Frank Act also directed FHFA to work with other regulators in rulemakings concerning mortgage underwriting standards, derivatives, and executive compensation.

A major focus for the Administration and Congress in FY2011 will be legislation on the future of the housing finance system. FHFA will provide information, analysis, and insight to both the Administration and Congress as this legislation develops.

While addressing the many challenges related to overseeing the regulated entities, FHFA will continue to enhance the infrastructure, policies, and processes needed to operate effectively. These important building block activities will serve as the foundation for accomplishing the agency's mission in the years ahead.

Program Data and Financial Performance

This report contains complete and reliable performance and financial data for FHFA, and, where appropriate, notes data limitations in connection with specific performance goals. Based on the agency's assessment of internal controls and compliance with OMB Circular A-123, I can provide reasonable assurance that the agency's risk management and internal control systems, taken as a whole, conform to the standards prescribed by the Government Accountability Office and the Federal Managers' Financial Integrity Act. The details of management assurances can be found in the "Management's Discussion and Analysis" section of the report.

In FY 2010, FHFA received an unqualified audit opinion on its financial statements from the Government Accountability Office. FHFA met or exceeded 12 (46 percent) of its performance goals and did not meet 14 (54 percent). Several of the 14 goals were fully or mostly achieved as of this report but not under the timeframes established in the Annual Performance Plan. Others were not met due to the impact of external market events.

Conclusion

FHFA has existed as an agency for only two years. In the past fiscal year, FHFA continued to establish itself as a new federal regulator dedicated to its mission of supporting the nation's housing finance system through oversight of its regulated entities.

Though the challenges ahead are significant, and the economic climate is difficult, I am optimistic about FHFA's future. The explanation for my optimism is threefold. First, FHFA staff is working tirelessly to meet the unprecedented challenges facing the agency and the housing markets. They are smart, eager, and forward-looking. They represent the best in public service, and I look forward to working with them as we strive to improve our nation's housing finance system. Second, we continue to build staff and strengthen the agency's operational infrastructure. Finally, we remain focused on the goal of strengthening our prudential supervision of the regulated entities.

Edward J. DeMarco

Edward J. DeMarco
Acting Director
November 15, 2010

Fiscal Year 2010 Performance and Accountability Report

Overview

The Federal Housing Finance Agency (FHFA) annually prepares and issues its *Performance and Accountability Report* (PAR) to describe and quantify its fiscal year performance relative to the goals and measures set forth in its annual performance plan. Publicly releasing this information promotes transparency in FHFA's operations and improves the public's understanding of FHFA's operations and accomplishments.

The 2010 PAR has four sections: Management's Discussion and Analysis, Performance Section, Financial Section, and the Appendix. The purpose and content of those four sections are summarized in the table below.

Section of Report	Section Purpose and Contents
Management's Discussion and Analysis	• FHFA's Mission • FHFA's Values • Description of FHFA • Performance Highlights • Management Challenges • FY 2010 Performance Summary • FY 2010 Financial Summary • Statement of Assurance from FHFA Acting Director
Performance Section	• Managing and Measuring Performance • Strategic Goal 1 (Safety and Soundness) • Strategic Goal 2 (Affordable Housing) • Strategic Goal 3 (Conservatorship) • Resource Management Strategy
Financial Section	• Message from the Chief Financial Officer • Report of Independent Auditors • Financial Statements • Notes to Financial Statements
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Management's Discussion and Analysis

FHFA's Mission

FHFA's Values

Description of FHFA

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Statement of Assurance from FHFA Acting Director

FHFA'S MISSION

Provide effective supervision, regulation, and housing mission oversight of Fannie Mae, Freddie Mac, and the Federal Home Loan Banks to promote their safety and soundness, support housing finance and affordable housing, and support a stable and liquid mortgage market.

FHFA's Values

- ***Accountability***
  We foster responsibility on the part of individual employees and divisions through defined delegations of authority. We align our actions and resources with our mission and respond promptly and proactively to emerging risks. We adhere to a predictable, risk-based supervision program. We use agency resources and authorities efficiently and effectively to achieve our mission and goals.
- ***Responsiveness***
  We cooperate, collaborate, and communicate within FHFA, with other government agencies, Congress, and the public. We respond promptly to external requests and regularly disseminate information about the housing industry and markets. We promptly address and clearly communicate issues, decisions, and conclusions to the regulated entities.
- ***Independence***
  We are the independent regulator of Fannie Mae, Freddie Mac, and the Federal Home Loan Banks. Our evaluations of the regulated entities are unbiased and remain free from external influence.
- ***Integrity***
  We adhere to the highest ethical and professional standards. We treat the regulated entities, the public, policy makers and other stakeholders fairly with impartiality and respect. We apply consistent treatment to and among the housing regulated entities and base our decisions on the merits of their current actions and conditions.
- ***Professionalism***
  We maintain a highly skilled, dedicated, and diverse workforce. We promote equal opportunity and advancement on the basis of merit. We recognize employees who demonstrate competence and effectiveness in their decisions and actions and whose results serve the agency's mission and the public interest. We judge the regulated entities against defined industry standards through a disciplined examination approach.

Description of FHFA

The Housing and Economic Recovery Act of 2008 (HERA) established FHFA by merging the Office of Federal Housing Enterprise Oversight, the Federal Housing Finance Board, and certain Department of Housing and Urban Development's (HUD) staff, to oversee the financial safety and soundness and the housing mission compliance of the housing-related government-sponsored enterprises (GSEs or regulated entities). These include Fannie Mae, Freddie Mac, and the FHLB System, comprised of 12 Federal Home Loan Banks.

FHFA is an independent government agency with a workforce that includes highly skilled economists, analysts, examiners, subject matter experts, technology specialists, accountants, and attorneys. FHFA had a staff of 453 employees at the end of FY 2010. In FY 2011, the agency plans to add 103 employees, in addition to staff in the Office of Inspector General following the appointment in September 2010, of the agency's first Inspector General. FHFA's Director sets the direction for the agency to achieve its mission. FHFA divisions and offices have specific responsibilities and work together to ensure effective execution of the agency's mission.

The **Division of Federal Home Loan Bank Regulation** is responsible for the supervision and examination of the FHLBanks and the Office of Finance. The division conducts annual on-site examinations, periodic visitations, and off-site monitoring. Other division responsibilities include supervisory policy and program development, regulatory analysis and developments, and economic research and analysis in support of FHLBank regulation.

The **Division of Enterprise Regulation** is responsible for the supervision and examination of Fannie Mae and Freddie Mac. The division conducts on-site continuous supervision, targeted examinations, and off-site monitoring. The division provides oversight and ensures coordination among all FHFA mission-critical supervisory functions, including programs for capital adequacy, compliance, examination, financial analysis, and quality assurance in support of the Enterprises.

The **Division of Housing Mission and Goals** is composed of the following three offices, each with responsibilities that span all of the regulated entities:

- The **Office of Housing and Community Investment** is responsible for regulatory policy relating to community investment, affordable

FHFA staff assembled for Town Hall Meeting at the National Press Club, April 19, 2010 housing, certain new business activities, and housing goals of the Enterprises and FHLBanks.

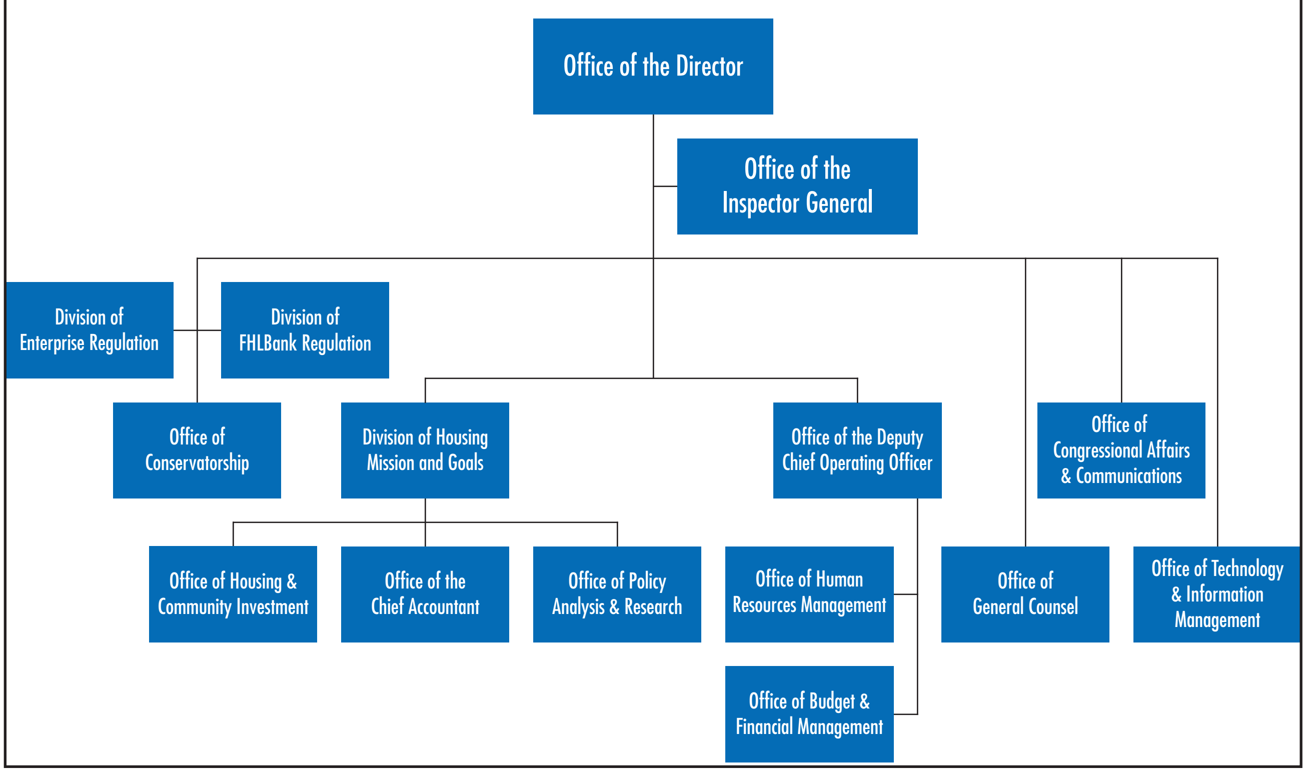
- The **Office of the Chief Accountant** develops safety and soundness guidance and policies related to accounting, auditing, and financial reporting and disclosure at the regulated entities. The office monitors the compliance of the regulated entities with such policies and also promotes the application of consistent accounting policies across the regulated entities.
- The **Office of Policy Analysis and Research** conducts research and policy analysis to assess the short- and long-term effect of trends and issues in the activities of the regulated entities, housing finance, and financial regulation on the regulatory and supervisory functions of FHFA. The office also prepares data series and publications that inform the public about the housing finance system, changes in housing prices, and helps support development of FHFA regulatory policies.

The **Office of Conservatorship Operations** assists the FHFA Director, as conservator, in preserving and conserving Fannie Mae and Freddie Mac's assets and property. The office ensures the Enterprises appropriately focus on their mission, including the stability, liquidity, and affordability of the housing market.

The **Office of the General Counsel** advises and supports the Director and all FHFA staff on legal matters related to the functions, activities, and operations of FHFA and the regulated entities, specifically providing support for supervision functions, promulgation of regulations, and enforcement actions. The Office also manages the Freedom of Information and Privacy Act programs. In addition, the agency ethics official provides advice, counseling and training to FHFA employees concerning ethical standards and conflicts of interest, and manages the agency's financial disclosure program.

The **Office of Inspector General** (**OIG**) conducts independent and objective audits, evaluations, and investigations to assist FHFA in meeting its mission;

Figure 1. Organization Chart for FHFA



keeps the FHFA Director, Congress, and the American public up to date and fully informed of problems and deficiencies relating to FHFA programs and operations; and works collaboratively with FHFA staff and program participants to ensure success of the agency's program goals. This office came into being upon the confirmation of Steve A. Linick by the U.S. Senate on September 29, 2010.

The **Office of Internal Audit** through FY 2010, until the appointment of the FHFA Inspector General, reported directly to the FHFA Director and carried out a variety of audit functions for FHFA as delegated by the Director.

The **Office of Congressional Affairs and Communications** is responsible for the public affairs and congressional relations functions at FHFA and is the primary point of contact for the external and internal communications of the agency. OCAC prepares and disseminates pertinent public information and responds to inquiries from Congress, the media, industry, and the public at large.

The **Office of the Deputy Chief Operating Officer** provides operational support and services to the agency in the areas of human resources, budget and financial management, performance management, emergency preparedness, and facilities.

The **Office of Technology and Information Management** is responsible for ensuring the integrity, confidentiality, and availability of FHFA's information systems and assets. The office maintains the agency's information technology (IT) infrastructure; oversees the IT security program; develops and maintains custom applications and data repositories; manages technology resources, investments, and assets; establishes IT strategic plans, policies and procedures; supports business partners; and manages the agency's records and information management program.

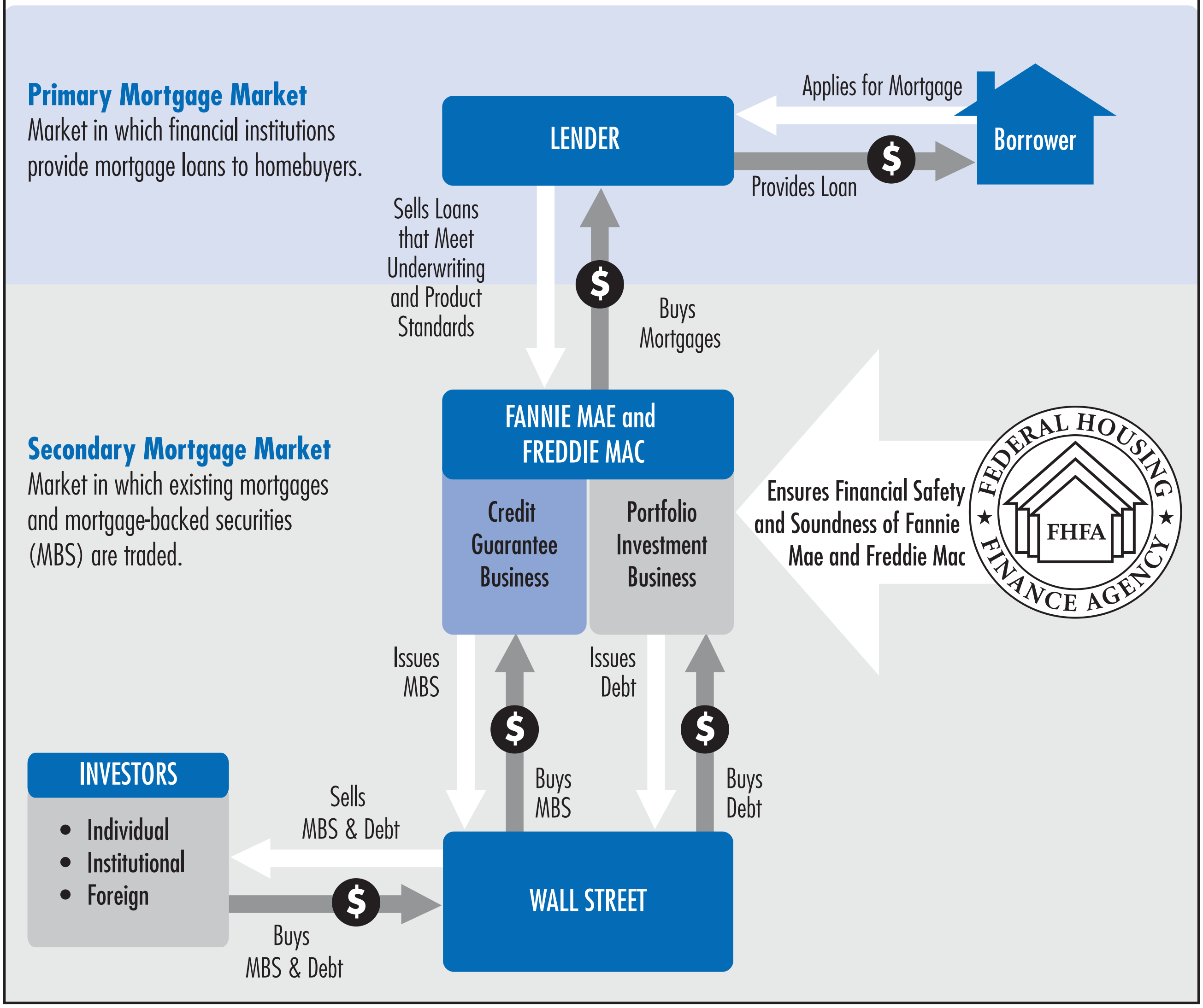
The Enterprises

In the primary mortgage market, financial institutions make mortgage loans directly to homebuyers. This process begins when a potential homeowner or borrower applies for a mortgage loan from a lender. For example, the lender may be a savings bank, credit union, mortgage banking company, commercial bank, savings and loan, or state or local housing finance agency. Once the loan is originated, the lender either holds the loan in its own portfolio or sells the loan. The secondary mortgage market is the market in which mortgages or mortgage-backed securities are traded. The Enterprises acquire mortgages and issue mortgage-backed securities in the secondary mortgage market (See Figure 2).

Congress established the Enterprises to provide liquidity, stability, and affordability to the secondary mortgage market. In the secondary mortgage market, the Enterprises make funds readily accessible to banks, savings and loans, and mortgage companies that make loans in the primary mortgage market to finance housing. Fannie Mae and Freddie Mac are the largest buyers of mortgages in the secondary market. They hold the mortgages they purchase in their portfolios or package the loans into mortgage-backed securities (MBS). The Enterprises also have the authority to buy other agency and private-label MBS for their own portfolios. Lenders may use the cash raised by selling mortgages to the Enterprises to lend to other homebuyers and real estate investors. Roughly half of the mortgages purchased by Fannie Mae and Freddie Mac finance dwelling units that are affordable to households with income at or below 80 percent of the area median income. More than one-fourth of the mortgages are located in geographic areas designated as underserved.

MBS are traded in the secondary mortgage market. Because Fannie Mae and Freddie Mac package mortgages as MBS and guarantee timely payment of principal and interest on the underlying mortgages, investors who might not otherwise invest in mortgages enter the secondary mortgage market, which expands the pool of funds available for housing. Such capital makes the secondary mortgage market more liquid and helps lower the interest rates paid by homeowners and other mortgage borrowers.

Figure 2. FHFA's Oversight Role – Fannie Mae and Freddie Mac



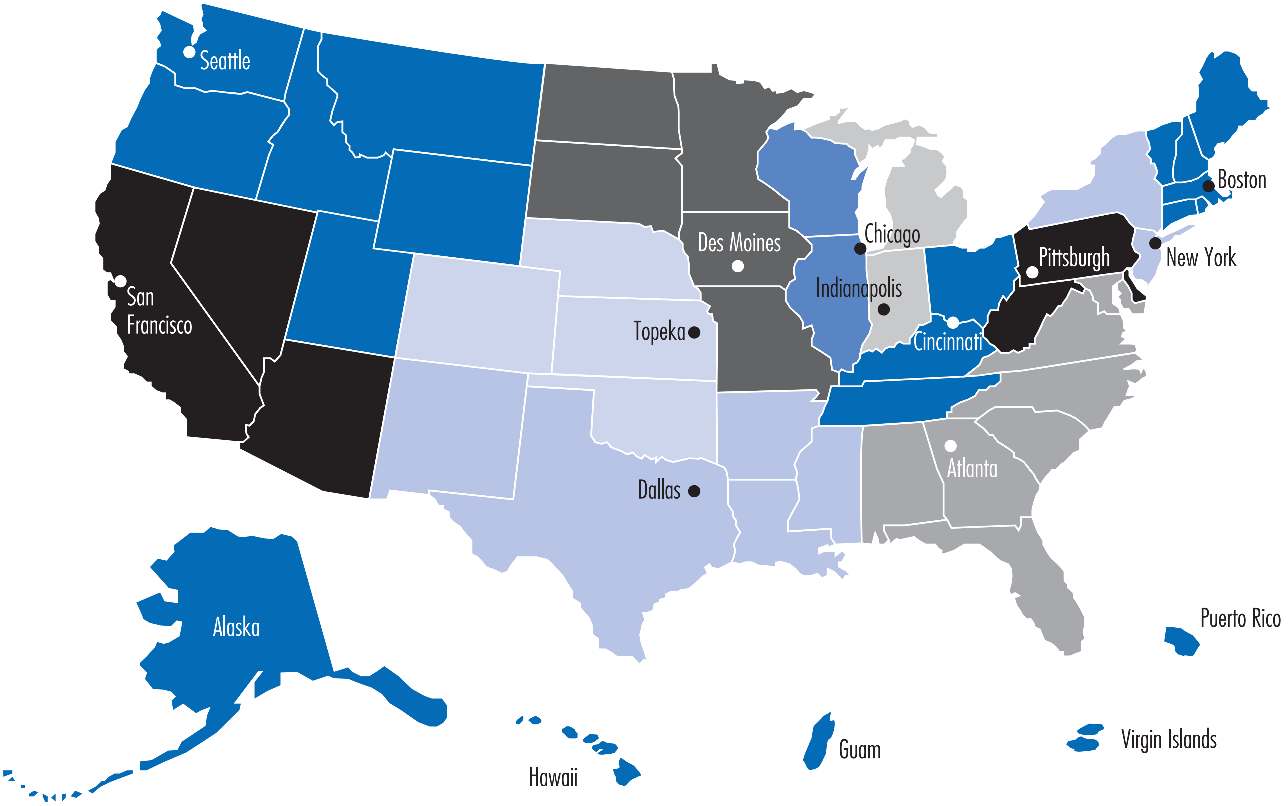
The Federal Home Loan Banks

The FHLBanks provide a readily available, low-cost source of funds to support housing finance and member liquidity. The FHLBanks are member-owned cooperatives. Only members own the capital stock in each FHLBank, and only members can borrow from an FHLBank. Membership is limited to regulated depository institutions (banks, thrifts, and credit unions), insurance companies, and community development financial institutions (CDFIs) engaged in residential housing finance (See Figure 3). The regions comprise combinations of whole states.

Each FHLBank conducts the majority of its credit and mortgage program businesses exclusively with its members or eligible housing associates.

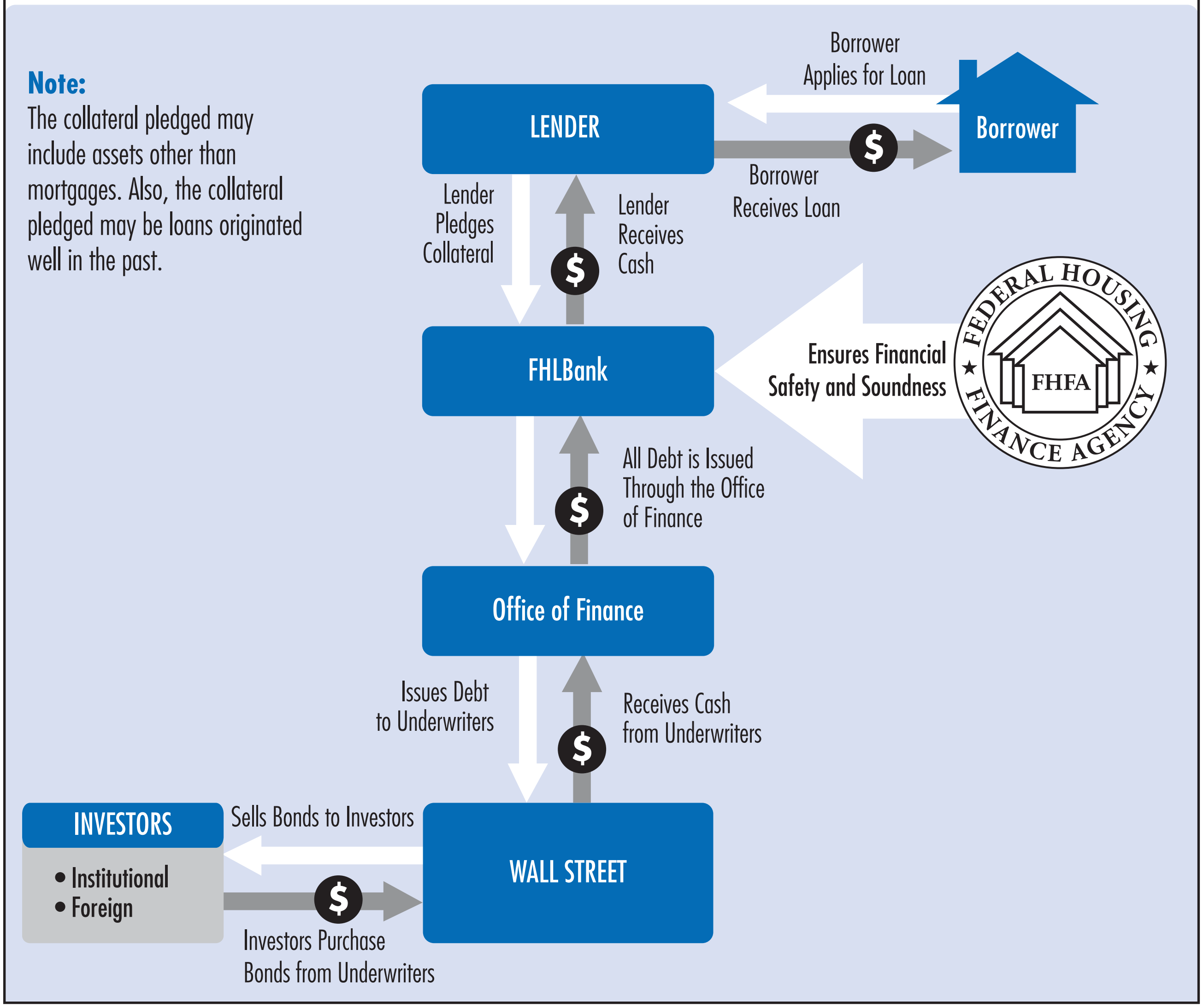
The FHLBanks offer credit and credit-related products, including loans (advances), letters of credit, and lines of credit to their members and eligible housing associates. All advances must be fully collateralized by mortgages and other eligible collateral pledged by the borrowing member or housing associates. Advances are the largest category of FHLBank assets. By providing

Figure 3. Federal Home Loan Bank Districts



Atlanta	Alabama, District of Columbia, Florida, Georgia, Maryland, North Carolina, South Carolina, Virginia
Boston	Connecticut, Maine, Massachusetts, New Hampshire, Rhode Island, Vermont
Chicago	Illinois, Wisconsin
Cincinnati	Kentucky, Ohio, Tennessee
Dallas	Arkansas, Louisiana, Mississippi, New Mexico, Texas
Des Moines	Iowa, Minnesota, Missouri, North Dakota, South Dakota
Indianapolis	Indiana, Michigan
New York	New Jersey, New York, Puerto Rico, Virgin Islands
Pittsburgh	Delaware, Pennsylvania, West Virginia
San Francisco	Arizona, California, Nevada
Seattle	Alaska, Guam, Hawaii, Idaho, Montana, Oregon, Utah, Washington, Wyoming
Topeka	Colorado, Kansas, Nebraska, Oklahoma

Figure 4. FHFA's Oversight Role – FHLBanks



advances and other credit-related products to their members, FHLBanks increase the availability of credit for residential mortgages.

