
Federal Housing Finance Board

Performance and Accountability Report

Fiscal Year 2007



November 15, 2007

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MESSAGE FROM THE CHAIRMAN

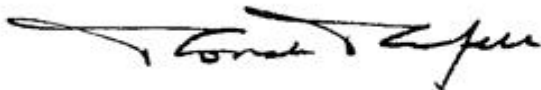
I am pleased to present the Federal Housing Finance Board's (Finance Board) Performance and Accountability Report for fiscal year 2007 (FY2007). This Report summarizes the agency's success in meeting its FY2007 goals and objectives as set forth in the FY2007 Annual Performance Budget and provides Finance Board financial and program performance information.

The primary duty of the Finance Board is to ensure that the Federal Home Loan Banks (FHLBanks) and the Office of Finance operate safely and soundly. The Finance Board also assesses the FHLBanks' administration of their affordable housing and community investment programs (AHP and CIP, respectively).

FY2007 was a productive year at the Finance Board. The agency met the goals established in the FY2007 Annual Performance Budget. In addition, the Finance Board made substantial progress toward strengthening and positioning the agency to carry out its responsibilities more efficiently and effectively.

The agency's FY2007 financial statements, including an unqualified opinion, are provided in this Report. The opinion states that the financial statements are fairly presented and demonstrate accountability in the execution of the agency's responsibilities. This Report also includes a statement of reasonable assurance that the Finance Board's management accountability and internal controls are adequate and effective.

The Finance Board will continue to work to promote the safety and soundness of the FHLBanks and build on the agency's accomplishments.



Ronald A. Rosenfeld
Chairman

MANAGEMENT DISCUSSION AND ANALYSIS

MISSION, VISION, AND VALUES

MISSION

The Finance Board's mission is to ensure that the FHLBanks are safe and sound so they serve as a reliable source of liquidity and funding for the nation's housing finance and community investment needs.

VISION

To maintain the public's trust, the Finance Board is dedicated to the highest professional standards of accountability and independence in carrying out its responsibilities for FHLBank supervision and oversight.

VALUES

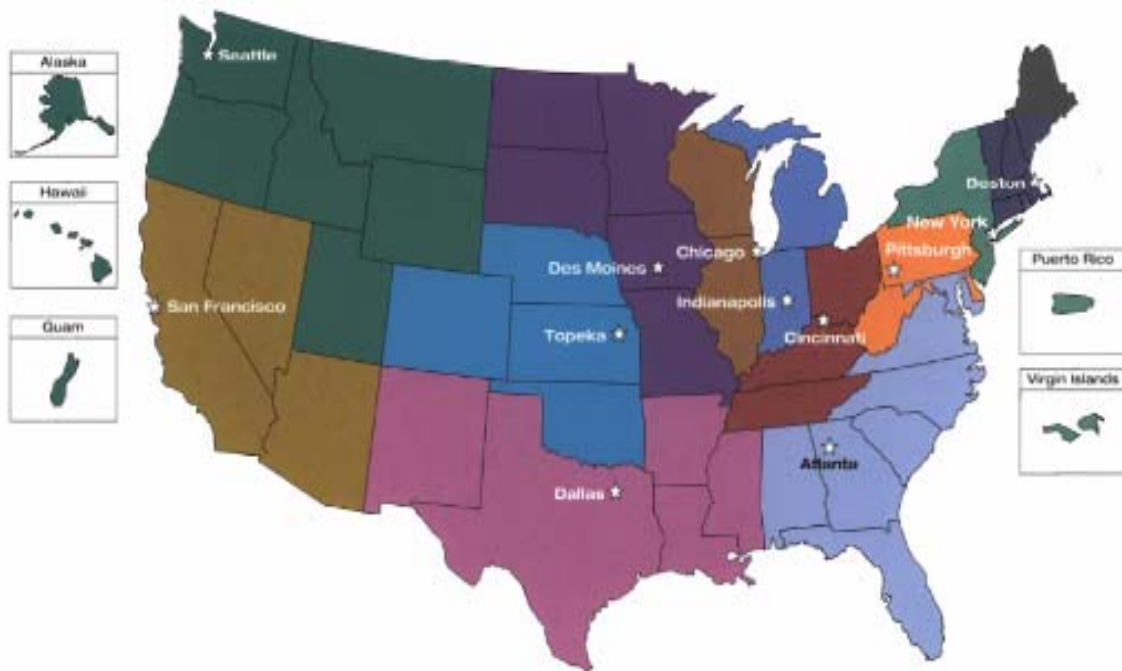
The core values underlying the mission and vision of the Finance Board, which guide its organizational decisions and actions, are:

- Independence. The Finance Board is the arm's-length regulator of the FHLBanks and the Office of Finance.
- Accountability. The Finance Board is a steward of the public's trust and will use its resources efficiently and in the public interest.
- Responsiveness. The Finance Board aligns its actions with its mission and responds promptly and effectively to emerging risks and opportunities in the finance system.
- Integrity. The Finance Board discharges its responsibilities fairly and adheres to the highest standards of ethical conduct.
- Excellence. The Finance Board strives for excellence in carrying out its responsibilities and recognizes the contributions of employees who demonstrate the highest professional standards in their work.

THE FEDERAL HOME LOAN BANK SYSTEM

In 1932, Congress authorized the establishment of the FHLBanks to stimulate mortgage finance and provide liquidity to credit markets. Until 1989, FHLBank members consisted primarily of savings and loan associations engaged in home financing. In 1989, Congress extended eligibility for FHLBank membership to commercial banks and federally insured credit unions (subject to a home financing requirement). In 1999, Congress made FHLBank membership voluntary for all types of eligible institutions.

FEDERAL HOME LOAN BANK DISTRICTS



The FHLBanks are privately capitalized, government-sponsored enterprises that provide wholesale credit to members and certain nonmembers to be used for mortgage lending and related activities. In addition, the FHLBanks have a mandate to promote housing and community investment finance. The FHLBanks provide long-term, flexible financing to more than 8,100 member financial institutions around the country. As of September 30, 2007, the FHLBanks had combined assets exceeding \$1.2 trillion dollars.

The FHLBanks are funded principally by the issuance of consolidated obligations of the FHLBank System. These consolidated obligations consist of bonds (with original maturities of one year or longer) and discount notes (with original maturities of less than one year). Consolidated obligations are not guaranteed or insured by the U.S. government. However, their status as government-sponsored enterprises enables the FHLBanks to raise funds at rates slightly higher than comparable obligations issued by the U.S. Treasury. Debt issued by the FHLBanks through the Office of Finance is the joint-and-several obligation of all 12 FHLBanks.

Members use short-and long-term advances (collateralized loans) to fund their lending activities and to maintain liquidity for their operations. Long-term advances may be used only to support residential housing finance and, in the case of a community financial institution, to support lending to small businesses, small farms, and small agricultural businesses. The preponderance of the collateral supporting advances consists of mortgage assets.

In addition to advances, the FHLBanks purchase qualifying mortgage loans from members under various acquired member asset programs. Under these programs, the FHLBank manages the market risk associated with the loans while members bear most of the credit risk through a loss-sharing arrangement or the purchase of mortgage insurance for the loans sold to the FHLBank.

KEY FEDERAL HOME LOAN BANK FINANCIAL STATISTICS (in millions)

	Sep 30 2007	Dec 31 2006	Dec 31 2005
Advances to Members	\$824,000	\$640,682	\$619,859
Mortgage Loans, Net	92,963	97,974	105,242
Investments	305,465	275,267	272,115
Other Assets	<u>8,228</u>	<u>7,215</u>	<u>5,904</u>
Total Assets	<u>\$1,230,656</u>	<u>\$1,021,138</u>	<u>\$1,003,120</u>
Consolidated Obligations	\$1,136,681	\$938,762	\$921,475
Deposits and Borrowings	25,965	21,186	21,769
Other Liabilities	16,557	16,155	15,318
Capital	51,453	45,035	44,558
Net income	\$1,961*	\$2,586	\$2,494

*Reflects income for first 9 months of 2007

Members have access to several programs to support affordable housing and community investment activities. The Federal Home Loan Bank Act of 1932 (Bank Act), as amended, requires each FHLBank to allocate ten percent of its annual net income to fund a subsidy program known as the Affordable Housing Program (AHP).