In addition, some FHLBanks have an Acquired Member Assets (AMA) program to purchase mortgages from their members. Under these programs, members may sell qualifying mortgages to, or fund them through, an FHLBank. Members also may borrow from an FHLBank to fund low-income housing, helping members satisfy their regulatory requirements under the Community Reinvestment Act.
Finally, some FHLBanks offer their members a variety of services, such as correspondent banking, which includes security safekeeping, wire transfers and settlements, cash management, letters of credit, and derivative intermediation.

The FHLBanks fund their operations principally through the sale of debt instruments known as consolidated obligations, which are joint and severable obligations of the 12 FHLBanks. These debt instruments are sold to the public through the Office of Finance. Consolidated obligations are not obligations of the United States, and the U.S. Government does not guarantee them (Figure 4).

Performance Highlights

Changes in the Housing and Mortgage Markets During FY 2010

Housing prices declined at a slower rate in 2010 than in 2009. For the 12 months ending in August 2010, housing prices fell 2.4 percent, based on FHFA's monthly House Price Index. At the end of August 2010, the index was 13.6 percent below its peak, which occurred in April 2007.

Mortgage rates generally declined during FY 2010. In September 2010, the average interest rate on conventional 30-year, fixed rate mortgage loans of $417,000 or less was 4.58 percent, compared to 5.23 percent in September 2009. Recovery in the housing and mortgage markets has generally been slowed by several economic factors, including unemployment, but there are signs of progress.

Stephen Cross, Acting Chief Operating Officer, addresses FHFA staff at an FHFA Town Hall meeting on April 19, 2010.

In July 2010, Congress passed and President Obama signed the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act or the Act), designed to correct problems that led to the financial crisis. Among other things, the Dodd-Frank Act, provides that taxpayers will not be called upon to bail out failing financial companies or cover the cost of their liquidation. The Act also strengthens regulatory oversight and enhances regulators' authority to pursue financial fraud. The Act does not address the future of the Enterprises, the secondary mortgage market or of the housing finance system.

During FY 2010, FHFA carried out its mission against this backdrop of financial regulatory reform and changing conditions in the housing market. The agency accomplished a number of important goals as both conservator of the Enterprises and safety and soundness regulator of the 14 housing GSEs.

Preserving and Conserving the Assets of the Enterprises

Since September 2008, when both Enterprises were placed into conservatorship, FHFA has worked to preserve and conserve their assets. As conservator, FHFA assumed the powers of each Enterprise's management, board, and shareholders. FHFA provides approvals and guidance for the Enterprises as they conduct their business activities and day-to-day operations.

During FY 2010, FHFA prohibited the Enterprises from developing and offering new products to eliminate the operational challenges and risks inherent in such offerings. This restriction, standard for troubled financial institutions, directs focus of the Enterprises on existing core businesses while minimizing credit losses and remediating internal control weaknesses.

During FY 2010, FHFA also directed the Enterprises and the FHLBanks to undertake prudential actions to address significant safety and soundness concerns presented by energy retrofit lending programs denominated as Property Assessed Clean Energy (PACE). PACE loans foster lending for retrofits of residential or commercial properties through a county or city's tax assessment. In some states, such loans have a priority lien over existing mortgages, which could result in an alteration of lien priorities, thereby posing credit risk to lenders and secondary market entities. The actions required by FHFA were designed to mitigate risks posed by those PACE programs that altered lien priorities and failed to operate with sound underwriting guidelines and consumer protections.

In July 2010, exercising broad authority granted under HERA, FHFA issued 64 subpoenas to various entities seeking documents related to private-label MBS in which the Enterprises had invested. Information obtained from the subpoenas will aid FHFA in determining whether private-label MBS issuers and others are liable to the Enterprises for losses sustained on these securities, and enable the Enterprises to assess any claims arising from the failure of the loans or their servicing to meet required standards. Before FHFA issued the subpoenas, the Enterprises had been unsuccessful in their attempts to obtain such information.

FHLBank Corporate Governance

In April 2010, FHFA sent to the *Federal Register* a final rule that restructures the board of directors of the FHLBank System's Office of Finance and enhances the responsibility of the Office of Finance board of directors audit committee for the System's combined financial reports. The Office of Finance is responsible for issuing consolidated obligations on behalf of the 12 Federal Home Loan Banks, serves as their fiscal agent, and prepares disclosure materials associated with the marketing and sale of that debt, including the System's quarterly and annual combined financial reports.

Under the new rule, the Office of Finance board of directors expanded from three to 17 members. The new board of directors is composed of the president of each of the 12 Federal Home Loan Banks and five independent directors, each of whom must be a U.S. citizen with no material financial relationship to the System. The rule also provides that the five independent directors serve as the audit committee for the Office of Finance, and gives the audit committee increased authority over the form and content of the information that the FHLBanks provide to the Office of Finance for use in the System's combined financial reports.

The FHLBanks' Resolution Funding Corporation Obligations

Recent trends indicate that the FHLBanks will, within the next two fiscal years, fulfill their obligation to pay their portion of the interest on bonds issued by the Resolution Funding Corporation (REFCORP) as part of the savings and loan cleanup of 1989.

Currently, each FHLBank's REFCORP obligation is 20 percent of its net earnings. When the REFCORP obligation is satisfied, FHFA will expect the FHLBanks to allocate a commensurate sum each quarter to retained earnings. By increasing retained earnings, the FHLBanks will be in a better position to support par value repurchases and redemptions of member capital stock and will otherwise enhance their safety and soundness.

Responding to the Administration, Congress, and the Public

Addressing the financial crisis required a collaborative effort among the Administration, Congress, regulators, the public, and other industry stakeholders. FHFA responded promptly to inquiries, published reports and data pertaining to the secondary mortgage market, and met regularly with industry stakeholders. FHFA also gave a series of presentations regarding affordable housing and community investment activities for participants of the NeighborWorks Training Institutes.

In FY 2010, FHFA's Acting Director testified before Congressional committees on five occasions. Throughout 2010, FHFA responded promptly to numerous Congressional inquiries. FHFA received 253 Congressional inquiries and responded to 88 percent of them within 15 business days. FHFA participated in the President's Working Group on Financial Markets to help coordinate regulatory activities. FHFA also held meetings with representatives from U.S. Department of the Treasury (Treasury), HUD, the Council of Economic Advisers, the National Economic Council, and the Enterprises to discuss ways to improve the performance of the Enterprises and increase the stability of the secondary mortgage market.

FHFA provided information on the regulated entities and other housing-related topics through the FHFA website and several published papers and reports. In FY 2010, FHFA published two working papers: *Estimating Median House Prices* and *Automatic Recapitalization Alternatives*. FHFA also published five new research papers: *Revisions to FHFA's House Price Index in the Recent National House Price Boom and Bust*; *Housing and Mortgage Markets and the Housing Government-Sponsored Enterprises in 2008; Market Estimation Model for the 2010 and 2011 Enterprise Single-Family Housing Goals; Data on the Characteristics and Performance of Single-Family Mortgages Originated in 2001-2008 and Financed in the Secondary Market*; and *An Approach for Calculating Reliable State and National House Price Statistics*. A mortgage market note was titled *The Housing Goals of Fannie Mae and Freddie Mac in the Context of the Mortgage Market: 1996-2009*. In addition to this mortgage market note, FHFA published two mortgage market note updates. In August 2010, FHFA released its first *Conservator's Report on the Enterprises' Financial Condition*, which provided an overview of various aspects of the financial condition of the Enterprises during conservatorship. FHFA also published a monthly *Federal Property Managers Report*, described further in the next section.

Foreclosure Alternatives and Loss Mitigation

The Enterprises have long had programs to mitigate losses. These programs typically consisted of repayment plans and modest changes to loan terms, rather than any substantial modification to reduce the borrowers' monthly payments to an affordable level.

As the housing crisis persisted, it was clear that a more aggressive and broader approach to loss mitigation—one that included mortgages securitized in private-label securities, mortgages held as whole loans in bank portfolios, and mortgages owned or guaranteed by the Enterprises—was needed. This recognition led to the Enterprises' participation in the Administration's Making Home Affordable (MHA) program, including the Home Affordable Modification Program (HAMP) and the Home Affordable Refinance Program (HARP). MHA is a plan developed by the Administration to stabilize the housing market and help struggling homeowners get relief and avoid foreclosure. HAMP provides mortgage servicers a single, consistent program to modify mortgage payments for borrowers with delinquent mortgages or in imminent default to make them more affordable. FHFA oversees Fannie Mae and Freddie Mac's participation as financial agents for HAMP, as well as their efforts to carry out these and other loss mitigation strategies.

Fannie Mae and Freddie Mac have played key roles in the development and implementation of HAMP. A well-designed loan modification is often a lower cost resolution to a delinquent mortgage than foreclosure, and these alternatives to foreclosure lower Enterprise costs and save taxpayers money. Loan modification programs also can offer benefits beyond reducing losses directly on the Enterprises' resolutions of their delinquent mortgages, by improving stability in housing markets and reducing credit exposure.

During FY 2010, FHFA published a monthly *Foreclosure Prevention and Refinance Report* to publicize the progress of MHA, promote transparency in the Enterprises' foreclosure prevention activities, and provide data on the Enterprises' mortgage refinance and loan modification activities. In addition, FHFA published a monthly *Federal Property Managers Report*, which detailed the number and types of loan modifications and the number of foreclosures during the reporting period.

Housing Mission Compliance

On September 2, 2010, FHFA sent a final rule to the *Federal Register*, establishing new housing goals for the Enterprises for calendar years 2010 and 2011. The final rule establishes three, single-family, owner-occupied home purchase mortgage goals for low-income families, very low-income families, and families living in geographical areas with lower-income populations, areas with high concentrations of minority residents, and federally-declared disaster areas. The latter goal also includes a specialized subgoal to ensure that the Enterprises address housing needs in lower-income and minority areas. The final rule also contains a goal for single-family, owner-occupied refinance mortgages for low-income families.

While the Enterprises are in conservatorships, FHFA expects them to continue to fulfill their core statutory purposes, which includes their support for affordable housing. One set of measures of the Enterprises' support for affordable housing comes through the housing goals, which Congress revised significantly in HERA.

FHFA does not intend for the Enterprises to undertake imprudent or high-risk activities in support of the goals, nor does it intend conservatorship to be a justification for withdrawing support from these market segments. Under the conservatorships, the Enterprises have tightened their underwriting standards to avoid poor quality mortgages, such as those that contributed so much to their losses. Through FHFA oversight, the Enterprises will be expected to maintain this type of sound underwriting discipline going forward.

As before enactment of HERA, the FHLBanks will continue to support affordable housing for low- and moderate-income households principally through the Affordable Housing Program (AHP). Beginning in 2011, HERA also requires FHFA to establish affordable housing goals for the FHLBanks. The affordable housing goals for the FHLBanks must be consistent with those for the Enterprises and take into consideration the unique mission and ownership structure of the FHLBanks.

On May 27, 2010, FHFA published in the *Federal Register* a proposed rule to establish a framework for affordable housing goals for the FHLBanks. Under the proposed rule, an FHLBank would be subject to the proposed housing goals if its AMA-approved mortgage purchases in a given year exceed a volume threshold of $2.5 billion. FHFA received public comments on the establishment of three purchase money mortgage goals and one refinancing mortgage goal applicable to the FHLBanks' purchases of mortgages on owner-occupied single-family housing under their AMA programs.

Under the AMA programs, the FHLBanks purchase only single-family, fixed-rate mortgages below the conforming loan limit. While at one time, all FHLBanks offered AMA programs, several no longer offer the program, and mortgage loan balances are stable or declining at most of the FHLBanks. As of September 30, 2010, the combined value of the AMA mortgage loans in the FHLBanks' portfolios was $64 billion.

Executive Compensation

During FY 2010, FHFA established a new executive compensation program for the Enterprises as part of its oversight responsibilities as conservator. FHFA designed the new compensation structure in consultation with the Special Master for Troubled Asset Relief Program (TARP) Executive Compensation.

In addition, FHFA also lowered executive officer pay at the Enterprises by an average of 40 percent from pre-conservatorship levels. The significant salary structure changes implemented during FY 2010 include the following:

- No executive officers will receive perquisites exceeding $25,000 without FHFA approval in consultation with the U.S. Department of the Treasury.
- No retirement plans for executives may use more generous formulas than plans for lower-ranking employees.
- No expense reimbursements to executives will include "tax gross-ups," which are reimbursements to an employee for taxes owed on relocation expense payments.
- Deferred salary and incentive pay for all executive officers will be subject to "claw backs" by the Enterprises in the event of gross misconduct, gross negligence, conviction of a felony, or erroneous performance metrics. Claw backs allow FHFA to reclaim previously given monies or benefits, if it is later determined that management fell short through either adverse action or inaction.

The agency also issued the final rule, *FHLBank Board of Directors Eligibility, Elections, Compensation, and Expenses*. HERA repealed the statutory caps on the annual compensation an FHLBank may pay its directors. The final rule allows each FHLBank to pay its directors reasonable compensation and expenses, subject to the authority of the FHFA Director to prohibit compensation determined to be unreasonable. This is consistent with the authority the FHFA Director has used to reform compensation practices at Fannie Mae and Freddie Mac.

FHLBank Membership

On January 5, 2010, FHFA published a final rule that authorizes CDFIs, that have been certified by the CDFI Fund of the U.S. Department of the Treasury, to become members of the FHLBanks. Congress provided for such membership in the FHLBanks to enable CDFIs with increased access to long-term funding to increase their capacity to promote economic growth and stability in low- and moderate-income communities.

Figure 5. Regulations Published in FY 2010	
Proposed	**Minority and Women Inclusion** (75 FR 1289, January 11, 2010, 12 CFR Part 1207)
	Minimum Capital Temporary Increase (75 FR 6151, February 8, 2010, 12 CFR 1225)
	Use of Community Development Loans by Community Financial Institutions to Secure Advances, Secured Lending by Federal Home Loan Banks to Members and their Affiliates; Transfer of Advances and New Business Activity Regulations (75 FR 7990, February 23, 2010, 12 CFR 1266, 1272)
	Equal Access to Justice Act Implementation (75 FR 17622, April 7, 2010, 12 CFR 1203)
	Federal Home Loan Bank Investments (75 FR 23631, May 4, 2010, 12 CFR 1267)
	Federal Home Loan Bank Housing Goals (75 FR 29947, May 28, 2010, 12 CFR 1281)
	Enterprise Duty to Serve Underserved Markets (75 FR 32099, June 7, 2010, 12 CFR 1282)
	Conservatorship and Receivership (75 FR 39462, July 9, 2010, 12 CFR 1237)
	Office of Ombudsman (75 FR 47495, August 6, 2010, 12 CFR 1213)
	Rules on Practice and Procedure (75 FR 49313, August 12, 2010, 12 CFR Parts 1209)
	Private Transfer Fee Covenants (74 FR 49932, August 16, 2010)
	Information Sharing among Federal Home Loan Banks (75 FR 60347, September 30, 2010, 12 CFR Part 1260)
Final	**Post-Employment Restriction for Senior Examiners** (74 FR 51073, October 5, 2009, 12 CFR 1212)
	Federal Home Loan Bank Membership for Community Development Financial Institutions (75 FR 677, January 5, 2010, 12 CFR Parts 1263, 1290)
	Reporting of Fraudulent Financial Instruments (75 FR 4255, January 27, 2010, 12 CFR 1233)
	Federal Home Loan Bank Housing Associates, Core Mission Activities and Standby Letters of Credit (75 FR 8239, February 24, 2010, 12 CFR 1264, 1265, 1269)
	Federal Home Loan Bank Director's Eligibility, Elections, Compensation and Expenses (75 FR 17037, April 5, 2010, 12 CFR 1261)
	Board of Directors of Federal Home Loan Bank System Office of Finance (75 FR 23152, May 3, 2010, 12 CFR Parts 1273, 1274)
	Affordable Housing Program Amendments: Federal Home Loan Bank Mortgage Refinancing Authority (75 FR 29877, May 28, 2010, 12 CFR 1291)
	Supplemental Standards of Ethical Conduct for Employees of the Federal Housing Finance Agency (75 FR 52607, August 27, 2010, 5 CFR 9001)
	2010 - 2011 Enterprise Affordable Housing Goals; Enterprise Book-entry Procedures (75 FR 55892, September 14, 2010, 12 CFR Parts 1249, 1282)

An FHFA meeting wherein FHFA operating as conservator of Fannie Mae and Freddie Mac is carrying out the assumed powers of the Board and management of the two Enterprises.

The final rule sets forth eligibility and procedural requirements for CDFIs to become members of the FHLBanks. The eligible CDFIs include community development loan funds, certain venture capital funds, and state-chartered credit unions without federal insurance.

Providing Regulatory Guidance

In addition to the rulemaking described above, FHFA issued an array of other rules, some to implement new authorities provided in HERA and some to update or change regulations previously issued by one of FHFA's predecessor agencies. Figure 5 lists the proposed and final regulations issued by FHFA during FY 2010. Importantly, FHFA finalized a rule on post-employment restrictions for senior examiners, which restricts senior examiners from taking a job with a regulated entity for one year after leaving FHFA.

Management Challenges

FHFA as Conservator

Conservatorship cannot be a permanent state for the Enterprises. As debate continues over the future design of the housing finance system, FHFA remains focused on the fundamental purposes of the conservatorships: conserving the Enterprises' assets and maintaining their activities in the secondary mortgage market.

The statutory role of FHFA as conservator also requires the agency to take actions to preserve the assets of the Enterprises and restore them to a financially safe and sound condition. In the conservator role, FHFA has consistently emphasized that the Enterprises will continue to be responsible for normal business activities and day-to-day operations, seeking conservator approval and guidance as needed; in FY 2010, the companies focused on these principles. Pursuant to FHFA's mandate, the Enterprises, while they are in conservatorship, are not permitted to engage in new lines of business.

Managing and Reporting on the Conservatorship

During 2009, Treasury and the Federal Reserve provided unprecedented support to the mortgage markets via the Enterprises. Treasury established three support mechanisms: the GSE Credit Facility, the GSE Mortgage-Backed Securities (GSE MBS) Purchase Facility, and the Senior Preferred Stock Purchase Agreements. As required by law, the GSE Credit Facility and GSE MBS Purchase Facility terminated at the end of 2009. The GSE Credit Facility was never used. However, Treasury used the GSE MBS Purchase Facility to buy $221 billion of Fannie Mae and Freddie Mac MBS from September 2008 through December 2009. In addition, the Federal Reserve completed its commitment to purchase $1.25 trillion of Enterprise and the Government National Mortgage Association (Ginnie Mae) MBS as of March 31, 2010.

Treasury reaffirmed its commitment to the stability and liquidity of the mortgage market through the Senior Preferred Stock Purchase Agreements with two modifications in 2009 to the original agreements. First, Treasury announced an increase in the financial commitment to each company from $100 billion to $200 billion in February 2009, a move that emphasized the importance of the agreements in maintaining market confidence in the Enterprises. Legal authority to commit additional funds was set to expire at year-end, so Treasury reaffirmed its commitment on December 24, 2009, by amending the agreements to provide funding for each Enterprise up to the greater of: (1) $200 billion; or (2) $200 billion plus the cumulative total of draws for each calendar quarter in 2010, 2011 and 2012, minus any amount by which the assets of the Enterprise exceed its liabilities on December 31, 2012. This funding is to ensure that each Enterprise maintains a non-negative net worth, thereby avoiding a statutory requirement that an Enterprise be put in receivership following an extended period of negative net worth.

The December 2009 amendment was designed to quell market uncertainty by assuring investors of the soundness of Enterprise securities. That December amendment allows the Enterprises to be able to serve as a stable source of funds for new home purchases and refinancing of existing mortgages. This amendment also assures capital market investors that Enterprise securities are sound investments.

Although the Enterprises' substantial market presence has been a key step to restoring market stability, neither company would be capable of serving the mortgage market today without the ongoing financial support provided by Treasury. Losses at the Enterprises have totaled $226 billion since year-end 2007. At the end of FY 2010, Fannie Mae had drawn $85.1 billion and Freddie Mac $63.1 billion in Treasury support from the Senior Preferred Stock Purchase Agreements, nearly $148.2 billion in total. To provide the public with clear information about the Enterprises, FHFA began posting on its website in August 2010, quarterly data on the Enterprises' financial performance in conservatorship.

FHFA previously determined that capital classifications would be suspended during conservatorship. Both Enterprises have depleted all of their shareholders' equity, with the negative balances of those accounts offset by Treasury's investments under the Senior Preferred Stock Purchase Agreements. Consequently, levels of capital and capital adequacy, key measures of safety and soundness, cannot be measured for the Enterprises while operating under conservatorship with financial support from Treasury. Reliance on the U.S. Department of Treasury's backing will continue until legislation produces a final resolution of the Enterprises' future.

Each Enterprise continues to realize credit losses from mortgages originated in the years prior to conservatorship. Between 2004 and 2007, the Enterprises increased the amount of their exposure in nontraditional and high-risk mortgages, including Alt-A and interest only loans, which resulted in substantial losses. For example, during the first quarter of calendar year 2010, Alt-A loans accounted for 37 percent of Fannie Mae's losses for the quarter and 42 percent of Freddie Mac's. Figure 6 shows the characteristics of the Enterprises' single-family mortgage acquisitions since 2006.

Past business decisions cannot be undone; however, with the oversight and guidance of FHFA as conservator and regulator, the Enterprises are actively seeking ways to minimize these credit losses and ensure that new business generated during conservatorship is profitable. During the first quarter of 2010, less than 2 percent of Fannie Mae's purchases were interest only loans. Freddie Mac did not purchase any interest only loans. Alt-A loans were less than 1 percent of acquisitions for both Enterprises during the first quarter of 2010.

Operational challenges remain a critical concern at each Enterprise. In conservatorship, the Enterprises can continue their existing core business activities and take actions necessary to advance the goals of the conservatorship. They cannot commence new products or lines of business.

FHFA will work with the Administration and Congress on a complete review of, and legislative action on, the future of the housing finance system and of the Enterprises beyond conservatorship. Also, FHFA is looking at possible changes in the way the Enterprises do business that may be desirable in the interim period, as Congress contemplates and debates statutory options.

For example, this year FHFA directed the two Enterprises to work collectively to expand and enhance the data submitted by loan sellers. The goal of this initiative is to raise the quality and consistency of key mortgage and property information, which in turn should improve the Enterprises' risk management capabilities. The changes should also improve the functioning of the mortgage market and be beneficial regardless of what course the larger-scale restructuring of the housing finance system takes.

FHFA as Regulator

FHFA has the statutory responsibility of conducting an annual examination program for the Enterprises, the FHLBanks, and the Office of Finance. FHFA's annual examination program assesses the regulated entities' financial safety and soundness and overall risk management practices.

FHFA examiners use a risk-based approach to supervision. Through examinations, data analysis, and risk monitoring activities, FHFA identifies matters requiring corrective action by the regulated entities and monitors their efforts to correct deficiencies.

Setting Expectations for the FHLBank System

The FHLBanks face challenges. In FY 2010, the FHLBanks incurred aggregate credit-related impairment charges of more than $900 million on their holdings of private-label MBS. However, all but one of the 12 FHLBanks was adequately capitalized at the end of FY 2010, and the 12th FHLBank met regulatory minimum capital requirements but FHFA used its discretionary authority to deem it "undercapitalized" because of losses associated with its holdings of private-label MBS.

Four FHLBanks have negative accumulated other comprehensive income (AOCI) in excess of retained earnings. The negative AOCI principally reflects non-credit impairment in private-label MBS for which OTTI has been taken. The excess of negative AOCI over retained earnings is large at two FHLBanks, both with significant exposure to private-label MBS backed by non-traditional mortgages originated in 2005-08.

During FY 2010, the FHLBanks worked collectively to improve the rigor and consistency of their analytical framework for valuing their holding of private-label MBS. FHFA conducted two reviews of the "common platform" for FHLBank OTTI analyses and separately evaluated their OTTI modeling. FHFA offered recommendations for improvement, but concluded that the FHLBanks' methodology was generally sound.

A key objective of FHFA is to return the focus of FHLBank operations to providing advances to member institutions and to establish stability at each FHLBank to permit repurchases and redemptions of member stock at par. FHFA expects advances to represent an increasing share of total FHLBank assets over time. FHFA also expects Banks to achieve and maintain a market value of equity equal to or greater than the par value of their capital stock.

In recent years, FHLBank investment portfolios had grown beyond levels needed for liquidity and mission achievement at some FHLBanks. In some cases, interest rate exposures and credit risk rose significantly. Several FHLBanks experienced sharp declines in net asset values, which in turn led to restrictions on dividend payments, stock repurchases, and stock redemptions. Some of those restrictions have been voluntary, while others have stemmed directly from supervisory action. But, in either case, the restrictions disrupt the normal operations of the FHLBanks and affect the value proposition of membership.

Against this backdrop, FHFA expects all the FHLBanks to review, rethink and reformulate their business strategies with an increased emphasis on mission achievement and a focus on the traditional business of making advances to member institutions, while de-emphasizing investment portfolios not needed to support core activities.

Source of Losses

Enterprises

In its annual *Report of Examinations* for each Enterprise, FHFA rated both Fannie Mae and Freddie Mac as critical supervisory concerns, mainly due to credit-related expenses and forecasted credit losses yet to be recognized on purchases and guarantees of mortgages originated in 2006 and 2007. FHFA expects the high delinquency rates to continue for these vintage mortgages because of uncertainty about the overall economy, housing prices, and unemployment rates.

Both Enterprises also face a high degree of operational risk and limitations in their operational capacity. Constraints on operational capacity are also a concern for mortgage servicers, many of whom received incentives to keep costs low during the housing boom and subsequently have been strained by record mortgage defaults.

Both Enterprises have been working to develop alternative servicing solutions for high-risk mortgage portfolios because of rapidly rising inventories of real estate owned. Not only do large volumes of foreclosed houses present operational challenges, but these properties must be liquidated in a manner that does not needlessly exacerbate weaknesses in housing markets.

Each Enterprise funds more than $700 billion in mortgage-related assets through the issuance of debt securities. The interest rate risk of mortgage portfolios of this size is inherently large, but the challenges of managing this portfolio have become even larger because of the difficulty of estimating prepayments.

The need to carefully manage the interest rate risk of these portfolios is heightened by the fact that many of the new mortgages in the Enterprises' portfolios were originated at historically low rates. In an environment of rising interest rates, the average duration of these investments would significantly extend. If interest rate risk is not properly managed in the present, such a situation could lead to significant future funding challenges. Furthermore, the retained portfolio mix is changing with a much larger concentration of distressed assets that have cash flows that are difficult to model and may not be as sensitive to changes in rates. Finally, the asset mix within the retained portfolios is becoming less liquid.

Figure 6. Characteristics of the Enterprises' Single-Family Mortgage Acquisitions

Percent of New Single-Family Business *(Categories overlap and are not additive)*

	Fannie Mae				YTD	Freddie Mac				YTD
	2006	2007	2008	2009	June '10	2006	2007	2008	2009	June '10
Alt-A	22%	17%	3%	0%	0%	18%	22%	7%	0%	1%
Interest-only	15%	15%	6%	1%	2%	17%	21%	6%	0%	0%
Credit Score < 620	6%	6%	3%	0%	1%	5%	6%	3%	1%	1%
LTV > 90 Percent	10%	16%	10%	4%	8%	6%	11%	9%	4%	9%
Average LTV	73%	75%	72%	67%	69%	73%	74%	71%	67%	70%
Average Credit Score	716	716	738	761	758	720	718	734	756	750

Notes:

1. New business is defined as issuance of MBS plus purchases of whole loans and does not include purchases of mortgage-related securities.
2. For Fannie Mae, Alt-A generally refers to a mortgage loan that may be underwritten with reduced or alternative documentation than that required for a full documentation mortgage loan but may also include other alternative product features. In reporting Alt-A exposure, Fannie Mae classified mortgage loans as Alt-A if the lenders that delivered the mortgage loans to them classified the loans as Alt-A based on documentation or other product features. Fannie Mae classified private-label mortgage related securities held in its investment portfolio as Alt-A if the securities were labeled as such when issued.
3. In determining Alt-A exposure on loans underlying its single-family credit guarantee portfolio, Freddie Mac classified mortgage loans as Alt-A if the lender that delivered the mortgage loans classified the loans as Alt-A, or if the loans had reduced documentation requirements, as well as a combination of certain credit characteristics and expected performance characteristics at acquisition which, when compared to full documentation loans in Freddie Mac's portfolio, indicate that the loan should be classified as Alt-A. Freddie Mac's year-to-date figures include Alt-A purchases of $1.5 billion due to a long-term standby commitment termination and a subsequent participation certificate issuance. There was no change to the Alt-A exposure on these mortgages as a result of these transactions.
4. The years in the heading of this table are calendar years.

Sources:
Enterprises' Forms 10-K, credit supplements to SEC disclosures, and management reports.

Federal Home Loan Banks

Risk management deficiencies are present at some individual FHLBanks. Also, FHLBanks with substantial investments in private-label MBS have seen a decline in their market value of equity compared to the par value of capital stock, which has resulted in a reduction or suspension of dividends and limits on their ability to repurchase or redeem stock.

By the end of FY 2010, FHLBank advances had declined to the lowest level for the System since the third quarter of 2004. Advances accounted for less than 60 percent of total assets for the first time since the first quarter of 1998. The decline in advances reflects continuing deposit growth and members' tepid loan demand, which reduces their need for wholesale funding. In addition, ongoing consolidation in the financial services industry has resulted in some large borrowers being acquired by firms with a lower historical use of advances.

The FHLBanks' AHP continues to be a source of funding for national and local affordable housing initiatives supported by member institutions. However, the decline in FHLBank income has reduced program contributions from $331 million in 2007 to $258 million in 2009.

Participating in Regulatory Reform

The Dodd-Frank Act requires new rules for mortgages and mortgage securitizations. Among other things, the Act requires FHFA to work with other federal regulators and agencies to define low-risk, "qualified residential mortgage." Such mortgages will be exempt from certain risk-retention requirements related to their securitization.

In addition, the Act establishes the Consumer Financial Protection Bureau, which will be responsible for regulations governing certain disclosures and mortgage lending practices. FHFA expects to work with the Bureau on mortgage-related consumer protection matters.

Future of the Housing Finance System

Numerous ideas about the future of the housing finance system have been proposed in the past two years. Large-scale restructuring of the housing finance system that would provide an explicit federal guarantee of any kind, assign the functions of the Enterprises to a federal agency or corporation, or establish more than two federally chartered secondary market firms would require new legislation.

The Administration, Congressional Budget Office, U.S. Government Accountability Office (GAO), trade associations, academics, and others have identified a variety of approaches related to the future structure and functions of the Enterprises or their successors. FHFA is participating in internal and multiagency efforts to review and evaluate the strengths, weaknesses, and risks of the various options. FHFA's experience with, and understanding of, secondary mortgage markets and institutions will be valuable to the Administration and Congress as they consider restructuring housing finance and financial regulation and address the secondary mortgage market and the role of the Enterprises.

Though much of the debate will focus on the Enterprises or their successors in the secondary mortgage market, FHFA expects the discussion to include the future of the FHLBanks. The FHLBanks have played a critical role in providing financing to large and small member financial institutions through advances, but their residential mortgage portfolios are small compared to those of the Enterprises. To prepare for future policy decisions, FHFA is closely monitoring markets and holding discussions with various stakeholders.

Challenges for the Housing GSEs and FHFA as the Policy Debate Commences

The upcoming national debate on the future of the country's housing finance system will pose unique challenges for the housing GSEs and FHFA. As the debate progresses, the Enterprises will be expected to continue providing an active, stable secondary mortgage market so that mortgage lending may continue uninterrupted and unimpeded by policy debates. Yet the management and staff at each Enterprise will be sensitive to the terms and course of the debate, as it will include discussions of whether and how the Enterprises may exist in the future. The ongoing policy debate poses challenges for Enterprise management as well as for FHFA in ensuring the continued staffing and efficient operations at each Enterprise.

As the FHLBanks are an important part of the country's housing finance system, the policy debate may soon include consideration of possible new or changing roles and responsibilities for the FHLBanks. As with the Enterprises, the FHLBanks will be challenged with maintaining ongoing operations as policy discussions about the FHLBank System take place.

For FHFA, the broad Administration and congressional review of the country's housing finance system also poses challenges and opportunities. Since its creation two years ago, FHFA has worked to realize HERA's purpose in having a single housing finance regulator capable of a broad view of wholesale mortgage financing and of the liquidity of the nation's mortgage market. Internally, FHFA continues to make strides in how it organizes and manages its responsibilities so as to realize the benefits of being a single, unified housing GSE regulator. In FY 2011, FHFA will continue to develop its internal management structure to more fully realize the benefits of combining its three predecessor agencies. It will also be active in supporting the policy debate on the future of housing finance, while remaining focused on the difficult challenges facing the country's housing finance system and its institutions today.

FY 2010 Performance Summary

FHFA's Strategic Planning

FHFA sets long-term and annual goals and monitors progress throughout the year to produce results using strategic and performance planning. The second section of this report describes FHFA's results and their relation to the agency's FY 2010 performance goals.

FHFA's *FY 2010 Annual Performance Plan* was developed and released in January 2010, and includes a total of 26 performance measures: 20 annual performance goals in support of three strategic goals and objectives; and six annual performance goals in support of FHFA's resource management strategy. This section describes the agency's performance against its *FY 2010 Annual Performance Plan*, which outlined the means and strategies to achieve the annual performance goals and related measures for the past year.

FHFA plans to refine and update the agency's strategic plan in time for the FY 2012 budget development, in response to OMB's directive. Consistent with OMB guidance and sound strategic planning practices, FHFA will update its FY 2011 targets and set FY 2012 performance targets in advance of preparing its FY 2012 budget.

In FY 2010, FHFA began tracking resource allocations and program costs by strategic goals that are outlined in the agency's strategic plan.

FHFA's Strategic Goals

To achieve FHFA's mission, the agency established three strategic goals:

1. The housing GSEs operate in a safe and sound manner and comply with legal requirements.
2. The housing GSEs support a stable, liquid, and efficient mortgage market, including sustainable homeownership and affordable housing.
3. FHFA preserves and conserves the assets and property of the Enterprises, ensures focus on their housing mission, and facilitates their financial stability and emergence from conservatorship.

FHFA also has set a resource management strategy which states that FHFA has the personnel, resources, and infrastructure to effectively and efficiently achieve its mission and goals.

FHFA FY 2010 Performance

The performance section describes the agency's performance goals for each strategic goal and FHFA's accomplishments related to each performance goal and its associated performance measures. Performance goals are counted as *met* when targets for all performance measures have been achieved. FHFA reported on 26 performance measures in its *FY 2010 Annual Performance Plan*. The agency met or exceeded 12 of the performance measures in the plan. It failed to meet 14 of the performance measures.

The agency is not satisfied with that performance record. However, in a number of cases in which a goal was not fully satisfied, the agency did achieve a substantial degree of progress toward the goal. For example, one measure relating to the safety and soundness would require an improvement in at least one component examination rating for each of the two Enterprises. The objective was satisfied in one Enterprise, but not the other. In the other, progress was made in a number of component areas, but not enough progress to warrant a higher component rating. As such, the performance measure was not achieved, but the agency and the Enterprises made clear progress toward the measure's satisfaction.

Another example relates to the FHLBanks achieving a composite examination rating of "2" or better or operating under an approved remediation plan. Of the three FHLBanks that were not operating under an approved remediation plan within 90 days of the downgrade, one subsequently adopted a plan acceptable to FHFA during FY 2010. The other two FHLBanks adopted plans acceptable to FHFA during the first quarter of FY 2011.

In another case, a new examination documentation and retrieval tool was tested during the fiscal year, but the tool's specifications were not yet final. Certain key decisions had been made, but a final decision will be made in FY 2011, rather than in FY 2010. Similarly, the agency's housing goals and duty to serve rules for the Enterprises were delayed, but ultimately published for comment during the fiscal year. The associated performance measures were not met because the rulemakings did not meet their target dates.

Therefore, in preparing the agency's *FY 2011 Annual Performance Plan*, FHFA will look to refine its performance measures in light of progress made to date. Also, the FY 2011 performance measures will more clearly tie to measurable progress in the supervision of the Enterprises and the FHLBanks and enhancements to internal controls at FHFA.

Further, FHFA identified six of the 26 performance measures for FY 2010 as key performance indicators critical to its achievement of its strategic goals and objectives. Those key performance indicators represent each of the agency's three strategic goals and its resource management strategy, and represent the

Figure 7. Key FHFA Performance Indicators for FY 2010

Strategic Goal	Performance Goal	Key Performance Indicator
STRATEGIC GOAL 1 **The housing GSEs operate in a safe and sound manner and comply with legal requirements.**	**PERFORMANCE GOAL 1.1** **Fannie Mae and Freddie Mac (the Enterprises) comply with legal requirements and operate in a safe and sound manner with adequate capital and access to funds and capital.**	**PERFORMANCE MEASURE 1.1.1** Each Enterprise improves in one or more component ratings TARGET: September 30, 2010 **Not Met** Freddie Mac's market risk rating improved from critical concerns to significant concerns at the end of the second quarter. Fannie Mae did not improve in any component ratings during the fiscal year. Although most of Fannie Mae and Freddie Mac's component ratings did not improve, improvements were made in several areas, increasing the likelihood that some component ratings will improve in the next fiscal year.
	PERFORMANCE GOAL 1.2 **The FHLBanks and the Office of Finance comply with legal requirements and operate in a safe and sound manner with adequate capital and access to funds and capital.**	**PERFORMANCE MEASURE 1.2.1** Each FHLBank is rated 2 or better or operates under a performance improvement plan acceptable to FHFA within 90 calendar days of a downgrade below a rating of 2. TARGET: Quarterly, beginning June 30, 2010 **Not Met** In FY 2010, 7 FHLBanks were assigned a rating below "2", and 3 of those were not operating under an acceptable performance improvement plan within 90 days.

Strategic Goal	Performance Goal	Key Performance Indicator
STRATEGIC GOAL 2 **The housing GSEs support a stable, liquid, and efficient mortgage market including sustainable homeownership and affordable housing.**	**PERFORMANCE GOAL 2.1** **FHFA ensures the housing GSEs support a stable, liquid, and efficient mortgage market.**	**PERFORMANCE MEASURE 2.1.2** Absent a revival of the private market in FY 2010, each Enterprise's share of single-family mortgage purchases and originations does not decline by more than 10 percent of the share obtained in FY 2009. TARGET: Annually **Met** For Fannie Mae, the share of single-family mortgage purchases and originations decreased from 40.04 percent in FY 2009 to 36.26 percent in FY 2010. For Freddie Mac, the share of single-family mortgage purchases and originations decreased from 25.61 percent in FY 2009 to 23.75 percent in FY 2010.
	PERFORMANCE GOAL 2.2 **FHFA ensures the housing GSEs provide leadership in housing finance and affordable housing by operating these programs in an effective and efficient manner, developing products, establishing partnerships, and financing homes for very low-, low-, and moderate-income households.**	**PERFORMANCE MEASURE 2.2.1** The FHLBanks' Affordable Housing Program (AHP) funds are awarded in compliance with laws and regulations. TARGET: Annually **Met** FHFA conducted AHP examinations at all 12 FHLBanks. No substantive issues were found regarding compliance with laws and regulations.
STRATEGIC GOAL 3 **FHFA preserves and conserves the assets and property of the Enterprises, ensures focus on their housing mission, and facilitates their financial stability and emergence from conservatorship.**	**PERFORMANCE GOAL 3.2** **Delegate appropriate authorities to each Enterprise's management to continue with or improve upon the Enterprises' mission and their business operations.**	**PERFORMANCE MEASURE 3.2.1** FHFA provides approvals and guidance to the Enterprises on conservatorship-related issues within 30 business days. TARGET: 80 percent per quarter **Not Met** FHFA provided approvals and guidance to the Enterprises on conservatorship-related issues within 30 business days for 54 percent of the time in the fourth quarter, reflecting both improved ability to track performance and improved performance over prior period results. Early data problems with this measure are described later in this report.
RESOURCE MANAGEMENT STRATEGY **FHFA has the personnel, resources, and infrastructure to manage effectively and efficiently to achieve its mission and goals.**	**PERFORMANCE GOAL 4.4** **FHFA has the information technology and physical infra-structure needed to achieve its mission and goals.**	**PERFORMANCE MEASURE 4.4.2** FHFA completes its internal review of Examiner Workstation and finalizes a new strategic plan for Examiner Workstation. TARGET: September 30, 2010 **Not Met** Although the target deadline was missed, substantial development of the Proof of Concept was achieved. Feedback from ongoing testing was positive and will result in a more robust strategic plan.

highest priority measures for the agency. See Figure 7 above for a summary of FHFA's achievement of those six key performance indicators.

The data for FHFA's performance measures are complete and reliable. Data for FHFA's performance measures are created internally, reported in the agency's performance tracking system, and reviewed by senior management quarterly. Data related to supervision activities are collected through FHFA's supervision process and reviewed by FHFA quality assurance staff and agency management.

Program Evaluation

Because FHFA's Inspector General was not confirmed until the end of FY 2010, no program evaluations were conducted at FHFA during the fiscal year.

FHFA received, for the second consecutive year, the Certificate of Excellence in Accountability Reporting award for its FY 2009 Performance and Accountability Report from the Association of Government Accountants.

FY 2010 Financial Summary

For FY 2009 and FY 2010, its first and second year as a new agency, FHFA achieved an unqualified (clean) opinion from the GAO on its annual financial statements. GAO noted no material weaknesses or significant deficiencies in FHFA's internal controls and cited no instances of noncompliance with laws and regulations. In accordance with the Office of Management and Budget's (OMB) Circular No. A-123, *Management's Responsibility for Internal Control*, FHFA continued to assess the effectiveness of its internal controls annually. FHFA received, for the second consecutive year, the Certificate of Excellence in Accountability Reporting (CEAR) award for its *FY 2009 Performance and Accountability Report* (PAR) from the Association of Government Accountants (AGA). The CEAR is awarded to agencies that have demonstrated excellence in integrating performance and accountability reporting. FHFA also received a CEAR Best-In-Class award for providing the most comprehensive and candid presentation of forward-looking information in its FY 2009 PAR.

Source of Funds

HERA authorizes FHFA to collect annual assessments from its regulated entities to pay its costs and expenses and maintain a working capital fund. Under HERA, annual assessments are levied against the Enterprises and the FHLBanks to cover the cost and expenses of the agency's operations for supervision of the regulated entities.

FHFA calculates the assessments for each Enterprise by determining the proportion of each Enterprise's assets and off-balance sheet obligations to the total for both Enterprises and then applying each of the Enterprise's proportion (expressed as a percentage) to the total budgeted costs for regulating the Enterprises. FHFA calculates the assessments for each of the 12 FHLBanks by determining each FHLBank's share of minimum required regulatory capital as a percentage of the total minimum capital of all the FHLBanks and applying this percentage to the total budgeted costs for regulating the banks. Assessments are paid semiannually on October 1 and April 1. FHFA collected assessments of $143 million during FY 2010, which included a $10.4 million special assessment on the Enterprises related to conservatorship activities.

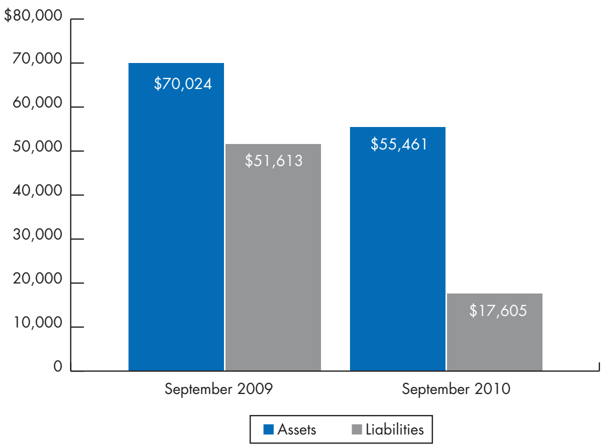
Analysis of Financial Statements

The principal financial statements present FHFA's financial position, net cost of operations, changes in net position, and budgetary resources for fiscal years 2010 and 2009. Financial statements and notes for fiscal years 2010 and 2009 appear on pages 70-86. Highlights of the financial information presented in the principal financial statements are shown below.

Balance Sheet

The Balance Sheet presents, as of the end of the fiscal year, the recorded value of assets and liabilities retained or managed by FHFA. The difference between the assets and liabilities represents FHFA's net position. The Balance Sheet reflects total assets of $55.5 million, a 21-percent decrease over FY 2009. The decrease is primarily due to FY 2010 assessment payments received during FY 2009 and increased cash outlays during FY 2010. FHFA's total liabilities decreased by $34 million, a 66-percent decrease over FY 2009. The decrease is primarily due to the decrease in deferred revenue. FHFA deferred revenue to reflect FY 2010 assessments that were received at the end of FY 2009. As a result, FHFA's net position as of September 30, 2010 was $37.9 million, a $19.5 million increase over the $18.4 million net position as of September 30, 2009.

Figure 8. Assets and Liabilities
(Dollars in Thousands)

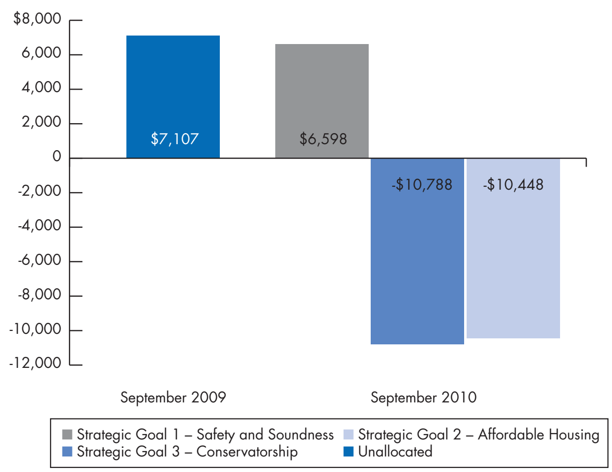


Statement of Net Cost

The Statement of Net Cost presents the components of FHFA's net cost, which is the gross cost incurred less any revenues earned. FHFA's total program net costs, as reflected on the Statement of Net Cost, were -$14.6 million (or net revenue) as compared to the $7.1 million net cost in FY 2009. This change reflects the increase in gross costs and earned revenue needed to carry out its mission as reflected in its FY 2010 operating budget. The operating budget increase between fiscal years is the result of increased mission costs and a special assessment levied on the Enterprises related to conservatorship activities. However, during the course of the year, FHFA was unable to fully expend its FY 2010 earned revenue, thereby resulting in an excess of revenue over cost. FHFA's costs for FY 2010 were less than expected and budgeted for, resulting in a surplus. FHFA issues a credit for unobligated funds as of September 30, 2010 against next year's assessment.

Consistent with the Government Performance and Results Act of 1993, the Statement of Net Cost is reported by FHFA's strategic goals. FHFA's program costs were reflected as one program for FY 2009, as defined by HERA Section 1311(b)(1). Beginning in FY 2010, FHFA tracked resource allocations and program costs to the strategic goals (responsibility segments) developed for FHFA's new strategic plan, which became effective for FY 2010. Strategic Goals, 1 – Safety and Soundness; 2 – Affordable Housing; and 3 – Conservatorship, guide program offices to carry out FHFA's vision and mission. FHFA has a Resource Management Strategy, which is distributed proportionately to Strategic Goals 1-3 based on the percentage of direct costs of each goal to the total direct costs for FHFA. Strategic Goal 1, Safety and Soundness, comprises the major portion of the total program costs.

Figure 9. Total Net Cost of Operations
(Dollars in Thousands)

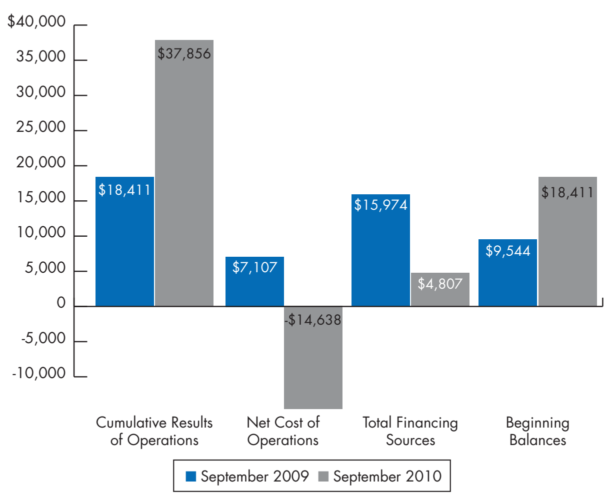


Statement of Changes in Net Position

The Statement of Changes in Net Position presents those accounting items that caused the net position section of the Balance Sheet to change from the beginning to the end of the reporting period. Financing sources increase net position. FHFA's financing source is imputed financing from costs absorbed on FHFA's behalf by other Federal agencies. Net cost of/income from operations impacts net position.

FHFA's cumulative results of operations for the period ending September 30, 2010 increased $19.5 million, due primarily to a combination of a decrease in net costs of $21.7 million and an increase in beginning balances of $8.9 million. Total financing sources decreased $11.2 million as a result of having no appropriation in FY 2010.