Under the AHP, each FHLBank provides funds to finance housing for very low-, low-, and moderate-income households through a competitive process. AHP funds also are awarded through the homeownership set-aside program in which members obtain AHP funds from the FHLBank to provide grants to eligible low- and moderate-income households for down payment, closing cost, and counseling cost assistance in conjunction with a purchase or rehabilitation of owner-occupied units. From the inception of the AHP in 1990 through December 31, 2006, the FHLBanks have awarded over \$2.9 billion in subsidies to assist more than 575,000 housing units.

	Competitive Application Program	Set-Aside Program
Time Period	1990-2006	1995-2006
Units Receiving Assistance (in thousands)	518	57
Total Funds Awarded (\$ in millions)	\$2,669	\$247

THE FEDERAL HOUSING FINANCE BOARD

The Finance Board is an independent agency established by the Financial Institutions Reform, Recovery, and Enforcement Act of 1989. It is the successor agency to the former Federal Home Loan Bank Board, which was established by the Bank Act. The Finance Board's statutory mandate is to ensure that the FHLBanks operate in a financially safe and sound manner, carry out their housing finance mission, and remain adequately capitalized and able to raise funds in the capital markets. In addition to its supervision of the FHLBanks, the Finance Board has regulatory authority and supervisory oversight responsibility for the Office of Finance, a joint office of the FHLBanks, which issues FHLBank System debt.

The Finance Board is governed by a five-member board of directors. Four of the directors are appointed by the President and confirmed by the Senate and must have extensive experience or training in housing finance or a commitment to providing specialized housing credit. The fifth member is the Secretary of the U.S. Department of Housing and Urban Development. No more than three directors may be members of the same political party.

At least one appointed director must be from an organization with more than a 2-year history of representing consumer or community interests in banking services, credit needs, housing, or financial consumer protections. The appointed members of the board of directors serve staggered 7-year terms. The President designates the chairperson of the board of directors from among these appointed members.

The Finance Board is organized into five Offices:

The *Office of the Board of Directors* is responsible for setting the agency's strategic direction and approving policies and regulations. By delegation from the full board, the chairperson supervises management and policy execution. The board generally meets monthly in public sessions. The agency's chief information officer, who is responsible for the Finance Board's technology and information systems, reports to the chairperson.