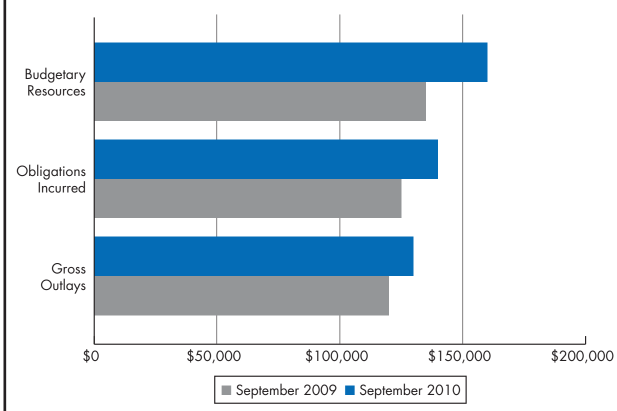
Figure 10. Statement of Changes in Net Position *(Dollars in Thousands)*



Statement of Budgetary Resources

This statement provides information about the provision of budgetary resources and their status as of the end of the reporting period. The statement shows that FHFA had $155.6 million in total budgetary resources for the 12 months ended September 30, 2010. These budgetary resources were composed of $143 million in assessments, $9.7 million in unobligated balance brought forward from FY 2009, and $2.7 million in recoveries of prior year unpaid obligations. Obligations incurred increased $16.6 million to $132.8 million in FY 2010. Gross outlays increased $5.5 million to $122.9 million in FY 2010.

Figure 11. Statement of Budgetary Resources Comparisons *(Dollars in Thousands)*



Limitations of the Financial Statements

FHFA management has prepared its fiscal years 2010 and 2009 financial statements from the books and records of the agency in accordance with the requirements of the Office of Management and Budget (OMB) Circular A-136, *Financial Reporting Requirements*, as amended. The financial statements represent the financial position and results of operations of the agency pursuant to the requirements of Chapter 31 of the U.S. Code section 3515 (b). While these statements have been prepared from the agency's books in accordance with the formats prescribed by the OMB, the statements are in addition to the financial reports used to monitor and control budgetary resources, which are prepared from the same books and records. These statements should be read with the understanding that they are for a component of the U.S. government, a sovereign entity.

Management Assurances

During FY 2010, FHFA adhered to the internal control requirements of the Federal Managers Financial Integrity Act of 1982 (FMFIA) and the guidance provided by OMB Circular A-123. FHFA's Executive Committee on Internal Controls met quarterly to oversee internal controls and provide recommendations to the Acting Director on the effectiveness of FHFA's internal controls.

In 2010, the executive committee members were the Senior Deputy Director/Chief Operating Officer who served as the Chairman, the Chief Administrative

Officer who served as the Vice-Chairman, the Chief Information Officer, the Chief Financial Officer, the Deputy Director for Enterprise Regulation, the Deputy Director for FHLBank Regulation, the General Counsel, and the Associate Director, Office of Supervision Infrastructure. The Chairman and Vice Chairman invited other FHFA executives when appropriate. The executive committee also established senior assessment teams to review specific areas when needed.

During FY 2010, pursuant to its obligations under OMB Circular A-123, FHFA monitored and assessed the following three areas:

- **Reliability over Financial Reporting**
  FHFA's Office of Budget and Financial Management assessed the agency's financial reporting controls according to the requirements outlined in OMB Circular A-123, Appendix A.
- **Compliance with Laws and Regulations**
  Assessment teams from FHFA divisions and offices identified the significant laws and regulations that relate to the operations for their respective offices. Assessment teams documented the actions that demonstrated compliance, and the agency's Office of General Counsel reviewed all submissions.
- **Effectiveness and Efficiency of Operations**
  Assessment teams from FHFA divisions and offices reviewed controls over operations using the criteria outlined in the GAO Internal Control Management and Evaluation Tool. Division and office managers and the Office of Budget and Financial Management reviewed the reports of the assessment teams.

The Executive Committee on Internal Controls reviewed documentation from all three areas. In compliance with the FMFIA requirements, the Acting Director, on the basis of a recommendation from the executive committee, provided reasonable assurance that internal controls over financial reporting as of September 30, 2010, were operating effectively and no material weaknesses were found in the design or operation of the internal controls over financial reporting. This assurance can be found in the "Management's Discussion and Analysis" of this report and meets the FMFIA reporting requirement for internal controls.

Federal Management System and Strategy

Section 1106(g)(3) of HERA requires FHFA to implement and maintain financial management systems that comply substantially with federal financial management systems requirements, applicable federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level. FHFA uses the Bureau of the Public Debt for its accounting services and that agency's financial management system (FMS) which includes (1) a core accounting system—Oracle Federal Financials; (2) three feeder systems—PRISM (procurement), GovTrip (travel), and Citidirect (charge card); (3) a reporting system—Discoverer; and (4) an inventory tracking system. FHFA is responsible for overseeing the Bureau of the Public Debt's performance of accounting services for the agency. A financial oversight document outlines the assignment of activities between FHFA and the Bureau of the Public Debt. FMS includes manual and automatic procedures and processes from the point at which a transaction is initiated to issuance of financial reports. FMS meets the requirements of HERA Section 1106(g)(3). FHFA also uses the National Finance Center, a service provider within the Department of Agriculture, for its payroll and personnel processing. FHFA has streamlined accounting processes by electronically interfacing data from charge cards, investment activities, the GovTrip travel system, the PRISM procurement system, and the National Finance Center payroll system to FMS.

Federal Information Security Management Act

Title III of the Electronic Government Act of 2002, titled the Federal Information Security Management Act (FISMA), requires all federal agencies to develop and implement an agency-wide information security program. The program provides the framework to protect the agency's information, operations, and assets. During FY 2010, OMB issued guidance requiring federal agencies to continuously monitor the security posture of information systems to enable timely decision making regarding identified vulnerabilities and threats. To accomplish this, agencies must automate security-related activities and acquire tools that correlate and analyze security-related information.

FHFA annually reviews the agency's information security program through its internal audit function and reports the results to OMB as required by FISMA. FHFA's information security program activities during FY 2010 reflect efforts in bringing the agency into compliance with the government-wide continuous monitoring requirement. Such compliance requires FHFA to proactively monitor the security posture of its information technology infrastructure through the implementation of automated security tools and supplemental resources for monitoring activities. The tools and activities include system log review and configuration management tools, and periodic vulnerability scans.

Other FY 2010 information security program activities included implementing an updated information security policy, comprehensive security procedures, and performing annual security control assessments. FHFA maintained security certification and accreditation on 100 percent of all major systems in production and provided security awareness training through an automated program to all FHFA employees and contractors. FHFA also addressed security-related weaknesses for systems noted in the prior year FISMA review.

The FY 2010 FISMA review concluded that FHFA had an effective information security program. The review disclosed weaknesses pertaining to monitoring of contractor systems, control and disposal of storage media for peripheral equipment such as copiers, noncompliance of the organizational structure of FHFA's information security program with FISMA, lack of completion of updates to the FHFA information security policy and related information security procedures, and vulnerabilities identified by network scans. All of the findings have been addressed and remediation efforts are underway. None of the weaknesses were classified as significant deficiencies.

Erroneous Payments

The Improper Payments Information Act of 2002 requires that agencies (1) review activities susceptible to significant erroneous payments; (2) estimate the amount of annual erroneous payments; (3) implement a plan to reduce erroneous payments; and (4) report the estimated amount of erroneous payments and the progress to reduce them. The Act defines significant erroneous payments as the greater of 2.5 percent of program activities or $10 million.

FHFA has implemented and maintains internal control procedures that ensure disbursement of federal funds for valid obligations. FHFA made no erroneous payments in FY 2010 that met the Act's thresholds.

Prompt Pay

The Prompt Payment Act requires federal agencies to make timely payments to vendors and improve the cash management practices of the government by encouraging the use of discounts when they are justified. This also means that FHFA must pay its bills within a narrow window of time. In FY 2010, the dollar amount subject to prompt payment was $28.7 million. The amount of interest penalty paid in FY 2010 was $126 or 0.00044 percent of the total dollars disbursed.

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Telephone: (202) 408-2500
Facsimile: (202) 408-1435
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October 15, 2010

Federal Managers' Financial Integrity Act
Statement of Assurance
Fiscal Year 2010

The Federal Housing Finance Agency (FHFA) management is responsible for establishing and maintaining effective internal control and financial management systems that meet the objectives of the Federal Managers' Financial Integrity Act (FMFIA).

FHFA conducted its assessment of the effectiveness of internal control over the effectiveness and efficiency of operations and compliance with applicable laws and regulations in accordance with OMB Circular A-123, Management's Responsibility for Internal Control. Based on the results of this evaluation, FHFA can provide reasonable assurance that its internal control over the effectiveness and efficiency of operations and compliance with applicable laws and regulations as of September 30, 2010 was operating effectively and that no material weaknesses were found in the design or operation of the internal controls.

In addition, FHFA conducted its assessment of the effectiveness of internal controls over financial reporting, which includes safeguarding of assets and compliance with applicable laws and regulations, in accordance with the requirements of Appendix A of OMB Circular A-123. Based on the results of this evaluation, FHFA can provide reasonable assurance that its internal controls over financial reporting as of September 30, 2010 were operating effectively and no material weaknesses were found in the design or operation of the internal controls over financial reporting.

In accordance with the requirements of FMFIA, FHFA's financial management systems are substantially in compliance with the requirements for federal financial management systems as presented in A-127, Financial Management Systems as of September 30, 2010.

Edward J. DeMarco

Edward J. DeMarco
Acting Director

10-10-10
Date

Performance Section

Managing and Measuring Performance

Strategic Goal 1 (Safety and Soundness)

Strategic Goal 2 (Affordable Housing)

Strategic Goal 3 (Conservatorship)

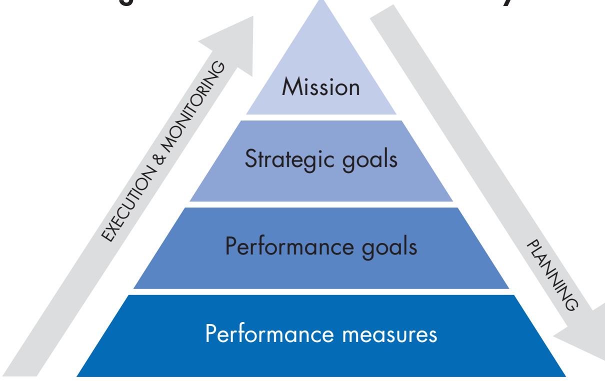
Resource Management Strategy

Performance Section

Managing and Measuring Performance

In FY 2009, FHFA developed and released a five-year strategic plan that presented the agency's long-term strategic goals. Additionally, FHFA develops an annual performance plan that establishes performance goals for specific outcomes to accomplish the strategic goals. The annual performance plan also outlines performance measures used to track the level of achievement of each performance goal. For FY 2010, there were 14 performance goals—10 related to the strategic goals and four related to the agency's resource management strategy. There were 26 performance measures. Performance measures indicate what level the agency achieved for the larger performance goal. This hierarchy of goals and measures is intended to ensure that FHFA devotes its resources to achieve its mission in practical and measurable ways. See Figure 12, which depicts FHFA's hierarchy of goals.

Figure 12. FHFA's Goal Hierarchy



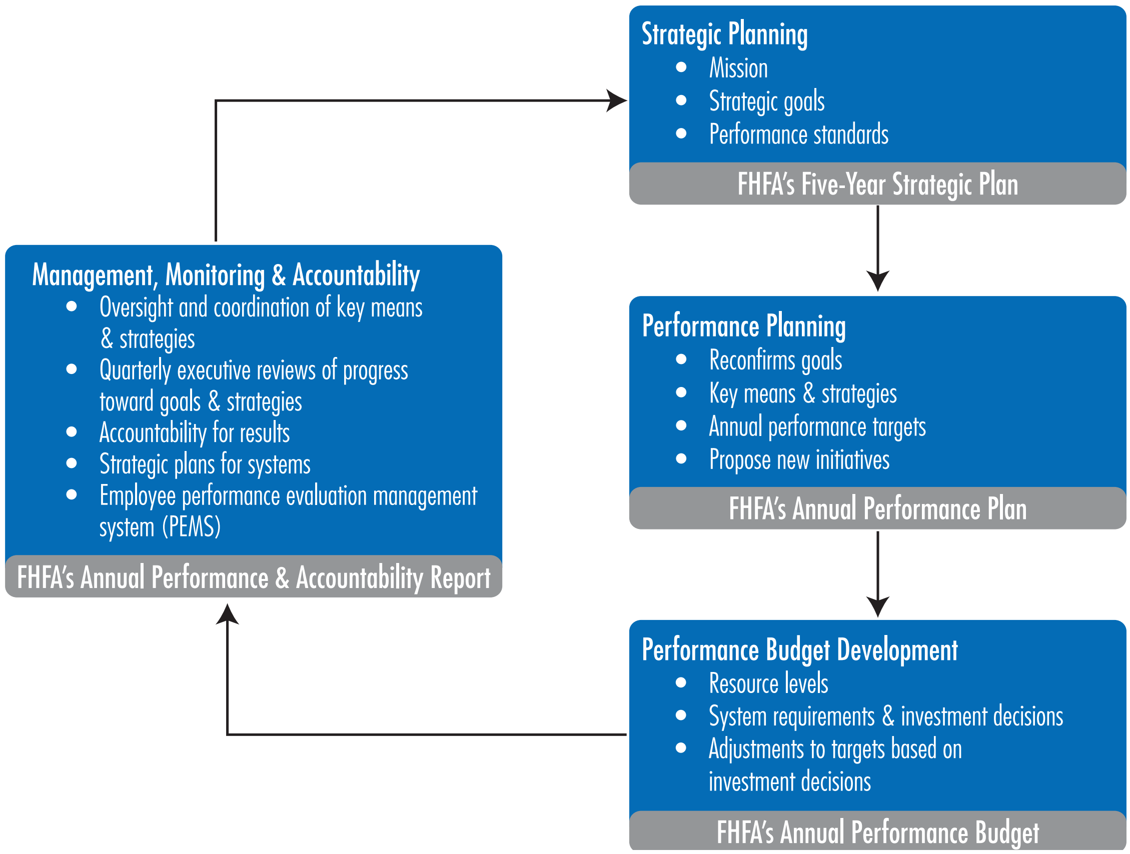
FHFA has adopted a numbering system that links performance measures with strategic and performance goals. For each performance measure, the first digit represents the strategic goal that it supports, the second digit the performance goal, and the third digit the performance measure number related to that performance goal. For example, performance measure 3.2.1 supports strategic goal 3, performance goal 3.2 and is the first performance measure under that performance goal.

The FHFA annual performance budget describes how FHFA achieves its goals and the costs, systems, and initiatives associated with them. FHFA primarily accomplishes its mission by:

- Examining the regulated entities;
- Monitoring their progress in completing their remediation plans;
- Assessing their capital adequacy;
- Setting and enforcing affordable housing goals;
- Monitoring credit and financial market conditions; and
- Conducting research and analysis about the regulated entities and the housing markets.

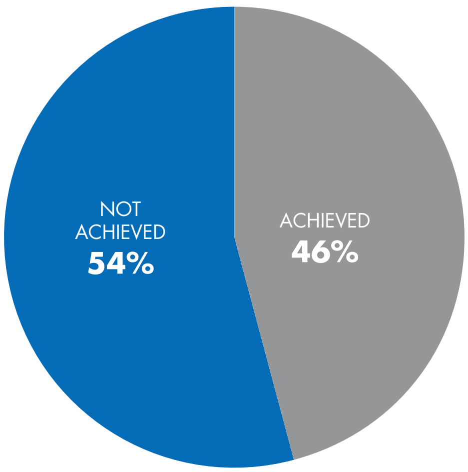
During FY 2010, FHFA executives reported their progress towards achieving the performance measures they were accountable for and then met with the Acting Director and other responsible executives to review the status and accomplishments reports each quarter. The agency used the quarterly reports as the basis for developing this report. See Figure 13 for an outline of FHFA's performance management cycle.

Figure 13. FHFA's Performance Management Cycle



Most of FHFA's performance indicators reflect data and milestones internal to the agency, with the exception of data used as input to the capital calculations. Some of FHFA's performance indicators depend on the actions and results of the regulated entities. The performance information reported in this PAR is complete and reliable. See Figure 14, which depicts FHFA's achievement of performance measures for FY 2010.

Figure 14. FHFA Performance Measures for FY 2010



STRATEGIC GOAL 1

SAFETY AND SOUNDNESS

The housing GSEs operate in a safe and sound manner and comply with legal requirements.

FHFA's primary duty as regulator of the housing GSEs is to promote the safety and soundness of the 14 regulated entities, so they have the financial strength and operational capacity to fulfill their role in the nation's housing finance system. Providing a comprehensive and effective oversight program requires attention to the regulated entities' operations and management; the risks inherent in their activities; the controls they have in place to manage those risks; and economic and business conditions.

FHFA strives to ensure that its supervisory practices further the ability of the regulated entities to fulfill their missions and meet legal requirements.

Performance GOAL 1.1	*Fannie Mae and Freddie Mac (the Enterprises) comply with legal requirements and operate in a safe and sound manner with adequate capital and access to funds and capital.*	
PERFORMANCE MEASURE 1.1.1	Each Enterprise improves in one or more component ratings.	TARGET: September 30, 2010
2010 PERFORMANCE The market risk rating for Freddie Mac improved from critical to significant concerns for the quarter ending March 31, 2010, based on improvements in interest rate risk management. Component ratings did not improve at Fannie Mae during FY 2010. Several areas, improved, increasing the likelihood that some component ratings will improve during the next fiscal year.		
PERFORMANCE MEASURE 1.1.2	Within 90 calendar days of recognition, matters requiring attention (MRAs) are resolved or are in the process of being resolved in accordance with a remediation plan acceptable to FHFA.	TARGET: 90% Quarterly
2010 PERFORMANCE 80 MRAs were cited. Of those, 61, or 76 percent, were resolved or were in the process of being resolved in accordance with a remediation plan acceptable to FHFA within 90 calendar days of recognition. FHFA met this performance measure the last three quarters of the fiscal year, but the target was "not met" because of the failure to meet the target in the first quarter of FY 2010.		

Prior Year Performance – This is a new goal for 2010.

PERFORMANCE RESULTS KEY: Goal Fulfillment

- Target Met
- Target Not Met, But Improved Over Last Year
- Target Not Met

Senior staff of FHFA's Division of Enterprise Regulation

Discussion of Performance Goal 1.1

Since the start of the housing crisis, the Enterprises have incurred sizeable credit-related expenses, and losses on mortgages they own or guarantee. These losses overwhelmed the capital held by the Enterprises and continue to drive capital deficits. FHFA developed and implemented performance measure 1.1.1 in FY 2010, requiring improvement in the Enterprises' safety and soundness ratings based on a number of considerations. Recognizing the significance of the supervisory concerns at each Enterprise and not knowing how long the Enterprises would be in conservatorship, the agency was seeking signs of incremental improvements in the Enterprises' condition and performance. Despite continued stress in the mortgage markets, the market risk rating for Freddie Mac improved from critical to significant concerns based on improvements in interest rate risk and liquidity risk management. However, Fannie Mae did not improve in any component ratings during FY 2010.

In FY 2010, FHFA conducted continuous supervision and targeted examinations as well as supervisory analyses. FHFA also oversaw the remediation activities of the Enterprises and tracked their progress in addressing identified issues. FHFA regularly communicated its conclusions and required corrective actions to the Enterprises' management through meetings, letters, and an annual report of examination, which was provided to and discussed with the Boards of the Enterprises in March 2010. In FY 2010, FHFA identified 80 MRAs at the Enterprises and 61 of them, or 76 percent, were resolved or were in the process of being resolved in accordance with an approved remediation plan. FHFA did not meet its target of 90 percent for FY 2010. FHFA will continue to work to improve the process for resolving MRAs. Feature 1 outlines the GSE Enterprise risk rating structure.

Completeness and Reliability of Performance Data

The data for this performance goal are complete and reliable. The data are created internally, reported in the agency's performance tracking system, and reviewed by senior management quarterly. Data related to supervision activities are collected through FHFA's supervision process and reviewed by quality assurance staff and FHFA management.

Figure 15. GSE Enterprise Risk Rating System

		Quantity of Risk		
		Low	**Moderate**	**High**
Quality of Risk Management	**Strong**	No or Minimal Concerns	No or Minimal, or Limited Concerns	Limited Concerns
	Satisfactory	No or Minimal, or Limited Concerns	Limited Concerns	Significant Concerns
	Requires Improvement	Limited Concerns	Significant Concerns	Significant or Critical Concerns
	Weak	Significant Concerns	Significant or Critical Concerns	Critical Concerns

Feature 1. Risk Rating Structure for the Enterprise

The supervisory rating structure for the Enterprises is referred to as GSE Enterprise Risk (GSEER). GSEER stands for **G**overnance, **S**olvency, **E**arnings, and **E**nterprise **R**isk (credit, market, and operational risks). FHFA examination personnel recommend individual ratings for each risk area and an overall composite rating that provides the agency with a picture of the overall condition and safety and soundness of each Enterprise. The FHFA Director approves the final rating for each Enterprise.

Governance includes policies and controls related to financial and regulatory reporting, leadership effectiveness of the Board of Directors and Enterprise management, compliance, overall risk management, strategy, internal audit, and reputation risk.

Solvency includes capital adequacy as determined by regulatory standards, economic capital, capital management, and planning.

Earnings include the adequacy of earnings to build and maintain capital and provide acceptable returns to shareholders, quality of earnings, earnings projections, integrity of management information systems, and soundness of the business model.

Enterprise Risk includes credit risk, market risk, and operational risk. Credit risk comprises accounting, counterparty, credit models, multifamily, portfolio credit, and single family. Market risk comprises accounting, interest rate, liquidity, and market models. Operational risk comprises accounting, financial reporting, information technology, internal controls, and operational models.

When determining the safety and soundness level for each of the GSEER categories, examiners look at both the quantity of risk relative to earnings and capital and quality of risk management in each area. The rating scheme takes into account external factors, such as current market conditions and internal factors, including how much risk each Enterprise takes on and how well they measure and manage it. Ratings are given for each area on a four-tiered scale:

- No or Minimal Concerns
- Limited Concerns
- Significant Concerns
- Critical Concerns

The overall rating reflects FHFA's judgment about the safety and soundness of the Enterprise.

To determine the risks related to each of the GSEER categories, examiners review the operations and transactions of Fannie Mae and Freddie Mac throughout the year against standards set forth in the agency's supervisory handbook. Examiners complete an assessment and rating at the end of each quarter in a process of continuous supervision and examination. At the end of the calendar year, FHFA summarizes the safety and soundness and financial condition of each Enterprise in its annual *Report to Congress*, including the overall composite GSEER rating.

The supervisory handbook and annual *Report to Congress* are available on FHFA's website at **www.fhfa.gov**. See Figure 15 for a description of how the GSE Enterprise Risk Rating System reflects both the level of risk and the quality of risk management.

Performance GOAL 1.2	*The FHLBanks and the Office of Finance comply with legal requirements and operate in a safe and sound manner with adequate capital and access to funds and capital.*

PERFORMANCE MEASURE 1.2.1	Each FHLBank is rated 2 or better, or operates under a performance improvement plan acceptable to FHFA within 90 calendar days of a downgrade below 2.	TARGET: Quarterly, beginning JUNE 30, 2010

2010 PERFORMANCE
Seven FHLBanks were rated below 2 in FY 2010. Four were operating under an acceptable performance improvement plan within 90 days of the downgrade, three were not.

PERFORMANCE MEASURE 1.2.2	Each FHLBank is classified as adequately capitalized or operates in compliance with an approved capital restoration plan within 90 calendar days of the classification.	TARGET: Quarterly

2010 PERFORMANCE
Eleven of the 12 FHLBanks were adequately capitalized throughout FY 2010. One bank was classified as undercapitalized. That bank subsequently stipulated to a consent order, which constituted its approved capital restoration plan.

PERFORMANCE MEASURE 1.2.3	Within 90 calendar days of recognition, matters requiring attention (MRA) are resolved or are in the process of being resolved in accordance with a remediation plan acceptable to FHFA.	TARGET: 90% Quarterly

2010 PERFORMANCE
FHFA examiners provided MRAs to FHLBanks during FY 2010. All MRAs were either successfully resolved or in the process of being resolved in accordance with an approved remediation plan within 90 calendar days.

Prior Year Performance – This is a new goal for 2010.

Discussion of Performance Goal 1.2

The FHLBanks make loans, called advances, to their members and eligible housing associates, secured by mortgages and other collateral pledged by the borrower. The FHLBanks assume and manage market, credit, and operational risks in of their advance business, purchases of whole mortgages, and investments.

FHFA examined each of the FHLBanks and the Office of Finance for safety and soundness during FY 2010. Each FHLBank and the Office of Finance was assigned composite and component examination ratings. Ratings are outlined in Feature 2. Performance measure 1.2.1 established a target of 100 percent of the institutions (the FHLBanks and the Office of Finance) achieving a composite rating of 2 or better, or operating under an FHFA-approved performance improvement plan within 90 calendar days of a downgrade below 2. The standard was not met. Of the seven institutions that had a rating lower than 2, four institutions had an acceptable remediation plan in place within 90 days, but three institutions did not. Of the three FHLBanks that were not operating under an approved remediation plan within 90 days of a downgrade, one subsequently adopted a plan acceptable to FHFA during FY 2010. The other two FHLBanks adopted plans acceptable to FHFA during the first quarter of FY 2011.

Feature 2. FHLBank Rating System

FHFA uses a risk-focused rating system to rate each FHLBank and the Office of Finance annually.

FHFA issues ratings of the FHLBanks based on an evaluation of five key components:

- Corporate governance
- Market risk
- Credit risk
- Operational risk
- Financial condition and performance

The composite rating for the Office of Finance is based on an evaluation of corporate governance and operational risk.

FHFA takes into account the administration of an FHLBank's affordable housing and community investment activities under the corporate governance and operational risk components of the rating system.

Under the rating system, FHFA assigns each FHLBank and Office of Finance a composite rating from 1 to 4. A rating of 1 indicates the lowest degree of supervisory concern, and a rating of 4 indicates the highest degree of supervisory concern. FHFA bases the composite rating of each institution on the ratings of the components, which FHFA also rates on a scale of 1 to 4.

The composite rating assigned to an institution is not an arithmetic average of the component ratings. Instead, the relative importance of each component is determined case-by-case within the parameters established by this rating system.

For each of the components, the rating system guidance describes a nonexclusive list of the principal evaluative factors that relate to that component. FHFA judges the rating components as follows:

Corporate Governance. An institution's corporate governance rating is based on an assessment of factors relating to the Board of Directors and senior management, risk management and controls, and compliance.

Market, Credit, and Operational Risks. Examiners separately evaluate the market, credit, and operational risks of each FHLBank in two dimensions—the level of risk exposure and the quality of risk management. Examiners assess the level of market, credit, and operational risks as low, moderate, or high, and they assess the quality of risk management as strong, adequate, or weak. To derive component ratings for market, credit, and operational risks, examiners use a matrix to combine the level of risk exposure and the quality of risk management. See Figure 16. Examiners assign separate ratings to market, credit, and operational risks.

Financial Condition and Performance. An FHLBank's condition and performance rating is based on an assessment of key financial condition and performance factors that are not directly addressed under the market, credit, and operational risk components of the rating system, including earnings and profitability, operating efficiency, capital and retained earnings, and liquidity.

Following the completion of the annual examination of each FHLBank, FHFA summarizes the safety and soundness and financial condition of each FHLBank and Office of Finance and includes a composite rating in the report of examination delivered to the FHLBank's board of directors. The agency's annual *Report to Congress* describes the agency's assessment of each FHLBank, but does not explicitly include the assigned supervisory ratings.

The examination manual and annual *Report to Congress* are available on FHFA's website at **www.fhfa.gov**.

Figure 16. FHLBank Rating System

		Level of Risk		
		Low Risk	Moderate Risk	High Risk
Quality of Risk Management	Strong	1	1-2	2-3
	Adequate	1-2	2-3	3-4
	Weak	2-3	3-4	4

During FY 2010, FHFA assessed the FHLBanks' quarterly capital compliance position and prepared prompt corrective action capital classification letters each quarter. One FHLBank was classified as undercapitalized under the Director's discretionary authority in November 2009, and was not operating in compliance with an approved capital restoration plan within the 90-day target. That situation has since been remediated. FHLBanks' Types of Capital are displayed in Feature 3.

During examinations of the FHLBanks and the Office of Finance, FHFA identifies matters requiring attention (MRAs) by an institution's management or Board for correction. FHFA established performance measure 1.2.3 to assess the timely resolution of MRAs. During FY 2010, each MRA was either resolved or was in the process of being resolved in accordance with an approved remediation plan within 90 calendar days.

Completeness and Reliability of Performance Data

The data for this performance goal are complete and reliable. The data are created internally, reported in the agency's performance tracking system and reviewed by senior management quarterly. Data related to supervision activities are collected through FHFA's supervision process and reviewed by FHFA management. Standards for individual risk area rating and composite ratings are outlined in the *FHLBank Examination Manual*, which is available to the public at **www.FHFA.gov**.

Feature 3. FHLBanks' Types of Capital

Capital adequacy is essential to the regulated entities' safety and soundness and their continued financial viability. The discussion below attempts to explain different types of capital in the context of the FHLBanks.

Regulatory

FHLBanks may issue either Class A stock with a six-month redemption notice, or Class B stock with a five-year redemption notice. Under certain conditions, FHLBank stock may be repurchased before the scheduled redemption.

- *Permanent Capital* is the sum of the par value of Class B stock outstanding and retained earnings as determined in accordance with generally accepted accounting principles (GAAP).
- *Total Capital* is the sum of permanent capital, the par value of Class A stock outstanding, a general allowance for losses, and the amount of any other instruments identified in an FHLBank's capital plan that FHFA has determined to be available to absorb losses. FHFA considers mandatorily redeemable capital stock to be regulatory capital, because it is "paid-in" capital and may absorb losses up to the day of its redemption. When a member submits a request to have the FHLBank redeem its stock, GAAP requires the FHLBank to categorize that stock on its statement of condition as a liability–mandatorily redeemable capital stock. Dividends on mandatorily redeemable capital stock are treated as an interest expense on the statement of income.

Accounting

- *Accounting total capital* is the amount by which the book value of assets exceeds the book value of liabilities. For the FHLBanks, that is the sum of retained earnings and accumulated other comprehensive income (AOCI). AOCI reflects (1) the differences between the amortized cost of available-for-sale securities less estimated credit losses (if any) and the current market value of those securities; (2) differences between the amortized cost of held-to-maturity securities less estimated credit losses and the market value of those securities measured at the time any credit losses were recognized; and (3) gains or losses on certain types of hedging transactions. Although included in calculations of accounting total capital, AOCI is excluded from regulatory capital. The exclusion of AOCI from regulatory capital is consistent with its exclusion from Tier 1 capital for commercial banks and thrifts.

STRATEGIC GOAL 2

AFFORDABLE HOUSING

The housing GSEs support a stable, liquid, and efficient mortgage market including sustainable homeownership and affordable housing.

FHFA oversees the homeownership and affordable housing activities of the regulated entities. As part of that responsibility, FHFA is responsible for implementing affordable housing goals and overseeing the administration of programs designed to sustain homeownership and promote affordable housing.

FHFA works to ensure that all homeownership and affordable housing programs comply with laws and regulations. FHFA strives to keep Congress, industry stakeholders, and the general public informed of key issues related to the agency and the regulated entities.

Performance GOAL 2.1	*FHFA ensures the housing GSEs support a stable, liquid and efficient mortgage market.*	
PERFORMANCE MEASURE 2.1.1	Each housing GSE maintains liquidity levels consistent with FHFA regulatory requirements.	TARGET: Monthly
2010 PERFORMANCE Fannie Mae did not maintain liquidity levels consistent with FHFA requirements. All of the other housing GSE's met the liquidity requirements.		Target Not Met
PERFORMANCE MEASURE 2.1.2	Absent a revival of the private market in 2010, each Enterprise's share of single-family mortgage purchases and originations does not decline by more than 10% of the share obtained in FY 2009.	TARGET: Annually
2010 PERFORMANCE For Fannie Mae, the share of single-family mortgage purchases and originations decreased from 40.04 percent in FY 2009 to 36.26 percent in FY 2010. For Freddie Mac, the share of single-family mortgage purchases and originations decreased from 25.61 percent in FY 2009 to 23.75 percent in FY 2010.		Target Met
Prior Year Performance – This is a new goal for 2010.		

Discussion of Performance Goal 2.1

FHFA uses its regulatory authority to establish prudential liquidity levels. Fannie Mae did not meet all three of the FHFA liquidity requirements, though it was in compliance with two of the requirements. Fannie Mae management expects it to be in compliance with all three liquidity requirements by December 31, 2010. Freddie Mac met all three FHFA liquidity requirements.

All FHLBanks met liquidity requirements each month during FY 2010. On September 1, 2010, one of the FHLBanks did not meet liquidity requirements for the rollover and renew scenario due to an operational error. FHFA issued a draft weakness finding requiring

PERFORMANCE RESULTS KEY: Goal Fulfillment

- Target Met
- Target Not Met, But Improved Over Last Year
- Target Not Met

the FHLBank to acquire or create an automated tracking tool that captures trade data and projects the FHLBank's liquidity position.

With the ongoing lack of funding in the private market, the Enterprises have helped stabilize the housing market by continuing to ensure the availability of mortgage credit. Fannie Mae's share of single-family mortgage purchases and originations decreased from 40.04 percent in FY 2009 to 36.26 percent in FY 2010. Freddie Mac's share of single-family mortgage purchases and originations decreased from 25.61 percent in FY 2009 to 23.75 percent in FY 2010.

Senior staff of FHFA's Division of Federal Home Loan Bank Regulation

Performance GOAL 2.2

FHFA ensures the housing GSEs provide leadership in housing finance and affordable housing by operating these programs in an effective and efficient manner, developing products, establishing partnerships, and financing homes for very low-, low-, and moderate-income households.

PERFORMANCE MEASURE 2.2.1

The FHLBanks' AHP funds are awarded in compliance with laws and regulations.

TARGET: Annually

2010 PERFORMANCE

FHFA completed AHP examinations at all 12 FHLBanks. FHFA identified one violation and recommended remediation.

PERFORMANCE MEASURE 2.2.2

Issue affordable housing goal regulations covering Fannie Mae, Freddie Mac, and the FHLBanks, as applicable, pursuant to the Housing and Economic Recovery Act of 2008 (HERA).

TARGET: May 1, 2010

2010 PERFORMANCE

FHFA sent a final rule establishing affordable housing goals for Fannie Mae and Freddie Mac on September 1, 2010. On May 24, 2010, FHFA sent to the *Federal Register* a proposed rule that would establish affordable housing goals for the FHLBanks.

PERFORMANCE MEASURE 2.2.3

Issue a duty to serve regulation per HERA requiring the Enterprises to serve the manufactured housing and rural housing segments of the housing market and to preserve multifamily affordable housing.

TARGET: May 15, 2010

2010 PERFORMANCE

On May 28, 2010, FHFA sent a proposed duty to serve regulation for the Enterprises to serve the manufactured housing and rural housing segments of the housing market. FHFA did not meet the target of issuing a regulation by May 15, 2010.

Prior Year Performance – This is a new goal for 2010.

Completeness and Reliability of Performance Data

The data for this performance goal are complete and reliable. The data are created internally, reported in the agency's performance tracking system, and reviewed by senior management quarterly. For FHLBanks, liquidity levels are verified by examining internal reports provided by the FHLBanks. Data related to supervision activities are collected through FHFA's supervision process and reviewed by FHFA management.

Discussion of Performance Goal 2.2

As required by law, the FHLBanks direct 10 percent of their annual earnings (after their contribution to pay a portion of the interest on bonds issued by the Resolution Funding Corporation) to the AHP. FHFA ensures that the FHLBanks award AHP funds in compliance with laws and regulations. During the calendar year 2010, FHFA conducted examinations of the AHP, Community Investment Program, and other Community Investment Cash Advance programs at all 12 FHLBanks. The AHP examination team visited those FHLBanks with AHP-related MRAs between annual examinations to assess progress in remediating findings. FHFA also held quarterly teleconferences with each FHLBank's community investment officer to address examination findings and identify emerging issues.

FHFA is required to issue affordable housing goal regulations for the regulated entities. Performance measure 2.2.2 established a target issuance date of May 1, 2010. FHFA did not meet the target date because of continued uncertainty in the housing market and competing agency objectives. FHFA sent a final rule to the *Federal Register* establishing new housing goals for the Enterprises on September 1, 2010. The final rule establishes three single-family, owner-occupied home purchase mortgage goals for low-income families, very low-income families, and families living in geographical areas with lower-income populations, areas with high concentrations of minority residents, and federally declared disaster areas.

Figures 17 and 18 outline the Enterprises performance for the 2009 Housing goals and Subgoals. Figure 19 shows the Enterprises Housing goals and Subgoals for 2010.

Figure 17. Enterprise Performance on 2009 Housing Goals

Housing Goals	2009 Target	2009 Performance	
		Fannie Mae	Freddie Mac
Low- and Moderate-Income	43%	47.6%	44.7%
Underserved Areas	32%	28.8%	26.8%
Special Affordable	18%	20.7%	17.8%

Figure 18. Enterprise Performance on 2009 Housing Subgoals

Housing Subgoals	2009 Target	2009 Performance	
		Fannie Mae	Freddie Mac
Low- and Moderate-Income	40%	51.7%	48.4%
Underserved Areas	30%	31.0%	27.9%
Special Affordable	14%	23.2%	20.6%
Special Affordable Multifamily Subgoals			
Fannie Mae	$6.56B	$6.42B	NA
Freddie Mac	$4.6B	NA	$3.69B

Figure 19. 2010 Enterprise Housing Goals and Subgoals in Final Rule		
Single-Family Goal Category	**Proposed Rule**	**Final Rule**
Low-Income Home Purchase	27%	27%
Very Low-Income Home Purchase	8%	8%
Low-Income Refinance	25%	21%
Low-Income Areas HP Subgoal[1]	13%	13%
Low-Income Areas HP Goal[1]	NA	24%
Low-Income Multifamily Goals		
Fannie Mae	237,000 units	177,750 units
Freddie Mac	215,000 units	161,250 units
Very Low-Income Multifamily Goals		
Fannie Mae	57,000 units	42,750 units
Freddie Mac	28,000 units	21,000 units

[1] Mortgages to families with incomes below area median income (AMI) in disaster areas are included in the low-income areas home purchase goal, but not in the subgoal.

The final rule includes a goal for single-family, owner-occupied refinanced mortgages for low-income families. It also includes multifamily goals, targeted to rental units for low-income families, and subgoals, targeted to very low-income families and required reporting on financing of low-income units in small multifamily properties. On May 24, 2010, FHFA sent to the *Federal Register* a proposed rule that would establish a framework for affordable housing goals for the 12 FHLBanks. FHFA expects to finalize that regulation shortly.

HERA requires FHFA to issue a duty to serve regulation that obligates the Enterprises to serve three specified underserved markets – manufactured housing, affordable housing preservation and rural markets – in order to increase the liquidity of mortgage investments and improve the distribution of capital available for mortgage financing for very low-, low- and moderate income families in those markets. In order to remain consistent with the requirements of conservatorship, FHFA limited the proposed rule to existing core businesses at the Enterprises and prohibited the Enterprises from engaging in new lines of business as a result of the proposed duty to serve rule. FHFA set a target to complete the duty to serve regulation by the second quarter of FY 2010. FHFA did not meet the target date. The agency sent the proposed duty to serve regulation to the *Federal Register* on May 28, 2010. The agency received and is reviewing over 3,900 comments on the proposed rule.

The proposed rule establishes a methodology for evaluating and rating Enterprise performance in each underserved market for 2010 and beyond, and describes the transactions and activities that would be considered for compliance. Under the proposed rule, the Enterprises would be evaluated on the following four statutory assessment factors:

1. Development of loan products, more flexible underwriting guidelines, and other innovative approaches to providing financing;
2. Extent of outreach to qualified loan sellers and other market participants;
3. Volume of loans purchased relative to the market opportunities available (subject to the statutory condition that FHFA not establish specific quantitative targets); and
4. Amount of investments and grants in projects that assist in meeting the needs of the underserved markets.

Completeness and Reliability of Performance Data

The data for this performance goal are complete and reliable. The data are created internally, reported in the agency's performance tracking system, and reviewed by senior management quarterly. Data related to supervision activities are collected through FHFA's supervision process and reviewed by FHFA management.

Performance GOAL 2.3	*FHFA supports an efficient secondary mortgage market through research that increases transparency of the housing GSEs' risks and activities and improves understanding of mortgage market developments.*	
PERFORMANCE MEASURE 2.3.1	Expand the quarterly House Price Index (HPI) and related products by producing a median HPI and increasing the number of geographical areas covered.	TARGET: September 30, 2010
2010 PERFORMANCE FHFA produced an HPI for Puerto Rico, which was released with the FY 2010 first quarter HPI in May. FHFA has also refined the process for estimating mean and median home prices at both the state and national level.		Target Met
PERFORMANCE MEASURE 2.3.2	Publish at least six working papers, mortgage market notes, or research papers.	TARGET: September 30, 2010
2010 PERFORMANCE FHFA published two working papers, six (one of which was an update) research papers, and three (two of which were updates) mortgage market notes during FY 2010.		Target Met
Prior Year Performance – This is a new goal for 2010.		

Discussion of Performance Goal 2.3

FHFA's research promotes an efficient secondary mortgage market. Accurate and timely information is critical to understanding mortgages, mortgage markets, and the housing GSEs' risks and activities. FHFA is uniquely positioned to serve as an information resource on these issues. It published a variety of data and reports throughout the year that increased the transparency of the housing GSEs' risks and activities, and informed the public about mortgage market developments.

During FY 2010, FHFA expanded its reporting on house prices by developing an HPI for Puerto Rico. FHFA also published a research paper describing a process for estimating mean and median home prices at both the state and national level, including up-to-date estimates.

In May 2010, FHFA delivered its 2009 *Report to Congress* and published the Report on its website (**www.fhfa.gov**). FHFA's *Report to Congress* includes conclusions from the examinations of the Enterprises and FHLBanks, information about the compensation of FHLBank directors, and housing mission and goals information for all 14 regulated entities.

FHFA regularly communicates with Congress, other regulatory agencies, and industry participants. During FY 2010, FHFA also contributed substantially to the public's understanding of housing-related topics through a variety of reports, research papers, and staff working papers that are available on the agency's website (**www.fhfa.gov**). In July 2010, FHFA also published *Fannie and Freddie Mac Single-Family Guarantee Fees* in 2008 and 2009. The results from that report are summarized in Feature 4.

PERFORMANCE RESULTS KEY: Goal Fulfillment

- Target Met
- Target Not Met, But Improved Over Last Year
- Target Not Met

Feature 4. Guarantee Fee Study Results for 2008 and 2009

HERA requires FHFA to conduct an ongoing study of the guarantee fees charged by the Enterprises and issue a report to Congress each year. Fannie Mae and Freddie Mac buy single-family mortgages from mortgage companies, commercial banks, credit unions, and other financial institutions.

In most cases, a seller receives MBS in exchange for the loans. Each Enterprise guarantees the payment of principal and interest on its MBS and charges a fee for providing that guarantee. The guarantee fee covers projected credit losses from borrower defaults over the life of the loans, administrative costs, and a return on capital. Lender guarantee fee payments generally take the form of ongoing monthly payments and frequently also include an upfront payment at the time of Enterprise loan acquisition. HERA requires FHFA to identify and analyze the:

- Revenue and costs associated with the Enterprises' guarantees,
- Factors considered in determining the fees,
- Average fee charged,
- Revenues and costs based on product type and risk classifications,
- Fees per lender size group, and
- Changes from the previous year.

The sample of mortgages used to prepare the guarantee fee report represented 89 percent and 96 percent, respectively, of the unpaid principal balance of single-family mortgages the Enterprises acquired in 2008 and 2009. The sample is based on flow business, but not bulk negotiated transactions. Analysis of that data indicated the following:

1. Although Fannie Mae and Freddie Mac consider model-derived estimates of cost in determining their single-family guarantee fees, their pricing often subsidizes their guarantees on some mortgages using higher returns than they expect to earn on guarantees of other loans. In 2009 as in 2008, cross-subsidization in single-family guarantee fees charged by each Enterprise was evident across product types, credit score categories, and loan-to-value (LTV) ratio categories. In each case, there were cross-subsidies from mortgages that posed lower credit risk on average to loans that posed higher credit risk. The greatest estimated subsidies generally went to the highest-risk mortgages. However, because the share of higher-risk loans acquired was substantially lower in 2009, overall there was less cross-subsidization in Enterprise single-family guarantee fee pricing than in the previous year.
2. The average total guarantee fee charged by Fannie Mae and Freddie Mac on single-family mortgages acquired on a flow basis decreased from 25 basis points in 2008 to 22 basis points in 2009. That change reflects declines in both the average ongoing fee and the average upfront fee.
   - The average ongoing fee declined 1 basis point, from 14 basis points to 13 basis points, due to an improvement in the credit quality of acquisitions.
   - The average upfront fee (as measured in estimated annualized revenue) fell 2 basis points, from 11 basis points to 9 basis points. That decline reflected the improved credit quality of acquisitions, with fewer loans being assessed upfront fees for specific risk attributes, and the longer expected lives of loans acquired by the Enterprises.
3. The decline in the total guarantee fees charged by each Enterprise in 2009, resulted from significant improvement in the credit profile of the single-family mortgages they acquired relative to 2008. There were improvements across the product, credit score, and LTV ratio spectrums: as 15-year fixed-rate mortgages grew as a share of total acquisitions; credit scores improved; and fewer loans with low down payments were acquired. The share of mortgages with risk layering—multiple features that increase credit risk—also fell significantly. The improvement in the credit profile of acquisitions more than offset the effect of the pricing increases implemented in 2008 and 2009, resulting in the decline in total guarantee fees charged in 2009.
4. The improvement in the credit profile of Enterprise acquisitions in 2009, also reduced the average expected costs of bearing the credit risk of those loans. The net effect of lower costs and lower guarantee fees charged was an improvement in the estimated fee gaps for the three major product categories: 30-year fixed-rate, 15-year fixed-rate, and adjustable-rate mortgages. Further, each Enterprise expected, on average at the time of loan acquisition, to earn its target rate of return on non-HARP mortgages acquired in 2009. HARP is the Home Affordable Refinance Program.
5. Average guarantee fees charged by the Enterprises decreased for every LTV-ratio category in 2009, reflecting improvements in the credit profile of mortgages acquired in each category.

Fees decreased the most for loans that had LTV ratios above 80 percent.

6. The improvement in the credit profile of acquisitions tended to reduce model-estimated costs in 2009 and improved the average fee gaps for loans with LTV ratios of 80 percent and below. Loans with LTV ratios above 80 percent continued to have negative fee gaps on average, and those gaps were much wider than in 2008. That widening was due to the Enterprises' acquisition of HARP mortgages. HARP activity began in the second quarter of 2009, and steadily increased over the remainder of 2009. For the Enterprises combined over the full year, HARP activity represented 4 percent of 2009 acquisition volume.
7. Fannie Mae and Freddie Mac supported HARP by limiting the upfront fees they charged on HARP mortgages. As a result, the estimated guarantee fees for those loans were much lower, relative to the fees that Enterprise costing models indicated were required to earn target rates of return, than for non-HARP mortgages. Despite the larger estimated negative fee gaps on HARP mortgages, their acquisition was beneficial to the Enterprises, since the loans refinanced existing mortgages that had higher or less stable monthly payments, thus reducing the Enterprises' exposure to credit risk, and the guarantee fees charged were generally higher than the fees on the mortgages they refinanced. On average, fees charged for non-HARP loans by each Enterprise were sufficient to cover expected costs, including a reasonable profit.
8. Single-family guarantee fees charged by the Enterprises decreased modestly for the highest and lowest credit score categories in 2009. In the middle credit score tiers, fees increased slightly. The Enterprises did not expect, at the time of loan acquisition, to earn their target rates of return on guarantees of loans in the credit score categories below 720. The estimated negative fee gaps in those categories were wider than in 2008, but the share of mortgages acquired in the categories was much lower.
9. A significant share of the single-family mortgages acquired by each Enterprise comes from a small group of large sellers. Loans acquired from the top 10 sellers combined accounted for 79 percent and 74 percent of their combined business volume in 2008 and 2009, respectively. Average guarantee fees on single-family mortgages decreased modestly in 2009, for each of the three acquisition, volume-based groups of sellers analyzed by FHFA.
10. The lenders that sell smaller volumes of single-family mortgages to the Enterprises tend to pay higher guarantee fees on loans of similar credit quality. That differential occurs for several reasons. First, in determining the guarantee fees they charge, the Enterprises give consideration to the total volume of mortgages delivered by each seller, since larger volumes contribute more to the liquidity that supports the demand for each Enterprise's outstanding MBS. Second, the largest sellers have achieved a degree of influence that can be used to negotiate better terms of business. Third, the administrative costs of doing business with a seller are generally fixed, so the per loan cost of guaranteeing a larger seller's business is lower. Fourth, the Enterprises' acquisition policies and standards expose them to counterparty risk, which tends to be higher for small-volume sellers than for typical larger-volume sellers, many of whom are subject to national bank and thrift regulatory standards and extensive financial disclosure requirements and may have access to varied financing and capital sources. Also, smaller sellers typically choose to sell whole loans, since they tend to lack the volume and capacity to swap loans for MBS. The whole loan programs offer certain benefits to smaller sellers such as faster cash proceeds and reduced hedging costs.

Completeness and Reliability of Performance Data

The data for this performance goal are complete and reliable. The data are created internally, reported in the agency's performance tracking system, and reviewed by senior management quarterly. Data related to supervision activities are collected through FHFA's supervision process and reviewed by quality assurance staff and FHFA management.

PERFORMANCE RESULTS KEY: Goal Fulfillment

- Target Met
- Target Not Met, But Improved Over Last Year
- Target Not Met

Performance GOAL 2.4	*FHFA collaborates with other Federal agencies and stakeholders to share information concerning mortgage markets, the nation's housing finance system and regulatory issues.*	
PERFORMANCE MEASURE 2.4.1	Meet with the President's Working Group, Federal Housing Finance Oversight Board, Financial Stability Oversight Board (FSOB), the housing GSEs, and other stakeholders quarterly.	TARGET: 100%
2010 PERFORMANCE FHFA met quarterly with the President's Working Group, Federal Housing Finance Oversight Board, and FSOB. FHFA also met regularly with industry stakeholders. The Acting Director met with the CEOs of Fannie Mae and Freddie Mac on a weekly basis.		
PERFORMANCE MEASURE 2.4.2	Respond to Congressional inquiries within 15 business days.	TARGET: 90%
2010 PERFORMANCE For FY 2010, FHFA responded to 253 formal congressional inquiries, and FHFA responded to 88 percent of those inquiries within 15 business days.		

Prior Year Performance – This is a new goal for 2010.

Discussion of Performance Goal 2.4

FHFA is committed to providing accurate information to industry stakeholders and the public in a timely way. It regularly updates its website to provide information on the regulated entities and issues concerning the agency. Some features of the website include a quarterly house price index, an HPI calculator, speeches and testimony, policies and guidelines, capital classifications, research and working papers, and news releases.

FHFA also continued to respond promptly to inquiries from the public during FY 2010. When FHFA receives inquiries from the public, it responds as quickly as possible, and for those inquiries that do not come within the agency's purview, FHFA staff makes every effort to direct the inquirer to the appropriate source.