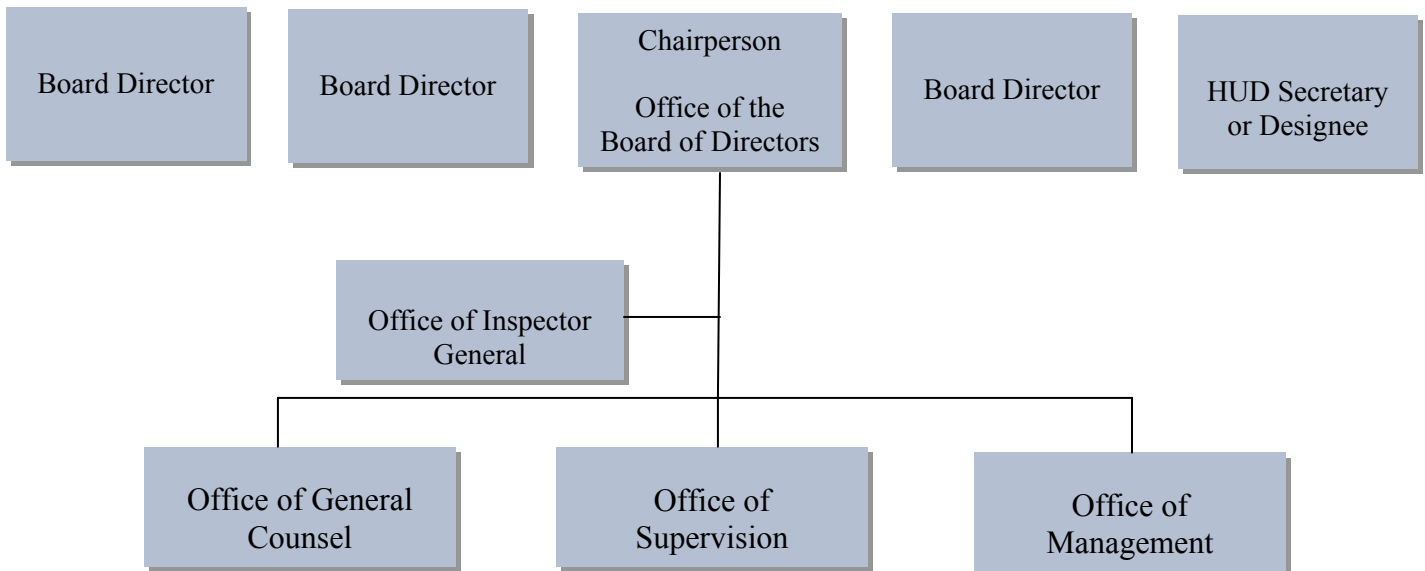
The *Office of Supervision* is responsible for the supervision and examination of the FHLBanks and the Office of Finance. The Office of Supervision performs this function through annual on-site examinations, periodic visitations, and off-site monitoring. Other Office of Supervision responsibilities include supervisory policy and program development, regulatory analysis and development, and economic research and analysis.

The *Office of General Counsel* provides legal support and guidance on interpretations of laws, regulations, and policies to Finance Board officials. The Office of General Counsel prepares legal documents on behalf of the Finance Board and represents the agency in judicial and administrative proceedings. The Office of General Counsel manages the Finance Board's ethics and Freedom of Information Act programs and acts as the secretary to the board.

The Office of Management is the principal advisor to the Chairman of the Finance Board on management and organizational policies and is responsible for the Finance Board's administrative management programs. This includes responsibility for the Finance Board's finance and accounting, budget, personnel, payroll, contracting and procurement, and facilities and property management.

The *Office of Inspector General* operates pursuant to the Inspector General Act of 1978, as amended. The Office of Inspector General conducts and supervises audits and investigations related to Finance Board programs and operations, and recommends policies to promote economy, efficiency, and effectiveness, and to prevent and detect fraud and abuse.

FEDERAL HOUSING FINANCE BOARD ORGANIZATION CHART



PRIORITIES, RESOURCES, AND PERFORMANCE MEASURES

The Finance Board's planning, budgeting, and performance management process sets the strategic direction, determines planned activities and resources, measures and monitors performance throughout the year, and performs an annual performance assessment. These components reflect a continuous cycle of performance management centered on outcomes. The agency uses annual performance assessments to analyze performance and improve effectiveness and efficiency.

The Finance Board produces three main reports as a result of this process. The agency's Strategic Plan, covering a 5-year period, sets overall strategic goals for the agency. Two annual reports illustrate the ways the agency is directing its resources to achieve and measure its progress in achieving its strategic goals. First, the agency produces an Annual Performance Budget, which describes how it will allocate its resources in the upcoming fiscal year to achieve the strategic priorities outlined in the Strategic Plan. Second, the agency produces a Performance and Accountability Report annually, which summarizes the agency's success during the fiscal year in meeting its goals and objectives as set forth in the Annual Performance Budget for that fiscal year. The Performance and Accountability Report also provides Finance Board financial and program performance information.