FHFA met quarterly with industry stakeholders and increased coordination and outreach on a number of issues pertaining to the regulated entities. FHFA's Acting Director participated in the President's Working Group on Financial Markets and serves on the Financial Stability Oversight Council and the Financial Stability Oversight Board. The Acting Director chairs the Federal Housing Finance Oversight Board. The Acting Director and other agency representatives met with the Enterprises on a regular basis to discuss matters specifically associated with the conservatorships.

FHFA remains committed to prompt and clear communication with members of Congress and their staffs. FHFA set a target of responding to congressional inquiries within 15 business days at least 90 percent of the time. FHFA met this target every quarter except the first quarter of FY 2010. During the first quarter of FY 2010, FHFA met the 15-day target on 78 percent of congressional inquiries. FHFA has enhanced its process for responding to inquiries to improve the timeliness of its responses.

Completeness and Reliability of Performance Data

The data for this performance goal are complete and reliable. The data are created internally, reported in the agency's performance tracking system, and reviewed by senior management quarterly. Data related to supervision activities are collected through FHFA's supervision process and reviewed by quality assurance staff and FHFA management.

STRATEGIC GOAL 3

CONSERVATORSHIP

FHFA preserves and conserves the assets and property of the Enterprises, ensures focus on their housing mission and facilitates their financial stability and emergence from conservatorship.

The Enterprises have been operating in conservatorship since September 2008. FHFA works to preserve and conserve the assets of the Enterprises so that they may continue to fulfill their mission and mitigate the systemic risk that contributed to instability in the financial markets. While FHFA holds the powers of the management, board and shareholders of each Enterprise, the Enterprises themselves are responsible for normal business decisions, activities, and day-to-day operations.

While in conservatorship, the Enterprises continue to play a crucial role in efforts to prevent avoidable foreclosures and to provide stability to the housing market. In those regards, the conservatorships have been effective to date, and as conservator, FHFA has worked to ensure that the programs and activities of the Enterprises aimed at resolving problems in the mortgage market are efficient and effective.

Performance GOAL 3.1

Preserve and conserve each Enterprise's assets and property.

PERFORMANCE MEASURE 3.1.1	Fill vacancies on the Boards and senior management teams within 180 calendar days.	TARGET: Quarterly
2010 PERFORMANCE Two vacancies, one on Freddie Mac's Board and one on Fannie Mae's senior management team, were not filled within 180 calendar days.		
PERFORMANCE MEASURE 3.1.2	Receive from the Enterprises and review a complete inventory of assets, partnerships, contracts, and litigation activities.	TARGET: Quarterly, beginning December 31, 2009
2010 PERFORMANCE Fannie Mae's inventory was received by FHFA on July 13, 2010, and Freddie Mac's inventory was received on July 16, 2010.		

Prior Year Performance – This is a new goal for 2010.

PERFORMANCE RESULTS KEY: Goal Fulfillment

- Target Met
- Target Not Met, But Improved Over Last Year
- Target Not Met

Discussion of Performance Goal 3.1

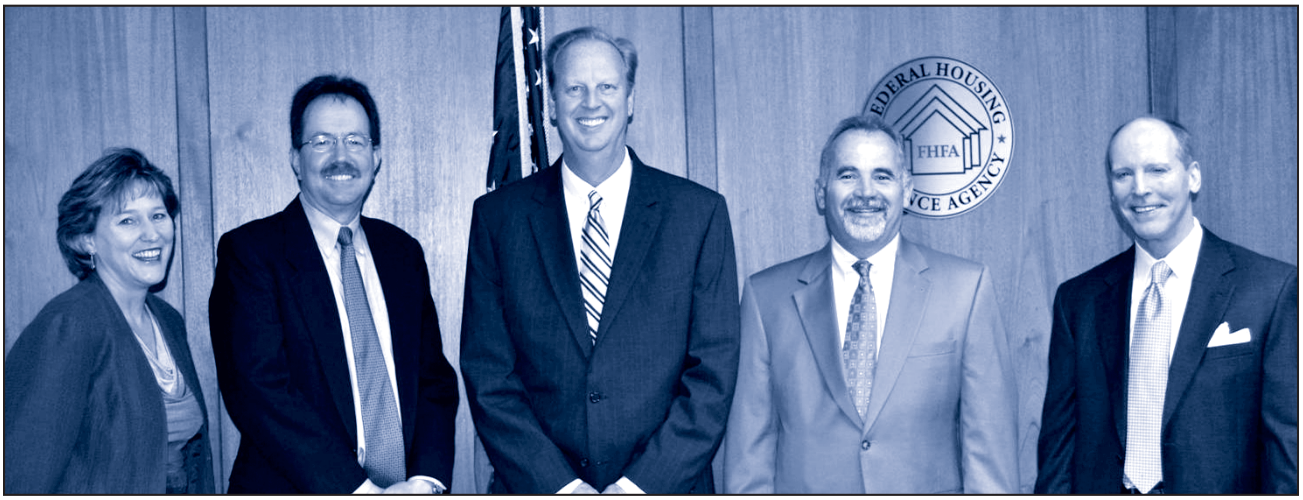
FHFA worked to ensure that critical vacancies on the Boards and senior management teams at the Enterprises were filled with well-qualified individuals. Uncertainties about the future of the Enterprises as well as the economy in general led to several vacancies. Recognizing the importance of filling key positions as the Enterprises strive to fulfill their mission, FHFA implemented performance measure 3.1.1, which set a target of filling all vacancies on the Boards and senior management teams within 180 calendar days. Despite the challenges of attracting and retaining senior managers and board members for two companies in conservatorship, the Enterprises and FHFA successfully filled most key positions within 180 days. Two vacancies, one at each of the Enterprises, were not filled within the time frame. Fannie Mae filled its head of external relations position more than 30 days past the target date. During this time frame, Fannie Mae filled the position on an interim basis with an internal and well-qualified individual, mitigating risk and exposure. Freddie Mac's vacant board position was filled on October 14, 2010, just outside of the 180-day window following a successful search for a well-qualified candidate. Both Enterprises kept FHFA informed of their progress in recruiting candidates.

Some key personnel at both Enterprises have sought other employment in light of uncertainty about the future structure of the Enterprises and the overall condition of the economy. FHFA has worked with the Enterprises to ensure that positions below the Board and senior management levels are filled.

As conservator, FHFA has closely monitored the assets and activities of the Enterprises. For FY 2010, FHFA implemented performance measure 3.1.2, which sets the target of receiving from the Enterprises and reviewing a complete inventory of assets, partnerships, contracts, and litigation activities each quarter. FHFA received Fannie Mae's initial inventory, covering the first quarter of FY 2010, on July 13, 2010. FHFA received Freddie Mac's inventory on July 16, 2010. FHFA commenced review and evaluation of the inventories in July 2010. The initial quarterly receipt was delayed as a result of processes designed to ensure ongoing quarterly submissions for future quarters. Given the implementation of these processes, future receipt of the data should be timely.

Completeness and Reliability of Performance Data

The data for this performance goal are complete and reliable. The data are created internally, reported in the agency's performance tracking system, and reviewed by senior management quarterly. Data related to supervision activities are collected through FHFA's supervision process and reviewed by quality assurance staff and FHFA management.



Staff of FHFA's Office of Conservatorship Operations

Performance GOAL 3.2 — *Delegate appropriate authorities to each Enterprise's management to continue with or improve upon the Enterprises' mission and business operations.*

PERFORMANCE MEASURE 3.2.1	FHFA provides approvals and guidance to the Enterprises on conservatorship-related issues within 30 business days.	TARGET: 80% Quarterly

2010 PERFORMANCE
FHFA provided approvals and guidance to the Enterprises on conservatorship-related issues within 30 days, 44 percent of the time during the third quarter and 54 percent of the time during the fourth quarter of 2010. Data and systems were not fully developed or reliable during the first two quarters of 2010.

Prior Year Performance – This is a new goal for 2010.

Discussion of Performance Goal 3.2

FHFA developed performance measure 3.2.1 recognizing the importance of timely and sound guidance to the Enterprises. This measure sets a quarterly target of providing an initial response to the Enterprises' requests on matters pertaining to the conservatorship within 30 business days. FHFA did not meet this target during any of the four quarters of FY 2010, but improved its tracking process and overall response time throughout the year. FHFA will continue to improve this process to ensure it provides approvals and effective guidance on conservatorship-related issues efficiently. In September 2010, FHFA adopted new reporting protocols formalizing the process and FHFA expects to automate the tracking system in early calendar year 2011.

As a new performance goal, FHFA encountered difficulties in the reporting, tracking, and measurement of these data, particularly in the final half of the year. In particular, numerous issues were reported as awaiting conservator response prematurely. In fact, these items were brought to the attention of FHFA and placed on the tracking system before the Enterprises had completed their own internal development and review work.

Completeness and Reliability of Performance Data

The data for this performance goal were not complete and reliable every quarter, but did become so later in the year. The data are created internally, reported in the agency's performance tracking system, and reviewed by senior management weekly. Data related to supervision activities are collected through FHFA's supervision process and reviewed by quality assurance staff and FHFA management.

PERFORMANCE RESULTS KEY: Goal Fulfillment

- Target Met
- Target Not Met, But Improved Over Last Year
- Target Not Met

Performance GOAL 3.3	*Ensure the Enterprises have effective programs that respond to problems in mortgage markets by reducing preventable foreclosures.*	
PERFORMANCE MEASURE 3.3.1	The Enterprises increase the number of loan modifications to 400,000.	TARGET: September 30, 2010
2010 PERFORMANCE As of August 2010, the Enterprises had increased the number of permanent loan modifications to 465,676.		
PERFORMANCE MEASURE 3.3.2	Less than 35 percent of modifications are 60-plus days delinquent after the modification.	TARGET: September 30, 2010
2010 PERFORMANCE Less than 35 percent of modified loans were 60-plus days delinquent after the modification in three of the past four quarters. In one quarter, the percentage of modified loans 60-plus days delinquent was 35 percent.		

Prior Year Performance – This is a new goal for 2010.

Discussion of Performance Goal 3.3

FHFA set a goal of ensuring that the Enterprises have programs that effectively reduce preventable foreclosures. In March 2009, Treasury announced the *Making Home Affordable* program to decrease mortgage defaults and prevent avoidable foreclosures. The Enterprises have played a vital role in administering the program and monitoring servicer compliance on behalf of the U.S. Department of the Treasury, as well as modifying loans to help at-risk borrowers. Performance measure 3.3.1 sets a target of increasing the number of loan modifications to 400,000. As of August 2010, the Enterprises increased the number of loan modifications to 465,676, exceeding the annual target prior to year-end September 30, 2010.

For FY 2010, FHFA set a target of having less than 35 percent of modified loans 60-plus days delinquent after modification. Less than 35 percent of modified loans were 60-plus days delinquent after the modification in 3 of the 4 quarters in FY 2010. In one quarter, the percentage of modified loans delinquent for 60-plus days was 35 percent.

Completeness and Reliability of Performance Data

The data for this performance goal are complete and reliable. The data are created internally, reported in the agency's performance tracking system, and reviewed by senior management quarterly. Data related to supervision activities are collected through FHFA's supervision process and reviewed by quality assurance staff and FHFA management.

Performance GOAL 3.4	*Work with the Administration and Congress to develop an effective structure for the Enterprises to emerge from conservatorship.*	
PERFORMANCE MEASURE 3.4.1	FHFA will provide technical assistance to Congress and the Administration on various future structures for the secondary mortgage market and for post-conservatorship outcomes for the Enterprises.	TARGET: Ongoing

2010 PERFORMANCE
FHFA has provided technical assistance to the Administration and Congress regarding the secondary mortgage market and post-conservatorship outcomes for the Enterprises through congressional testimony, full participation in the President's Working Group on Financial Markets, and meetings with representatives from Treasury, HUD, the Council of Economic Advisers, and the National Economic Council to explore topics related to Enterprise operations and overall housing policy.

Prior Year Performance – This is a new goal for 2010.

Discussion of Performance Goal 3.4

FHFA's coordination with the Administration and Congress is vital to achieving the most effective and efficient secondary mortgage market. During FY 2010, FHFA cooperated with the Administration and Congress by providing timely and thorough information and assistance. During FY 2010, FHFA continued to participate in the President's Working Group on Financial Markets to develop various strategies for improving the mortgage market. FHFA also hosted meetings with Treasury, U.S. Department of Housing and Urban Development (HUD), the Council of Economic Advisers, the National Economic Council, and the Enterprises to explore various topics on the overall housing market, as well as Enterprise operations. The Acting Director of FHFA testified before several congressional committees during FY 2010.

Completeness and Reliability of Performance Data

The data for this performance goal are complete and reliable. The data are created internally, reported in the agency's performance tracking system, and reviewed by senior management quarterly. Data related to supervision activities are collected through FHFA's supervision process and reviewed by quality assurance staff and FHFA management.

PERFORMANCE RESULTS KEY: Goal Fulfillment

- Target Met
- Target Not Met, But Improved Over Last Year
- Target Not Met

RESOURCE MANAGEMENT STRATEGY

FHFA has the personnel, resources, and infrastructure to manage effectively and efficiently to achieve its mission and goals.

FHFA strives to use all of its resources effectively and efficiently. An effective resource management strategy allows FHFA to focus on achieving its mission and goals. Now in its second full year of operation, FHFA has continued to improve its resource management strategy by developing new personnel policies, improving information technology systems, and enhancing financial systems and functions.

A small but growing agency, FHFA relies on staff and management to accomplish its goals through cross-organizational teams. FHFA managers make decisions on the basis of agency strategic planning, program performance, budget, and operational strategies. FHFA invests in the talents of its staff, relies on effective information technology solutions, and leverages human capital resources and commercial sources, such as contractors, to provide efficient and cost-effective services.

Performance GOAL 4.1

FHFA has a diverse workforce that is highly skilled, highly motivated and results oriented.

PERFORMANCE MEASURE 4.1.1	FHFA fills vacancies within 80 business days.	TARGET: 70% quarterly
2010 PERFORMANCE FHFA filled 11 out of 50, approximately 22 percent, of vacancies within the 80 day time-to-hire standard.		

Prior Year Performance – This is a new goal for 2010.

Discussion of Performance Goal 4.1

FHFA remains committed to recruiting and retaining highly qualified employees to advance the mission and goals of the agency. For FY 2010, FHFA adopted the Office of Personnel Management (OPM)-mandated performance measure of filling vacancies within 80 business days. This was an ambitious target that FHFA did not achieve, like many other agencies. FHFA is currently investigating new automated staffing tools and exploring other ways to increase efficiency.

Completeness and Reliability of Performance Data

The data for this performance goal are complete and reliable. The data are created internally, reported in the agency's performance tracking system, and reviewed by senior management quarterly. Data related to supervision activities are collected through FHFA's supervision process and reviewed by quality assurance staff and FHFA management.

Performance GOAL 4.2	*FHFA demonstrates a strong commitment to equal employment opportunity that supports diversity in employment, operations and the contracting of services.*	
PERFORMANCE MEASURE 4.2.1	Increase the number of qualified disabled, minority, and female job applicants.	TARGET: 5% annually
2010 PERFORMANCE The number of qualified female applicants increased by 3 percent, while the number of minority and disabled qualified applicants each decreased by 1 percent.		

Prior Year Performance – This is a new goal for 2010.

Discussion of Performance Goal 4.2

FHFA recognizes the importance of a highly qualified and diverse workforce. In FY 2010, FHFA participated in several recruitment events to access a diverse pool of applicants with the knowledge, skills, and abilities to perform duties necessary to advance the mission of the agency. Technical competence, skills, experience, and the ability to work in a team environment are crucial to ensuring the successful achievement of FHFA's goals.

For FY 2010, FHFA set a target of increasing the number of qualified disabled, minority, and female applicants to fill various positions at the agency by 5 percent. FHFA did not meet this target. Applicants are not required to report sex, race, or disability status, but may do so voluntarily; therefore, such data are not available for every applicant.

Polly Grago, FHFA Human Capital Manager, addresses staff gathered to acknowledge significant contributions of FHFA's summer 2010 interns.

During FY 2010, FHFA received and processed a total of 4,077 qualified applications, with voluntary self-reporting of 42-percent women, and 49-percent minorities. 67 disabled applicants self-reported. Of the qualified applicants, 9 percent did not self-report. The number of qualified female applicants increased by 3 percent, while the number of minority and disabled qualified applicants each decreased by 1 percent.

Completeness and Reliability of Performance Data

The data for this performance goal are complete and reliable to the extent that applicants voluntarily self-reported. The data are created internally, reported in the agency's performance tracking system, and reviewed by senior management quarterly. Data related to supervision activities are collected through FHFA's supervision process and reviewed by quality assurance staff and FHFA management.

PERFORMANCE RESULTS KEY: Goal Fulfillment

- Target Met
- Target Not Met, But Improved Over Last Year
- Target Not Met

Performance GOAL 4.3	*FHFA has effective financial and risk management programs.*	
PERFORMANCE MEASURE 4.3.1	FHFA's external audits and reviews have unqualified opinions with no material weaknesses or unacceptable risks.	TARGET: 100%
2010 PERFORMANCE In FY 2010, all of FHFA's external audits and reviews had unqualified opinions with no material weaknesses.		
PERFORMANCE MEASURE 4.3.2	FHFA net cost per value of the 14 housing GSEs' total book of business.	TARGET: 0.0025 percent
2010 PERFORMANCE For FY 2010, FHFA's net cost per value of the 14 housing GSEs is 0.0022 percent.		

Prior Year Performance – For FY 2009, FHFA net cost per value of the 14 housing regulated entities' total books of business was 0.0018 percent, and all of FHFA's external audits and reviews had unqualified opinions with no material weaknesses.

Discussion of Performance Goal 4.3

FHFA strives to manage its resources effectively and efficiently. In FY 2010, FHFA expanded its use of financial and performance information in managing program operations.

During the third quarter of FY 2010, FHFA received two reports from GAO on FHFA's FY 2009 Financial Statements. Both reports identified specific issues that would improve FHFA internal controls, and FHFA has addressed those issues. No material weaknesses or significant deficiencies were identified in GAO's reports. In the fourth quarter of FY 2010, FHFA's Office of Internal Audit issued a report on the handling of correspondence. That report did not identify any material weaknesses or unacceptable risks.

In addition, FHFA kept net cost per value of the 14 housing GSEs' total book of business at .0022 percent, which is below the FY 2010 target of .0025 percent.

Completeness and Reliability of Performance Data

The data for this performance goal are complete and reliable. The data are created internally, reported in the agency's performance tracking system, and reviewed by senior management quarterly. Data related to supervision activities are collected through FHFA's supervision process and reviewed by quality assurance staff and FHFA management.

Mark Kinsey, FHFA's Chief Financial Officer, and FHFA Acting Director Edward DeMarco prepare to receive the Association of Government Accountants prestigious Certificate of Excellence in Accountability Reporting (CEAR) Award on behalf of FHFA.

Performance GOAL 4.4	*FHFA has the information technology and physical infrastructure needed to achieve its mission and goals.*	
PERFORMANCE MEASURE 4.4.1	FHFA's infrastructure systems are continuously available for use by FHFA staff.	TARGET: 99% of the time each quarter
2010 PERFORMANCE FHFA system availability exceeded 99 percent each quarter of FY 2010.		
PERFORMANCE MEASURE 4.4.2	FHFA completes its internal review of Examiner Workstation and finalizes a new strategic plan for Examiner Workstation.	TARGET: September 30, 2010
2010 PERFORMANCE FHFA did not finalize a new strategic plan for Examiner Workstation by the target date of September 30, 2010.		

Prior Year Performance – In FY 2009, system availability exceeded 98 percent each quarter of the fiscal year.

Discussion of Performance Goal 4.4

FHFA relies heavily on information technology to effectively supervise and oversee the regulated entities. FHFA continues to improve its information technology processes, applications, and systems.

For each quarter of FY 2010, FHFA maintained continuous availability of infrastructure systems more than 99 percent of the time. FHFA continuously monitored and recorded its network to ensure maximum system availability. FHFA implemented tools to carry out monitoring of environmental controls, network components, file servers, and critical services. These monitors gave system performance alerts so systems staff could address issues expeditiously.

FHFA also set a target of completing an internal review and finalizing a new strategic plan for Examiner Workstation by the end of FY 2010. During the fourth quarter of FY 2010, FHFA completed development of the Information Management System Proof-of-Concept (IMS PoC) to automate the examination process in the Division of Federal Home Loan Bank Regulation (DBR). A short delay in the testing schedule for the IMS PoC affected the delivery of the Examiner Workstation Strategic Plan. Initial testing of the new system began on September 21, 2010 and ended on September 24, 2010. Following initial testing, OTIM and DBR continued refinements of the workflow functionality of the system. The new strategic plan is expected to be completed during the first quarter of 2011.

Completeness and Reliability of Performance Data

The data for this performance goal are complete and reliable. The data are created internally, reported in the agency's performance tracking system and reviewed by senior management.

PERFORMANCE RESULTS KEY: Goal Fulfillment

- Target Met
- Target Not Met, But Improved Over Last Year
- Target Not Met

Financial Section

Message from Chief Financial Officer

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Message from the Chief Financial Officer

Mark Kinsey, Chief Financial Officer
Federal Housing Finance Agency

I am pleased to report that, in its second full year of operations, the Federal Housing Finance Agency (FHFA) once again received an unqualified 'clean' audit opinion on its financial statements from the Government Accountability Office (GAO). In its financial audit report, GAO concluded that 1) FHFA's FY 2010 financial statements are fairly presented in all material respects; 2) FHFA had effective internal control over financial reporting; and 3) there were no reportable instances of noncompliance with the laws and regulations it tested.

In addition to its clean financial audits, FHFA received the Certificate for Excellence in Accountability Reporting (CEAR) award for FY 2009 from the Association of Government Accountants. This is the second straight year FHFA received this prestigious award. The CEAR award is given to government agencies that received unqualified audit opinions on their financial statements and produced Performance and Accountability Reports (PARs) that achieved the highest standards in communicating results and demonstrating accountability.

These impressive accomplishments could not have been achieved with out the commitment from management and staff to maintain effective programs of internal control over important agency activities. FHFA's Executive Committee on Internal Controls works to establish a strong control environment for the agency and meets at least quarterly to monitor and evaluate the effectiveness of the agency's internal control programs.

As always, I am very proud to work with a highly dedicated group of professionals whose efforts contributed significantly to these accomplishments.

Sincerely,

Mark Kinsey
Chief Financial Officer
November 10, 2010

G A O
Accountability * Integrity * Reliability

United States Government Accountability Office
Washington, D.C. 20548

To the Acting Director of the Federal Housing Finance Agency

In accordance with the Housing and Economic Recovery Act of 2008 (HERA), we are responsible for conducting audits of the financial statements of the Federal Housing Finance Agency (FHFA). In our audits of FHFA's fiscal years 2010 and 2009 financial statements, we found

- the financial statements are presented fairly, in all material respects, in conformity with U.S. generally accepted accounting principles,
- FHFA maintained, in all material respects, effective internal control over financial reporting as of September 30, 2010, and
- no reportable noncompliance with laws and regulations we tested.

The following sections discuss in more detail (1) these conclusions; (2) our conclusions on FHFA's Management's Discussion and Analysis; (3) our audit objectives, scope, and methodology; and (4) agency comments and our evaluation.

Opinion on Financial Statements

FHFA's financial statements, including the accompanying notes, present fairly, in all material respects, in conformity with U.S. generally accepted accounting principles, its assets, liabilities, and net position as of September 30, 2010 and 2009; and its net costs, changes in net position, and budgetary resources for the fiscal years then ended.

Because fiscal year 2009 was the first full year of FHFA's operations, fiscal year 2010 is the first year in which FHFA prepared comparative financial statements. As discussed in note 10, the statement of net cost presents costs as one program for fiscal year 2009. For fiscal year 2010, consistent with its new strategic plan, FHFA tracked and reported resource allocations and costs by strategic goal (responsibility segment). Consequently, the fiscal year 2010 statement of net cost presents FHFA's costs by strategic goal.

As discussed in note 1A of the financial statements, FHFA's fiscal years 2010 and 2009 financial statements do not include the assets, liabilities, and activities associated with Fannie Mae and Freddie Mac. In early September 2008, less than 2 months after FHFA's establishment, the then-Director of FHFA placed Fannie Mae and Freddie Mac into conservatorship under the authority of the Federal Housing Enterprises Financial Safety and

Soundness Act of 1992, as amended by HERA. FHFA's goal in placing the two entities into conservatorship was to stabilize them with the objective of maintaining normal business operations and restoring safety and soundness. As of September 30, 2010, about $148.2 billion in direct financial support from Treasury has been provided to Fannie Mae and Freddie Mac. Shortly after Fannie Mae and Freddie Mac were placed in conservatorship, OMB and Treasury determined that the assets, liabilities, and activities of these entities would not be included in the financial statements of the federal government or those of the Treasury, although Treasury records an asset for its investment in Fannie Mae and Freddie Mac and a liability for future payments to the two entities in its financial statements. In making this determination, OMB and Treasury reviewed the criteria contained in Statement of Federal Financial Accounting Concepts No. 2, *Entity and Display*. They concluded that because the entities were not listed in the section of the federal government's budget, entitled "Federal Programs by Agency and Account," and because the nature of the conservatorships and the federal government's ownership and control of the entities were considered to be temporary, the entities did not meet the conclusive or indicative criteria in Concept Statement No. 2 for consolidation. OMB and Treasury reaffirmed this conclusion with respect to both fiscal years 2009 and 2010. FHFA management concurred with this conclusion. Consequently, FHFA did not consolidate Fannie Mae and Freddie Mac into its fiscal years 2010 and 2009 financial statements. Should circumstances change, such as the inclusion of Fannie Mae and Freddie Mac in the federal budget or a determination that the current degree of federal control and ownership of the entities is other than temporary, this decision would need to be revisited.

Opinion on Internal Control

FHFA maintained, in all material respects, effective internal control over financial reporting as of September 30, 2010, which provided reasonable assurance that misstatements, losses, or noncompliance material in relation to the financial statements would be prevented or detected and corrected on a timely basis. Our opinion is based on criteria established under 31 U.S.C. § 3512 (c), (d), commonly known as the Federal Managers' Financial Integrity Act of 1982 (FMFIA).

During our audit of FHFA's fiscal year 2009 financial statements, we identified certain deficiencies in FHFA's system of internal control that we did not consider to be material weaknesses or significant deficiencies.[1] These deficiencies involved matters related to certain accounting and monitoring procedures, access controls, and information security management. FHFA has made progress in addressing these deficiencies during fiscal year 2010. However, not all actions were completed as of the completion of our fiscal year 2010 audit. During our fiscal year 2010 audit, we also identified additional deficiencies in accounting procedures. We do not consider the deficiencies found during our fiscal year 2009 and 2010 audits, individually or in the aggregate, to be material weaknesses or significant deficiencies. We have communicated these matters to management and, where appropriate, will report on them separately.

Compliance with Laws and Regulations

Our tests of FHFA's compliance with selected provisions of laws and regulations for fiscal year 2010 disclosed no instances of noncompliance that would be reportable under U.S. generally accepted government auditing standards. The objective of our audit was not to provide an opinion on overall compliance with laws and regulations. Accordingly, we do not express such an opinion.

Consistency of Other Information

FHFA's Management's Discussion and Analysis and other accompanying information contain a wide range of information, some of which is not directly related to the financial statements. We did not audit and we do not express an opinion on this information. However, we compared this information for consistency with the financial statements and discussed the methods of measurement and presentation with FHFA officials. On the basis of this limited work, we found no material inconsistencies with the financial statements, with U.S. generally accepted accounting principles, or with OMB Circular No. A-136, *Financial Reporting Requirements*.

[1] A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented or detected and corrected on a timely basis. A significant deficiency is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis.

Objectives, Scope, and Methodology

FHFA management is responsible for (1) preparing the financial statements in conformity with U.S. generally accepted accounting principles, (2) establishing and maintaining effective internal control over financial reporting and evaluating its effectiveness, and (3) complying with applicable laws and regulations. FHFA management evaluated the effectiveness of FHFA's internal control over financial reporting as of September 30, 2010, based on the criteria established under FMFIA. FHFA management's assertion based on its evaluation is included in appendix I.

We are responsible for planning and performing the audit to obtain reasonable assurance and provide our opinion about whether (1) FHFA's financial statements are presented fairly, in all material respects, in conformity with U.S. generally accepted accounting principles, and (2) FHFA management maintained, in all material respects, effective internal control over financial reporting as of September 30, 2010. We are also responsible for (1) testing compliance with selected provisions of laws and regulations that have a direct and material effect on the financial statements, and (2) performing limited procedures with respect to certain other information accompanying the financial statements.

In order to fulfill these responsibilities, we

- examined, on a test basis, evidence supporting the amounts and disclosures in the financial statements;
- assessed the accounting principles used and significant estimates made by management;
- evaluated the overall presentation of the financial statements;
- obtained an understanding of the entity and its operations, including its internal control over financial reporting;
- considered FHFA's process for evaluating and reporting on internal control over financial reporting that FHFA is required to perform by FMFIA;
- assessed the risk that a material misstatement exists in the financial statements and the risk that a material weakness exists in internal control over financial reporting;

- evaluated the design and operating effectiveness of internal control over financial reporting based on the assessed risk;

- tested relevant internal control over financial reporting;

- tested compliance with selected provisions of the following laws and their related regulations: 31 U.S.C. § 3902 (a), (b), (f)—Interest penalties under the Prompt Payment Act; 31 U.S.C. § 3904—Limitations on Discount Payments Under the Prompt Payment Act; 12 U.S.C. § 4515—Personnel; Federal Employees' Retirement System Act of 1986, as amended; Social Security Act of 1935, as amended; Federal Employees Health Benefits Act of 1959, as amended; 12 U.S.C. § 4516 (g)(4), which makes applicable 31 U.S.C. § 3512 (c), Federal Managers' Financial Integrity Act of 1982; and Federal Housing Enterprises Financial Safety and Soundness Act of 1992, as amended by the Housing and Economic Recovery Act of 2008; and

- performed such other procedures as we considered necessary in the circumstances.

An entity's internal control over financial reporting is a process affected by those charged with governance, management, and other personnel, the objectives of which are to provide reasonable assurance that (1) transactions are properly recorded, processed, and summarized to permit the preparation of financial statements in conformity with U.S. generally accepted accounting principles, and assets are safeguarded against loss from unauthorized acquisition, use, or disposition; and (2) transactions are executed in accordance with the laws governing the use of budget authority and other laws and regulations that could have a direct and material effect on the financial statements.

We did not evaluate all internal controls relevant to operating objectives as broadly established under FMFIA, such as those controls relevant to preparing statistical reports and ensuring efficient operations. We limited our internal control testing to testing controls over financial reporting. Our internal control testing was for the purpose of expressing an opinion on the effectiveness of internal control over financial reporting and may not be sufficient for other purposes. Consequently, our audit may not identify all deficiencies in internal control over financial reporting that are less severe than a material weakness. Because of inherent limitations, internal control may not prevent or detect and correct misstatements due to error or fraud, losses, or noncompliance. We also caution that projecting any evaluation of effectiveness to future periods is subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

We did not test compliance with all laws and regulations applicable to FHFA. We limited our tests of compliance to selected provisions of laws and regulations that have a direct and material effect on the financial statements for the fiscal year ended September 30, 2010. We caution that noncompliance may occur and not be detected by these tests and that such testing may not be sufficient for other purposes.

We performed our audit in accordance with U.S. generally accepted government auditing standards. We believe our audit provides a reasonable basis for our opinions and other conclusions.

Agency Comments and Our Evaluation

In commenting on a draft of this report, FHFA stated that it was pleased that the audit found that its fiscal year 2010 and 2009 financial statements were presented fairly, that it maintained effective internal control over financial reporting, and that there had been no instances of reportable noncompliance with laws and regulations we tested. FHFA noted that it would continue to work to enhance its internal controls and ensure the reliability of its financial reporting, its soundness of operations, and public confidence in its mission.

The complete text of FHFA's response is reprinted in appendix II.

Steven J. Sebastian
Director
Financial Management and Assurance

November 9, 2010

FEDERAL HOUSING FINANCE AGENCY

Balance Sheet

As of September 30, 2010 and 2009
(In Thousands)

	2010	2009
Assets:		
Intragovernmental		
Fund Balance With Treasury (Note 2)	$ 1,000	$ 29,076
Investments (Note 3)	50,878	37,668
Accounts Receivable (Note 4)	-	3
Prepaid Expenses	307	-
Total Intragovernmental	**52,185**	**66,747**
Accounts Receivable (Note 4)	6	3
Property, Equipment, and Software, Net (Note 5)	2,397	3,273
Prepaid Expenses	873	1
Total Assets	**$ 55,461**	**$ 70,024**
Liabilities:		
Intragovernmental		
Accounts Payable	$ 430	$ 758
Payroll Taxes Payable (Note 7)	799	652
Total Intragovernmental	**1,229**	**1,410**
Accounts Payable	4,358	4,268
Deferred Revenue (Note 6)	-	35,122
Other (Note 7)	12,018	10,813
Total Liabilities	**$ 17,605**	**$ 51,613**
Net Position:		
Cumulative Results of Operations	$ 37,856	$ 18,411
Total Net Position	$ 37,856	$ 18,411
Total Liabilities and Net Position	**$ 55,461**	**$ 70,024**

The accompanying notes are an integral part of these financial statements.

FEDERAL HOUSING FINANCE AGENCY

Statement of Net Cost

For the Fiscal Years Ended September 30, 2010 and 2009
(In Thousands)

	2010	2009
Program Costs by Strategic Goal: (Note 10)		
Safety and Soundness:		
Gross Costs	$ 95,870	$ -
Less: Earned Revenue	(89,272)	-
Net Safety and Soundness Costs/(Income)	**$ 6,598**	**$ -**
Affordable Housing:		
Gross Costs	$ 16,031	-
Less: Earned Revenue	(26,819)	-
Net Affordable Housing Costs/(Income)	**$ (10,788)**	**$ -**
Conservatorship:		
Gross Costs	$ 16,663	$ -
Less: Earned Revenue	(27,111)	-
Net Conservatorship Costs/(Income)	**$ (10,448)**	**$ -**
Total Gross Program Costs	$ 128,564	$ 122,816
Less: Total Earned Revenue	(143,202)	(115,709)
Net (Income from)/Cost of Operations	**$ (14,638)**	**$ 7,107**

The accompanying notes are an integral part of these financial statements.

FEDERAL HOUSING FINANCE AGENCY

Statement of Changes in Net Position

For the Fiscal Years Ended September 30, 2010 and 2009
(In Thousands)

	2010	2009
Cumulative Results of Operations:		
Beginning Balances	$ 18,411	$ 9,544
Budgetary Financing Sources:		
Appropriations Used	-	12,896
Other Financing Sources (Non-Exchange):		
Imputed Financing Sources	4,807	3,078
Total Financing Sources	4,807	15,974
Net Income From/(Cost of) Operations	14,638	(7,107)
Net Change	19,445	8,867
Cumulative Results of Operations	$ 37,856	$ 18,411
Unexpended Appropriations:		
Beginning Balances	$ -	$ 12,896
Budgetary Financing Sources:		
Appropriations Used	-	(12,896)
Total Budgetary Financing Sources	-	(12,896)
Total Unexpended Appropriations	$ -	$ -
Net Position	**$ 37,856**	**$ 18,411**

The accompanying notes are an integral part of these financial statements.

FEDERAL HOUSING FINANCE AGENCY

Statement of Budgetary Resources

For the Fiscal Years Ended September 30, 2010 and 2009
(In Thousands)

	2010	2009
Budgetary Resources:		
Unobligated Balance:		
Unobligated Balance, Brought Forward, October 1	$ 9,657	$ 5,132
Recoveries of Prior Year Unpaid Obligations	2,693	6,002
Budget Authority		
Appropriation - Assessments	143,028	115,669
Appropriation - Investment Interest	72	30
Spending Authority From Offsetting Collections		
Earned		
Collected	104	4,572
Change In Receivables From Federal Sources	(3)	(1,459)
Change In Unfilled Customer Orders		
Without Advance From Federal Sources	-	(4,038)
Subtotal	143,201	114,774
Total Budgetary Resources	**$ 155,551**	**$ 125,908**
Status of Budgetary Resources:		
Obligations Incurred (Note 11)		
Direct	$ 132,707	$ 111,682
Reimbursable	101	4,569
Subtotal	132,808	116,251
Unobligated Balance		
Exempt From Apportionment	22,743	9,657
Total Status of Budgetary Resources	**$ 155,551**	**$ 125,908**
Change in Obligated Balance:		
Obligated Balance, Net		
Unpaid Obligations, Brought Forward, October 1	$ 21,968	$ 29,146
Uncollected Customer Payments From		
Federal Sources, Brought Forward, October 1	(3)	(5,500)
Total Unpaid Obligated Balance, Net	**21,965**	**23,646**
Obligations Incurred Net	132,808	116,251
Gross Outlays	(122,948)	(117,427)
Recoveries of Prior Year Unpaid		
Obligations, Actual	(2,693)	(6,002)
Change In Uncollected Customer Payments		
From Federal Sources	3	5,497
Obligated Balance, Net, End of Period		
Unpaid Obligations	29,135	21,968
Uncollected Customer Payments From		
Federal Sources	-	(3)
Total Unpaid Obligated Balance, Net, End of Period	**$ 29,135**	**$ 21,965**
Net Outlays:		
Gross Outlays	$ 122,948	$ 117,427
Offsetting Collections	(104)	(4,572)
Distributed Offsetting Receipts	(143,100)	(115,699)
Net Outlays	**$ (20,256)**	**$ (2,844)**

The accompanying notes are an integral part of these financial statements.

FEDERAL HOUSING FINANCE AGENCY

Notes to the Financial Statements

for the Years Ended September 30, 2010 and 2009

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Reporting Entity

The Federal Housing Finance Agency (FHFA) was established on July 30, 2008, when the President signed into law the Housing and Economic Recovery Act of 2008 (HERA). FHFA is an independent agency in the Executive branch empowered with supervisory and regulatory oversight of the twelve Federal Home Loan Banks (FHLBanks), Federal National Mortgage Association (Fannie Mae), and Federal Home Loan Mortgage Corporation (Freddie Mac), all of which are referred to as regulated entities within this document. FHFA is responsible for ensuring that each regulated entity operates in a safe and sound manner, including maintenance of adequate capital and internal controls, and carries out their housing and community development finance missions.

HERA abolished the Federal Housing Finance Board (FHFB) and Office of Federal Housing Enterprise Oversight (OFHEO) effective at the end of the 1-year period beginning on July 30, 2008. FHFB and OFHEO existed until then solely for the purpose of winding up their affairs. During fiscal year 2009, in accordance with HERA, the transfer of personnel, property, and program activities of FHFB, OFHEO, and certain employees and activities of the Department of Housing and Urban Development related to the regulation of the mission of Fannie Mae and Freddie Mac were made to FHFA.

Under the authority of the Federal Housing Enterprises Financial Safety and Soundness Act of 1992, as amended by HERA, FHFA placed Fannie Mae and Freddie Mac under conservatorship on September 6, 2008, to stabilize the two entities with the objective of maintaining normal business operations and restoring safety and soundness. FHFA, as conservator, assumed the power of stockholders, boards, and management. FHFA delegated to Fannie Mae and Freddie Mac certain business and operational authority. FHFA personnel monitor the operations of the enterprises.

In September 2008, after Fannie Mae and Freddie Mac were placed in conservatorship under the FHFA, the Office of Management and Budget (OMB) determined that the assets, liabilities and activities of the companies would not be included in the financial statements of the federal government. For fiscal year 2008, OMB and the Department of the Treasury (Treasury) concluded that Fannie Mae and Freddie Mac did not meet the conclusive or indicative criteria for a federal entity contained in OMB Circular A-136 and Statement of Federal Financial Accounting Concepts No. 2, *Entity and Display* because they are not listed in the section of the federal government's budget entitled "Federal Programs by Agency and Account," and because the nature of FHFA's conservatorships over Fannie Mae and Freddie Mac and the federal government's ownership and control of the entities is considered to be temporary. Treasury reaffirmed this position for fiscal year 2009, with which FHFA concurs. OMB continued to hold this view in the President's fiscal year 2010 and fiscal year 2011 budget submissions to Congress. Consequently, the assets, liabilities, and activities of Fannie Mae and Freddie Mac have not been consolidated into FHFA's financial statements. However, Treasury records the value of the federal government's investments in Fannie Mae and Freddie Mac in its financial statements as a General Fund asset.

Both Fannie Mae and Freddie Mac, as represented by FHFA as their Conservator, entered into separate agreements with Treasury known as the Senior Preferred Stock Purchase Agreements (Agreements) on September 7, 2008. These two Agreements are identical and have since been amended three times, on September 26, 2008, May 6, 2009 and December 24, 2009. The Agreements commit Treasury to provide funding for each Enterprise up to the greater of: (1) $200 billion; or (2) $200 billion plus the cumulative total of draws for each calendar quarter in 2010, 2011 and 2012 minus any amount by which the assets of the Enterprise exceed its liabilities on December 31, 2012. This funding is to ensure that each Enterprise maintains a non-negative net worth, thereby avoiding a statutory requirement that an Enterprise be put in receivership following an extended period of negative net worth. Under the Agreements, each Enterprise submits a request for any needed draw amount once their financials (to be published in their 10-K or 10-Q) are finalized. The Enterprise also submits a statement certifying compliance with Agreement covenants, which include limits on portfolio size and indebtedness. FHFA, in its role as Conservator, reviews any request for a draw and certifies that the request is available for funding under the agreement. FHFA then sends a letter to Treasury requesting the draw amount prior to the end of the current quarter. FHFA as Conservator also issues an order to the Enterprises each quarter requiring each Enterprise to pay dividends to Treasury as required by the Agreements. Additionally, the Agreements require each Enterprise to obtain Treasury approval for the disposition of assets, except under certain circumstances. FHFA as Conservator reviews these requests. Fannie Mae and Freddie Mac draws on their Agreements with Treasury are summarized below. Such draws are reported in Treasury's financial statements.

Enterprise Draws on Treasury Agreements
(Dollars in Billions)

Draw Dates	Fannie Mae	Freddie Mac
September 30, 2008	$ -	$ 13.8
December 31, 2008	15.2	30.8
March 31, 2009	19.0	6.1
June 30, 2009	10.7	-
September 30, 2009	15.0	-
December 31, 2009	15.3	-
March 31, 2010	8.4	10.6
June 30, 2010	1.5	1.8
Cumulative Draws	$ 85.1	$ 63.1

B. Basis of Presentation

FHFA's principal statements were prepared from its official financial records and general ledger in conformity with accounting principles generally accepted in the United States and follow the presentation guidance established by OMB Circular A-136 "Financial Reporting Requirements," revised September 29, 2010. The statements are a requirement of the Government Management Reform Act of 1994, the Accountability of Tax Dollars Act of 2002, and HERA. These financial statements are in addition to the financial reports prepared by FHFA, pursuant to OMB directives, which are used to monitor and control budgetary resources. As required by HERA, the financial statements of FHFA are audited by the U.S. Government Accountability Office (GAO). The financial statements have been prepared to report the financial position, net cost of operations, changes in net position, and the status and availability of budgetary resources of FHFA. Unless specified otherwise, all amounts are presented in thousands.

C. Basis of Accounting

Transactions are recorded on both an accrual accounting basis, and a budgetary basis. Under the accrual basis of accounting, revenues are recognized when earned, and expenses are recognized when a liability is incurred, without regard to receipt or payment of cash. Budgetary accounting facilitates compliance with legal requirements and controls over the use of federal funds. FHFA conforms to accounting principles generally accepted in the United States for federal entities as prescribed by the standards set forth by the Federal Accounting Standards Advisory Board (FASAB). FASAB is recognized by the American Institute of Certified Public Accountants as the body designated to establish generally accepted accounting principles for federal entities. Certain assets, liabilities, earned revenues, and costs have been classified as intragovernmental throughout the financial statements and notes. Intragovernmental is defined as exchange transactions made between two reporting entities within the federal government.

D. Revenues, Imputed & Other Financing Sources

Operating revenues of FHFA are obtained through assessments of the regulated entities. The agency's acting Director, in September 2009, approved the annual budget. By law, FHFA is required to charge semi-annual assessments to the entities. Assessments collected shall not exceed the amount sufficient to provide for the reasonable costs associated with overseeing the entities, plus amounts determined by the acting Director to be necessary for maintaining a working capital fund.

FHFA develops its annual budget using a 'bottom up' approach. Each office within the agency is asked to bifurcate their budget request between the amount of resources needed for the regulation of Fannie Mae and Freddie Mac and the resources needed for the regulation of the twelve FHLBanks. The office requests are then aggregated (with overhead costs distributed proportionately) to determine the total expected costs associated with regulating Fannie Mae and Freddie Mac and the total expected costs associated with regulating the FHLBanks. These two totals, along with any expected collection for the working capital fund, comprise the fiscal year budget for the agency. Additionally, FHFA levied a special assessment for conservatorship activities on Fannie Mae and Freddie Mac during fiscal year 2010.

Fannie Mae and Freddie Mac pay a pro rata share of their portion of the total assessment based on the combined assets and off-balance sheet obligations of each enterprise. Each FHLBank's share of their portion of the total assessment is based on the dollar value of its capital stock relative to the combined dollar value of all FHLBanks' capital stock. Assessment letters are sent to the entities 30 days prior to the assessment due dates of October 1st and April 1st. Assessments received prior to due dates are available for investment but are unavailable for obligation. These assessments are recorded as deferred revenue.

Federal government entities often receive goods and services from other federal government entities without reimbursing the providing entity for all the related costs. In addition, federal government entities also incur costs that are paid in total or in part by other entities. An imputed financing source is recognized by the receiving entity for costs that are paid by other entities. FHFA recognized imputed costs and financing sources in fiscal years 2010 and 2009 as prescribed by accounting standards. FHFA recognizes as an imputed financing source the amount of pension and post-retirement benefit expenses for current employees accrued on FHFA's behalf by the Office of Personnel Management (OPM).

E. Use of Estimates

The preparation of the accompanying financial statements in accordance with U.S. generally accepted accounting principles requires management to make certain estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, and expenses. Actual results could differ from those estimates.

F. Earmarked Funds

FASAB's Statement of Federal Financial Accounting Standards (SFFAS) No. 27 "Identifying and Reporting Earmarked Funds" established certain disclosure requirements for funds defined as "earmarked." SFFAS No. 27 states that "(e)armarked funds are financed by specifically identified revenues, often supplemented by other financing sources, which remain available over time. These specifically identified revenues and other financing sources are required by statute to be used for designated activities, benefits or purposes and must be accounted for separately from the Government's general revenues." The standard also presents three required criteria for an earmarked fund. Based on the standard's criteria, FHFA determined that it has no earmarked funds.

G. Fund Balance with Treasury

The U.S. Treasury (Treasury) processes cash receipts and disbursements on FHFA's behalf. Funds held at the Treasury are available to pay agency liabilities and finance authorized purchase obligations. FHFA does not maintain cash in commercial bank accounts or foreign currency balances.

During the year, increases to FHFA's Fund Balance with Treasury are comprised of semi-annual assessments, investment interest, collections on reimbursable agreements, civil penalty monies, and Freedom of Information Act (FOIA) request fees. FHFA is not authorized to retain civil penalty monies or FOIA fees, and as such, records these as custodial liabilities (See Note 15. Incidental Custodial Collections).

HERA provides authority for FHFA to maintain a working capital fund. The working capital fund is defined in FHFA's Assessment Regulation as an account for amounts collected from the regulated entities to establish an operating reserve that is intended to provide for the payment of large or multiyear capital and operating expenditures, as well as unanticipated expenses. The balance in the working capital fund will be evaluated annually.

H. Investments

FHFA has the authority to invest in U.S. Treasury securities with maturities suitable to FHFA's needs. FHFA invests solely in U.S. Treasury securities, which are normally held to maturity and carried at cost. Investments are adjusted for unamortized premiums or discounts. Premiums and discounts are amortized and interest is accrued using the level-yield, scientific method of effective interest amortization over the term of the respective issues.

I. Accounts Receivable

Accounts receivable consists of amounts owed to FHFA by other federal agencies and the public. Amounts due from federal agencies are considered fully collectible and consist of interagency agreements. Accounts receivable from the public include reimbursements from employees, civil penalty assessments and FOIA request fees. An allowance for uncollectible accounts receivable from the public is established when either (1) management determines that collection is unlikely to occur after a review of outstanding accounts and the failure of all collection efforts, or (2) an account for which no allowance has been established is submitted to the Department of the Treasury for collection, which takes place when it becomes 180 days delinquent. Historical experience has indicated that the majority of the receivables are collectible.

J. Property, Equipment, and Software, Net

Property, Equipment, and Software is recorded at historical cost. It consists of tangible assets and software. Under FHFA's property management policy, equipment acquisitions of $25 thousand or more are capitalized and depreciated using the straight-line method over the estimated useful life of the asset. Additionally, for bulk purchases of similar items, which individually do not meet the test for capitalization, the acquisition is capitalized and depreciated if the depreciated basis of the bulk purchase is $250 thousand or more. Applicable standard governmental guidelines regulate the disposal and convertibility of agency property and equipment. The useful life classifications for capitalized assets are as follows:

Description	Useful Life (years)
Furniture, Fixtures, and Equipment	3
Automated Filing Storage Systems	15
Internal Use Software	3

A leasehold improvement's useful life is equal to the remaining lease term or the estimated useful life of the improvement, whichever is shorter. FHFA has no real property holdings or stewardship or heritage assets. Other property items, normal repairs and maintenance are charged to expense as incurred.

K. Advances and Prepaid Charges

Advance payments are generally prohibited by law. There are some exceptions, such as reimbursable agreements, subscriptions and payments to contractors and employees. Payments made in advance of the receipt of goods and services are recorded as advances or prepaid charges at the time of prepayment and recognized as expenses when the related goods and services are received.

L. Liabilities

Liabilities represent the amount of funds that are likely to be paid by FHFA as the result of a transaction or event that has already occurred.

FHFA reports its liabilities under two categories, Intragovernmental and With the Public. Intragovernmental liabilities represent funds owed to another government agency. Liabilities With the Public represent funds owed to any entity or person that is not a federal agency, including private sector firms and federal employees. Each of these categories may include liabilities that are covered by budgetary resources and liabilities not covered by budgetary resources.

Liabilities covered by budgetary resources are liabilities funded by a current appropriation or other funding source. These consist of accounts payable and accrued payroll and benefits. Accounts payable represent amounts owed to another entity for goods ordered and received and for services rendered except for employees. Accrued payroll and benefits represent payroll costs earned by employees during the fiscal year which are not paid until the next fiscal year.

Liabilities not covered by budgetary resources are liabilities that are not funded by any current appropriation or other funding source. These liabilities consist of accrued annual leave, deferred rent, and the amounts due to Treasury for collection and accounts receivable of civil penalties and FOIA request fees. Annual leave is earned throughout the fiscal year and is paid when leave is taken by the employee; the accrued liability for annual leave represents the balance earned but not yet taken. The Department of Labor (DOL) is the central paying agent for all workman compensation claims filed under the Federal Employees Compensation Act (FECA). Accrued FECA represents the amount FHFA is to reimburse DOL for claims paid to FHFA employees. No liability is recorded for future workman compensation as of September 30, 2010 and 2009, as FHFA's methodology for estimating the future workman compensation as prescribed by DOL determined that the liability would be negligible. Deferred rent is the difference at year-end between the sum of monthly cash disbursements paid to date for rent and the sum of the average monthly rent calculated based on the term of the lease. This determination and recording of deferred rent is applicable only to the lease agreement on the property at 1750 Pennsylvania Avenue that commenced in 2005 (See Note 8. Leases).