In its fiscal year 2007-2012 Strategic Plan, the Finance Board established two strategic goals that guide its operation. The Strategic Plan is available on the agency's website (www.fhfb.gov). The two strategic goals are:

- The FHLBanks operate safely and soundly; and
- The affordable housing and community investment programs of the FHLBanks operate effectively and efficiently.

For each strategic goal, the agency established strategic outcomes that it expects to achieve. The Finance Board developed annual performance goals to provide indicators of progress by the Finance Board and the FHLBanks. Finally, in recognition of the fact that the goals the Finance Board has set depend not only on the actions of the Finance Board but also on the actions of each of the FHLBanks, the Finance Board has adopted annual performance measures for Finance Board actions to ensure that the agency is doing the most it can to ensure that it meets the strategic goals and outcomes. The relationship between strategic goals, outcomes, annual performance goals, and measures is depicted below.

STRATEGIC GOALS	STRATEGIC OUTCOMES	ANNUAL PERFORMANCE GOALS	ANNUAL PERFORMANCE MEASURES
<p>1. The FHLBanks operate safely and soundly.</p>	<p>1. The FHLBanks effectively identify and manage risk.</p> <p>2. The FHLBanks remain adequately capitalized, and able to raise funds in the capital markets.</p>	<p>1. The FHLBanks address principal safety and soundness examination findings to the satisfaction of the Finance Board prior to the next examination.</p> <p>2. The FHLBanks correct supervisory or compliance issues within required timeframes.</p> <p>3. The FHLBanks' combined financial statements comply with applicable laws, rules, and regulations.</p>	<p>1. Conduct all safety and soundness activities, including annual examinations, quarterly visitations, and off-site monitoring.</p> <p>2. Review safety and soundness examination findings with the FHLBanks semi-annually to ensure the FHLBanks are making progress to remedy identified shortcomings.</p> <p>3. Conduct on-site examination of the Office of Finance and review annual and quarterly combined statements issued by the Office of Finance for compliance with disclosure requirements.</p>
<p>2. The FHLBanks' affordable housing and community investment programs operate effectively and efficiently.</p>	<p>1. The FHLBanks foster the development of owner-occupied and affordable rental housing for eligible very low-, low-, and moderate-income households.</p>	<p>1. The FHLBanks address principal affordable housing examination findings to the satisfaction of the Finance Board prior to the next examination.</p> <p>2. The FHLBanks distribute affordable housing funds as approved in the AHP application.</p>	<p>1. Conduct all affordable housing activities, including annual examinations and off-site monitoring.</p> <p>2. Review affordable housing and community investment examination findings with the FHLBanks semi-annually to ensure the FHLBanks are making progress to remedy identified shortcomings.</p> <p>3. Use examinations to review program effectiveness as well as compliance with the Bank Act, Finance Board regulations, and FHLBank policies.</p>

Strategic Goal 1. The Finance Board established two strategic outcomes to indicate the degree to which it is achieving its first strategic goal that the FHLBanks operate safely and soundly. To the extent that the FHLBanks are able to identify and manage risk, to remain adequately capitalized and to raise funds in the capital markets, they are more likely to operate safely and soundly. To provide even more precision, the Finance Board established annual performance goals to determine the degree to which the FHLBanks are acting promptly to correct deficiencies identified by the Finance Board, and to determine the degree to which the FHLBanks' combined financial statements comply with applicable laws and regulations. Finally, annual performance measures were established as indicators of how well the Finance Board is carrying out its mission to ensure the safe and sound operations of the FHLBanks.

Strategic Goal 2. The Finance Board has established a strategic outcome to indicate the degree to which it is meeting its second strategic goal that the affordable housing and community investment programs of the FHLBanks operate effectively and efficiently. The strategic outcome requires the FHLBanks to foster the development of owner-occupied and affordable rental housing for eligible very low-, low-, and moderate-income households. The Finance Board established two annual performance goals to reveal the degree to which the FHLBanks are acting promptly to correct deficiencies identified by the Finance Board, and whether each FHLBank is distributing its affordable housing funds as approved in the AHP application. Finally, annual performance measures were established as indicators that the Finance Board is meeting its mandate to ensure the effective and efficient operations of the FHLBanks' affordable housing and community investment programs.

PROGRAM PERFORMANCE OVERVIEW

The Finance Board achieved all of its performance goals in FY2007. The agency strengthened its supervisory program through the implementation of risk-based examinations and additional monitoring programs and tools. It also issued several final rules to 1) enhance board governance at the FHLBanks; 2) improve the quality and timeliness of data collected; 3) limit the use of excess stock at each FHLBank; and 4) enhance the effectiveness of the AHP. The following list summarizes key Finance Board achievements during FY2007.

MAJOR ACCOMPLISHMENTS

- Conducted safety and soundness examinations at all 12 FHLBanks and the Office of Finance;
- Reviewed the affordable housing program at 11 FHLBanks (FHLBank of Chicago was removed from the schedule);
- Introduced new FHLBank (Examination) risk rating system;
- Issued excess stock final rulemaking;
- Issued AHP final rulemaking;
- Issued financial interests of directors final rulemaking;
- Issued public interest director final rulemaking;
- Introduced new process for the appointment of public interest directors;
- Appointed full slate of public interest directors at each FHLBank;
- Completed safety and soundness examination manual;
- Prepared examiner workpaper guidance;
- Conducted examiner training on examination manual and workpaper guidance;
- Issued first cease and desist order in agency history (FHLBank of Chicago);
- Lifted written agreement with FHLBank of Seattle;
- Prepared preliminary draft of AHP examination manual;
- Enhanced data management and information systems (CRS.net);
- Formalized responsibility for quality assurance;
- Instituted weekly reporting of advance levels to monitor credit conditions;
- Prepared advisory bulletins on a range of issues;
- Responded to new business notices and capital plan amendments;
- Issued the semi-annual FHLBank profile books;
- Issued quarterly and monthly risk monitoring reports;
- Issued quarterly market risk monitoring reports;
- Enhanced the “Model Bank” application;
- Expanded the use of “Model Bank” in examinations and in support of enforcement actions; and
- Conducted AHP examiner training on assessing FHLBanks’ implementation plans.

THE YEAR IN REVIEW

The Finance Board's accomplishments in FY2007 were concentrated in the following areas:

Risk-Focused Supervision. In FY2007, the Finance Board implemented the FHLBank (Examination) Risk Rating System under which the Finance Board assigns each FHLBank and the Office of Finance a composite rating based on evaluation of various aspects of its operations.

The Finance Board also redesigned the risk-focused examination process. Under this redesign, the examination team develops the supervisory strategy immediately after finalizing an examination to ensure that salient matters are addressed in a timely manner. Examiners also make periodic visits to the FHLBanks and the Office of Finance during the year. They develop the examination scope based upon results from the previous year's examination, a review of events during periodic visits, and preplanning meetings held with all areas of the Office of Supervision and Office of the General Counsel. They may expand the scope as an examination unfolds and they identify new areas of concern.

The Finance Board also released a revised risk management (safety and soundness) examination manual and work programs to guide examiners in performing risk-focused examinations. The manual documents examination objectives and procedures, addresses subjects that examiners most often encounter when conducting an examination, provides guidance on new examination work paper requirements, and promotes examination consistency.

The Finance Board completed all safety and soundness and AHP examinations scheduled for the year and assigned component and composite ratings to each FHLBank based on the rating system. Two examinations led to the amendment and the termination of outstanding formal agreements and the issuance of the first cease and desist order (by consent of the board of directors of the FHLBank Chicago) in the Finance Board's history.