M. Employee Leave and Benefits

FHFA employees are entitled to accrue annual leave and sick leave at a rate based on years of federal service. For most employees, annual leave may be accrued up to 240 hours each year. The FHFA executive employees equivalent to the Senior Executive Service (SES) employees may accrue annual leave consistent with the rules for SES level employees. Accrued annual leave is treated as an unfunded expense with an offsetting liability when earned. The accrued liability is reduced when the annual leave is taken. Any unused annual leave balance is paid to the employee upon leaving federal service, based on the employee's earnings per hour. There is no maximum limit on the amount of sick leave that may be accrued. Upon separation, any unused sick leave of Civil Service Retirement System (CSRS) plan employees is creditable as additional time in service for the purpose of calculating an employee's retirement annuity. Credit is given for sick leave balances in the computation of annuities upon the retirement of Federal Employees Retirement System (FERS)-covered employees effective at 50% beginning in fiscal year 2010 and 100% beginning in fiscal year 2014.

Health Benefits and Life Insurance: FHFA, through programs established for all agencies by the federal government, offers its employees health and life insurance coverage through the Federal Employees Health Benefits Program and Federal Employees Group Life Insurance Program. The cost of each is shared by FHFA and its employees. In addition, all employees have 1.45% of gross earnings withheld to pay for future Medicare coverage.

N. Retirement Plans

FHFA employees participate in the retirement plans offered by OPM, which consist of CSRS, CSRS – Offset, or FERS. The employees who participate in CSRS are beneficiaries of FHFA's contribution, equal to 7% of pay, distributed to the employee's annuity account in the Civil Service Retirement and Disability Fund. Prior to December 31, 1983, all employees were covered under the CSRS program. From January 1, 1984 through December 31, 1986, employees had the option of remaining under CSRS or joining FERS and Social Security. Employees hired as of January 1, 1987 are automatically covered by the FERS program. Both CSRS and FERS employees may participate in the federal Thrift Savings Plan (TSP). FERS employees receive an automatic Agency contribution equal to 1% of pay and FHFA matches any employee contribution up to an additional 4% of pay. For FERS participants, FHFA also contributes the employer's matching share of Social Security.

FERS employees and CSRS – Offset employees are eligible to participate in the Social Security program after retirement. In these instances, FHFA remits the employer's share of the required contribution, which is 11.2% for FERS and 7% for CSRS.

FHFA expenses its contributions to the retirement plans of covered employees as the expenses are incurred. FHFA reports imputed (unfunded) costs with respect to retirement plans, health benefits and life insurance pursuant to guidance received from OPM. These costs are paid by OPM and not by FHFA. Disclosure is intended to provide information regarding the full cost of FHFA's program in conformity with generally accepted accounting principles.

FHFA does not report on its financial statements information pertaining to the retirement plans covering its employees. Reporting amounts such as plan assets, accumulated plan benefits, and related unfunded liabilities, if any, is the responsibility of OPM as the administrator.

In addition to the TSP, FHFA offers a supplemental 401(K) plan that is administered by T. Rowe Price. All CSRS employees are eligible to contribute to the 401(K). Only FERS employees contributing at least 3% to the TSP are eligible to participate in the 401(K). All eligible employees that participate may contribute up to 10% of their bi-weekly salary on a pre-tax basis while FHFA will match contributions up to 3% of the employee's salary. Qualified employees may participate in the TSP and/or FHFA's 401(K) Savings Plan, up to the Internal Revenue Code limitations established for salary deferral and annual additions.

O. Contingencies

Liabilities are deemed contingent when the existence or amount of the liability cannot be determined with certainty pending the outcome of future events. FHFA recognizes contingent liabilities, in the accompanying balance sheet and statement of net cost, when they are both probable and can be reasonably estimated. FHFA discloses contingent liabilities in the notes to the financial statements when a loss from the outcome of future events is more than remote but less than probable or when the liability is probable but cannot be reasonably estimated.

NOTE 2. FUND BALANCE WITH TREASURY

Fund Balance with Treasury consists of an Operating Fund and a Working Capital Fund. FHFA did not use the funds in the Working Capital Fund during fiscal years 2010 or 2009. In fiscal year 2010, the funds in the Working Capital Fund were fully invested. Fund Balance with Treasury (FBWT) account balances as of September 30, 2010 and 2009 were as follows:

(Dollars in Thousands)	2010	2009
Fund Balances:		
Operating Fund	$ 1,000	$ 26,076
Working Capital Fund	-	3,000
Total	**$ 1,000**	**$ 29,076**
Status of Fund Balance with Treasury:		
Unobligated Balance		
Available	$ 22,743	$ 9,657
Unavailable (See Note 6. Deferred Revenue)	-	35,122
Total Unobligated Balance	22,743	44,779
Obligated Balance Not Yet Disbursed	29,135	21,968
Investments	(50,878)	(37,668)
Uncollected Customer Payment Earned	-	(3)
Total	**$ 1,000**	**$ 29,076**

(See Note 12. Legal Arrangements Affecting Use of Unobligated Balances)

NOTE 3. INVESTMENTS

Investments as of September 30, 2010 consist of the following:

(Dollars in Thousands)	Cost	Amortized (Premium) Discount	Interest Receivable	Investments Net	Market Value Disclosure
Intragovernmental Securities:					
Non-Marketable Market-Based	$ 50,878	$ -	$ -	$ 50,878	$ 50,878

Investments as of September 30, 2009 consist of the following:

(Dollars in Thousands)	Cost	Amortized (Premium) Discount	Interest Receivable	Investments Net	Market Value Disclosure
Intragovernmental Securities:					
Non-Marketable Market-Based	$ 37,668	$ -	$ -	$ 37,668	$ 37,668

Non-marketable, market-based securities are Treasury notes and bills issued to governmental accounts that are not traded on any securities exchange, but mirror the prices of marketable securities with similar terms. FHFA is currently investing in one-day certificates issued by the U.S. Treasury. There were no amortized premiums/discounts or interest receivable on investments as of September 30, 2010 or 2009. Interest earned on investments was $72 thousand and $30 thousand for fiscal years 2010 and 2009, respectively.

NOTE 4. ACCOUNTS RECEIVABLE

Accounts Receivable balances as of September 30, 2010 and 2009 were as follows:

(Dollars in Thousands)	2010	2009
Intragovernmental		
Accounts Receivable	$ -	$ 3
With the Public		
Accounts Receivable	6	3
Total Accounts Receivable	**$ 6**	**$ 6**

There are no amounts that are deemed uncollectible as of September 30, 2010 and 2009.

NOTE 5. PROPERTY, EQUIPMENT, AND SOFTWARE, NET

Schedule of Property, Equipment, and Software as of September 30, 2010 *(Dollars in Thousands)*

Major Class	Acquisition Cost	Accumulated Amortization/Depreciation	Net Book Value
Equipment	$ 10,844	$ 9,975	$ 869
Leasehold Improvements	6,940	6,674	266
Capital Lease	22	22	-
Internal-Use Software	29,267	28,521	746
Internal-Use Software-in-Development	370	-	370
Construction-in-Progress	146	-	146
Total	**$ 47,589**	**$ 45,192**	**$ 2,397**

Schedule of Property, Equipment, and Software as of September 30, 2009 *(Dollars in Thousands)*

Major Class	Acquisition Cost	Accumulated Amortization/Depreciation	Net Book Value
Equipment	$ 10,303	$ 9,526	$ 777
Leasehold Improvements	6,881	6,270	611
Capital Lease	22	22	-
Internal-Use Software	29,093	27,280	1,813
Internal-Use Software-in-Development	61	-	61
Construction-in-Progress	11	-	11
Total	**$ 46,371**	**$ 43,098**	**$ 3,273**

NOTE 6. DEFERRED REVENUE

Deferred revenue for fiscal 2009 consists of $35.1 million and is classified as with the public for assessments received from the regulated entities prior to the due date of October 1st. These assessments are available for investment but unavailable for obligation. (See Note 2. Fund Balance With Treasury)

NOTE 7. OTHER LIABILITIES

The other liabilities for FHFA are comprised of payroll accruals, deferred lease liability and unfunded leave. Payroll accruals represent payroll expenses that were incurred prior to year-end but were not paid. Other liabilities not covered by budgetary resources consist of unfunded annual leave, compensatory time, and deferred lease liability.

As of September 30, 2010 and 2009 other liabilities not covered by budgetary resources were $7.9 million and $7.4 million, respectively. FHFA's other liabilities are classified as current.

(Dollars in Thousands)	2010	2009
Intragovernmental Liabilities		
Payroll Taxes Payable	$ 799	$ 652
Total Intragovernmental Liabilities	**$ 799**	**$ 652**
With the Public		
Accrued Funded Payroll	$ 4,124	$ 3,417
Unfunded Leave	7,837	7,256
Deferred Lease Liabilities	57	140
Total Public Liabilities	**$ 12,018**	**$ 10,813**

NOTE 8. LEASES

Operating Leases

1700 G Street NW

FHFA has an occupancy lease with the Office of Thrift Supervision (OTS) at 1700 G Street NW, Washington, DC, that covers office space and building services, including utilities, security guards, janitorial services, mail delivery, use of the loading dock, garage parking and building operation and maintenance. The initial term of the lease was for five years beginning in 1993, with the option to renew for three 5-year terms with OFHEO. This lease was transferred to FHFA with its creation. FHFA has exercised the third of the three option terms.

FHFA may terminate the lease agreement with OTS in whole or in part. In the event of termination at FHFA's discretion, FHFA would be required to pay two months' rent. If either party ceases to exist or merges with another entity by operation of law, either party may terminate the rental agreement. In the event of termination under this provision, neither party is liable for further costs, fees, damages or other monies due to the termination, except for payments through the date of the termination. Because of this termination clause, no deferred rent is established for this lease, nor is disclosure of minimum future lease payments required under Financial Accounting Standard Board Statement No. 13.

1750 Pennsylvania Avenue NW and 1625 Eye Street NW

FHFA leases office space in Washington, DC at 1750 Pennsylvania Avenue NW and 1625 Eye Street NW. The lease terms of 1750 Pennsylvania Avenue NW expire on March 30, 2011. The lease terms of 1625 Eye Street NW expire on June 30, 2015. Contingency space at an undisclosed location is also leased, with the lease expiring on March 31, 2011. Total rental payments for the fiscal years ended September 30, 2010 and 2009 were $4.91 million and $4.78 million, respectively. The minimum future payments for these leases are as follows:

Fiscal Year	Amount (Dollars in Thousands)
2011	$ 4,123
2012	3,674
2013	3,748
2014	3,823
2015	2,910
Thereafter	-
Total Future Payments	**$ 18,278**

NOTE 9. COMMITMENTS AND CONTINGENCIES

FHFA did not have any material commitments or contingencies that met disclosure requirements as of September 30, 2010 and 2009.

NOTE 10. PROGRAM COSTS

Pursuant to HERA, FHFA was established to supervise and regulate the fourteen regulated entities. The regulated entities include Freddie Mac, Fannie Mae and the twelve FHLBanks. FHFA's Program Costs were reflected as one program for fiscal year 2009 as defined by HERA Section 1311(b)(1). For fiscal year 2010, FHFA tracked resource allocations and program costs to the strategic goals (responsibility segments) developed for FHFA's new strategic plan, which was published in the last quarter of fiscal year 2009. The table below reflects the reporting change from fiscal year 2009 to 2010.

Program costs are broken out into two categories – "Intragovernmental" and "With the Public". Intragovernmental costs are costs FHFA incurs through contracting with other federal agencies for goods and/or services, such as rent paid to OTS, payroll processing services received from the Department of Agriculture and imputed financing costs for post-retirement benefits with OPM. With the Public costs are costs FHFA incurs through contracting with the private sector for goods or services, payments for employee salaries, depreciation, annual leave and deferred rent expenses. Revenue is comprised of assessments, investment interest, and miscellaneous revenue. Intragovernmental expenses relate to the source of goods and services purchased by the agency and not to the classification of related revenue. Such costs and revenue are summarized as follows:

(Dollars in Thousands)	2010	2009
Safety and Soundness		
Intragovernmental Costs	$ 21,703	$ -
Public Costs	74,167	-
Total Costs	95,870	-
Less: Intragovernmental Earned Revenue	108	-
Less: Public Earned Revenue	89,164	-
Net Safety and Soundness Costs	**6,598**	**-**
Affordable Housing		
Intragovernmental Costs	3,759	-
Public Costs	12,272	-
Total Costs	16,031	-
Less: Intragovernmental Earned Revenue	33	-
Less: Public Earned Revenue	26,786	-
Net Affordable Housing (Income)/Costs	**(10,788)**	**-**
Conservatorship		
Intragovernmental Costs	1,926	-
Public Costs	14,737	-
Total Costs	16,663	-
Less: Intragovernmental Earned Revenue	33	-
Less: Public Earned Revenue	27,078	-
Net Conservatorship (Income)/Costs	**(10,448)**	**-**
Total Intragovernmental costs	27,388	24,048
Total Public costs	101,176	98,768
Total Program Costs	128,564	122,816
Less: Total Intragovernmental Earned Revenue	174	33
Less: Total Public Earned Revenue	143,028	115,676
Total Program Net (Income)/Costs	**$ (14,638)**	**$ 7,107**

NOTE 11. APPORTIONMENT CATEGORIES OF OBLIGATIONS INCURRED

All obligations incurred are characterized as Category C, Exempt from apportionment (i.e. not apportioned), on the Statement of Budgetary Resources. Obligations incurred and reported in the Statement of Budgetary Resources in fiscal years 2010 and 2009 consisted of the following:

(Dollars in Thousands)	2010	2009
Direct Obligations, Category C	$ 132,707	$ 111,682
Reimbursable Obligations, Category C	101	4,569
Total Obligations Incurred	**$ 132,808**	**$ 116,251**

NOTE 12. LEGAL ARRANGEMENTS AFFECTING USE OF UNOBLIGATED BALANCES

HERA requires that any balance that remains unobligated at the end of the fiscal year, except for amounts assessed for contribution to FHFA's working capital fund, must be credited against the next year's assessment to the regulated entities. As of September 30, 2010 and 2009, the unobligated balance was $22.7 million and $44.8 million, of which $35.1 million of the balance at September 30, 2009 was deferred revenue, which was unavailable. The portion of the fiscal year 2010 unobligated available balance that will be credited against the regulated entities' April assessments is $16.7 million with the remaining $6.0 million retained in the working capital fund. (See Note 2. Fund Balance With Treasury)

NOTE 13. BUDGETARY RESOURCE COMPARISONS TO THE BUDGET OF THE UNITED STATES GOVERNMENT

Statement of Federal Financial Accounting Standards No. 7, "Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting", calls for explanations of material differences between amounts reported in the Statement of Budgetary Resources and the actual balances published in the Budget of the United States Government (President's Budget). The President's Budget that will include fiscal year 2010 actual budgetary execution information has not yet been published. The President's Budget is scheduled for publication in February 2012 and can be found at the OMB Web site: **http://www.whitehouse.gov/omb/**. The 2011 Budget of the United States Government, with the "Actual" column completed for 2009, has been reconciled to the Statement of Budgetary Resources and there were no material differences.

NOTE 14. UNDELIVERED ORDERS AT THE END OF THE PERIOD

For the fiscal years ended September 30, 2010 and 2009, undelivered orders amounted to $20.60 million and $12.87 million, respectively.

NOTE 15. INCIDENTAL CUSTODIAL COLLECTIONS

FHFA's custodial collections primarily consist of Freedom of Information Act requests and civil penalties assessed. Custodial collections will be reflected in the Fund Balance with Treasury amount on the Balance Sheet. While these collections are considered custodial, they are neither primary to the mission of the agency nor material to the overall financial statements. FHFA also collects civil penalties assessed against the regulated entities. FHFA's custodial collections are $288 for the year ended September 30, 2010. Custodial collections totaled $500 thousand for the year ended September 30, 2009 which resulted from a penalty collected from a former executive of Freddie Mac . There were no civil penalties assessed or collected in fiscal year 2010. Custodial collections are transferred to the Treasury General Fund on September 30 and are not reflected in the financial statements of the Agency.

NOTE 16. RECONCILIATION OF NET COST OF OPERATIONS TO BUDGET

FHFA has reconciled its budgetary obligations and non-budgetary resources available to its net cost of operations.

(Dollars In Thousands)	2010	2009
Resources Used to Finance Activities:		
Budgetary Resources Obligated		
Obligations Incurred	$ 132,808	$ 116,251
Less: Spending Authority from Offsetting Collections and Recoveries	2,794	5,077
Obligations Net of Offsetting Collections and Recoveries	130,014	111,174
Less: Offsetting Receipts	143,100	115,699
Net Obligations	(13,086)	(4,525)
Other Resources		
Imputed Financing from Costs Absorbed by Others	4,807	3,078
Total Resources Used to Finance Activities	**(8,279)**	**(1,447)**
Resources Used to Finance Items Not Part of the Net Cost of Operations:		
Change in Budgetary Resources Obligated for Goods, Services and Benefits Ordered But Not Yet Provided	7,729	(2,524)
Resources That Fund Expenses Recognized in Prior Periods	84	46
Resources That Finance the Acquisition of Assets	975	974
Total Resources Used to Finance Items Not Part of the Net Cost of Operations	8,788	(1,504)
Total Resources Used to Finance the Net Cost of Operations	**(17,067)**	**57**
Components of the Net Cost of Operations That Will Not Require or Generate Resources in the Current Period:		
Components Requiring or Generating Resources in Future Periods		
Increase in Annual Leave Liability	581	3,349
Other	1	-
Total Components of Net Cost of Operations That Will Require or Generate Resources in Future Periods	582	3,349
Components Not Requiring or Generating Resources		
Depreciation and Amortization	2,200	3,697
Other	(353)	4
Total Components of Net Cost of Operations That Will Not Require or Generate Resources	1,847	3,701
Total Components of Net Cost of Operations That Will Not Generate Resources in the Current Period	2,429	7,050
Net (Income from)/Cost of Operations	**$ (14,638)**	**$ 7,107**

NOTE 17. SUBSEQUENT EVENT

Subsequent events have been evaluated through November 15, 2010, the date the financial statements are available to be issued.

On October 25, 2010, the FHLBank of Seattle's Board of Directors agreed to a set of stipulations made by FHFA and consented to an FHFA order that set forth a comprehensive set of actions and requirements for the Bank. This was in response to investment decisions made in 2006 and 2007 and a series of supervisory determinations beginning in November 2009, when FHFA used its Prompt Corrective Action authority to make the discretionary determination that the FHLBank of Seattle was undercapitalized based on depreciation in the value of the Bank's investments in private-label MBS. The decline in value of private-label MBS investments and related shortcomings in its retained earnings made it inadvisable for the FHLBank of Seattle to honor pending requests for stock redemptions by member institutions. In response to the FHFA determination that the Seattle Bank was undercapitalized, the Bank submitted to FHFA a capital restoration plan in December 2009. In April 2010, FHFA directed the Bank to provide a business plan supplement to its capital restoration plan to address how the Bank would move toward more normal FHLBank functioning, including a greater balance sheet focus on advances and a return of capital at par to members. The Bank submitted the business plan supplement to FHFA on August 16, 2010, which was deemed complete upon a meeting at FHFA offices on August 31, 2010. FHFA responded to the Bank's capital restoration plan and business supplement in a meeting with the Bank's Board of Directors on October 22, 2010. The consent order and associated agreement with the Board constitute the Bank's approved capital restoration plan. The Bank also announced on October 25, 2010, that its President was stepping down and the current Chief Operating Officer would serve as the Bank's Acting President and Chief Executive Officer.

Appendix

Glossary

Acronyms

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Glossary

Accounting Total Capital – The amount by which the book value of assets exceeds the book value of liabilities. For the FHLBanks, it is the sum of capital stock outstanding, retained earnings, and accumulated other comprehensive income (AOCI).

Advances – Collateralized loan made by an FHLBank to a member to fund lending activities and to maintain liquidity for the member's operations. The FHLBank Act requires all advances to be collateralized and limits collateral to Treasury and agency securities, deposits in an FHLBank, residential mortgage loans, and other real estate-related collateral.

Alt-A Mortgage – Generally a loan with less than standard documentation, especially of borrower income of assets, but sometimes also includes loans with credit defects or other deviators from standard underwriting standards.

Capitalization – The sum of a firm or individual's long-term debt, stock, and retained earnings.

Collateralize – To secure a financial instrument, such as a loan, with an asset, such as a security or home.

Conservatorship – Statutory process designed to stabilize troubled institutions with the objective of maintaining normal business operation and restore their safety and soundness.

Consolidated Obligations – A term for the joint obligations of the 12 FHLBanks; Consolidated Obligations are debt instruments which are sold to the public through the Office of Finance, but are not guaranteed by the U.S. Government.

Correspondent Banking – An arrangement whereby the settlement or service-providing bank makes or receives payments, potentially performing additional banking services on behalf of the customer or user bank.

Enterprise – Fannie Mae or Freddie Mac.

Enterprise Risk – Includes enterprise credit risk, market risk, and operational risk.

Foreclosure – A legal process dictated by state law in which the mortgaged property is sold to pay off the mortgage of the defaulting borrower.

GAAP Net Worth – The amount by which a company's assets exceed its liabilities as determined by generally accepted accounting principles (GAAP).

Ginnie Mae – Government National Mortgage Association.

Loan Modification – A change or changes to the original mortgage terms, which may include a change to the product (adjustable-rate to fixed-rate), interest rate, term and maturity date, amortization term, and amortized balance.

Mortgage Delinquency Rate – A mortgage is considered delinquent or late when a scheduled payment is not made before the due date. The rate and total amount of the late fee is dependent upon the lender and the terms of the mortgage.

Mortgage Underwriting Standards – The process a lender uses to determine if the risk of lending to a particular borrower under certain parameters is acceptable. Most of the risks and terms that underwriters consider fall under the three C's of underwriting: credit, capacity, and collateral.

Permanent Capital – The sum of common stock, preferred stock, and retained earnings.

Portfolio – A collection of investments, either diverse or similar in nature, held by an institution or individual.

Secondary Mortgage Market – The market in which mortgages or mortgage-backed securities are acquired by the Enterprises and are traded.

Senior Preferred Stock – Capital stock owned by the U.S. Department of the Treasury which pays specific dividends before preferred stock or common stock dividends. In the event of liquidation, senior preferred stock takes precedence over preferred and common stock.

Senior Preferred Stock Purchase Agreements – The agreements ensure the Enterprises maintain a positive net worth so they may continue to be active suppliers of housing finance. The agreements are ongoing, explicit, and irreversible contractual commitments of the federal government, ensuring that Fannie Mae and Freddie Mac can meet their obligations and maintain a positive net worth.

Supervisory Rating – FHFA has established four rating levels for supervisory concerns: No or Minimal Concerns, Limited Concerns, Significant Concerns, and Critical Concerns. These ratings describe how well risks are identified, measured, monitored, controlled, and managed. No or Minimal Concerns have very minor weaknesses or criticisms that affect the Enterprise's safety and soundness, while Critical Concerns involve a consent order or formal agreement between FHFA and the Enterprise to ensure appropriate corrective action is taken.

Total Capital – The sum of permanent capital, the par value of Class A stock outstanding, a general allowance for losses, and the amount of any other instruments identified in an FHLBank's capital plan that FHFA has determined to be available to absorb losses.

Undercapitalized – A state of hindered operation for the FHLBanks due to limited amounts of capital.

Acronyms

AHP	Affordable Housing Program
AOCI	Accumulated Other Comprehensive Income
CDFI	Community Development Financial Institution
CSRS	Civil Service Retirement System
DER	Division of Enterprise Regulation
DOL	Department of Labor
ECIC	Executive Committee on Internal Controls
EESA	Emergency Economic Stabilization Act of 2008
Fannie Mae	Federal National Mortgage Association
FASAB	Federal Accounting Standards Advisory Board
FBWT	Fund Balance with Treasury
FECA	Federal Employees Compensation Act
FERS	Federal Employees Retirement System
FHFA	Federal Housing Finance Agency
FHFB	Federal Housing Finance Board
FHLBank	Federal Home Loan Bank
FISMA	Federal Information Security Management Act
FMFIA	Federal Managers Financial Integrity Act of 1982
FOIA	Freedom of Information Act
Freddie Mac	Federal Home Loan Mortgage Corporation
FSOC	Financial Stability and Oversight Council
FY	Fiscal Year
GAAP	Generally accepted accounting principles
GAO	U.S. Government Accountability Office
GSE	Government-sponsored enterprise
GSEER	Governance, Solvency, Earnings, and Enterprise Risk
HAMP	Home Affordable Modification Program
HARP	Home Affordable Refinance Program
HERA	Housing and Economic Recovery Act of 2008
HPI	House Price Index
HUD	Department of Housing and Urban Development
IT	Information Technology
MBS	Mortgage-backed securities
MHA	Making Homes Affordable (Program)
MRA	Matters requiring attention
OFHEO	Office of Federal Housing Enterprise Oversight
OIG	Office of the Inspector General
OMB	Office of Management and Budget
OPM	Office of Personnel Management
OTIM	Office of Technology and Information Management
OTS	Office of Thrift Supervision
OTTI	Other than temporary impairment
PACE	Property Assessed Clean Energy
Private-Label MBS	Private-label mortgage -backed securities
PMA	Presidential Management Agenda
REFCORP	Resolution Funding Corporation
TARP	Troubled Asset Relief Program

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