Economic and Financial Analysis. Economists and financial analysts supported the examination of the FHLBanks, provided analytical support in the evaluation of FHLBank programs, and provided analysis and input into the development of regulatory and policy initiatives at the Finance Board. The Finance Board relies on this research and analysis to produce the semi-annual profile book and quarterly market risk monitoring reports. The principal means for providing this support to examinations is through evaluations of the quality of risk modeling at the FHLBanks and analysis of the FHLBanks' financial condition and performance and of systemic trends affecting the FHLBanks and the FHLBank System.

As part of each examination, staff in the market risk modeling area closely reviewed and evaluated the Bank's own market risk model results and compared those results, for selected instruments, against results from modeling within the Finance Board. To ensure the quality of these modeling results, the Finance Board assessed the FHLBanks' modeling procedures and risk-related analysis as part of the annual examinations. Finance Board analysts reviewed FHLBank activities, financial condition, fiscal and operating performance, and regulatory compliance, and assessed market developments that may affect the FHLBank System. Economists, modelers, and analysts worked closely with examination staff to contribute to the establishment of the scope of examination. In FY2007, the Finance Board expanded and formalized the use of financial analysts, economists, and accountants as part of the on-site examination.

Off-Site FHLBank Monitoring and Analysis. In addition to the ongoing off-site monitoring of the FHLBanks described above, in FY2007, the Finance Board conducted a survey of the FHLBanks to assess their exposures to subprime and nontraditional mortgage loans. The survey results indicated that the FHLBanks are able to reasonably estimate their exposures and that the level of those exposures is manageable. In August 2007, in response to financial market difficulties stemming from the subprime and nontraditional mortgage loan segments, the Finance Board started weekly monitoring of trends at the FHLBanks, particularly their advance volumes.

Policy and Regulations In FY2007, the Office of Supervision created a Supervisory and Regulatory Policy Division, responsible for safety and soundness, accounting policy, and AHP and community investment policy. This division also took the lead on regulatory proposals, such as proposed rulemakings, and in the development of supervisory and examiner guidance, such as Advisory Bulletins, Examiner Guidance Bulletins, and Examination Procedures. This group provided technical support for examinations, particularly with respect to examination standards, technical accounting matters, and interpretations of AHP requirements.

During the year, the Finance Board finalized rules regarding appointment of FHLBank directors and permissible financial interests for those directors. After issuing those final rules, the Finance Board appointed public interest directors at each of the 12 FHLBanks. The Finance Board also issued a final rule limiting the amount of "excess" stock at each FHLBank to one percent of the FHLBank's total assets to ensure the FHLBanks have a strong and permanent capital base to support their operations. FHLBanks exceeding the one percent limit may not issue stock dividends or otherwise issue additional excess stock. The rule also required FHLBanks to base dividend declarations on actual rather than expected or projected dividends.

The Finance Board issued advisory bulletins and examiner guidance in several areas in FY2007. Advisory bulletins adopted the Federal Home Loan Bank Rating System and addressed the management of risks on nontraditional and subprime residential

mortgage loans. The Finance Board also developed guidance on examination reports to ensure that examiners' conclusions are supported, documented, and presented in a logical and orderly fashion.

Affordable Housing and Community Investment. The Finance Board completed AHP/Community Investment Cash Advance (CICA) examinations in FY2007 for 11 FHLBanks. For one FHLBank, AHP/CICA was excluded from the examination scope based on risk considerations. In addition, the Finance Board provided training to AHP examiners following the adoption of a revised AHP final rule and completed a draft of the AHP and CICA Program Examination Manual. Final publication of this manual will occur in FY2008.

Accounting. In FY2007, accountants at the Finance Board reviewed the FHLBank System's external auditor's workpapers for annual audits of the 12 FHLBanks' financial statements and the FHLBank System's combined financial statements - for both the 2005 and 2006 reporting periods. These reviews provide the Finance Board with information related to supervisory programs that could affect the scope of examinations and other supervisory actions.

Finance Board accountants also provided consultative services on accounting issues and questions identified at several FHLBanks, identified issues and answered inquiries regarding the financial information collected by the Finance Board in the CRS system, and analyzed new accounting and auditing standards and other guidance, and assessed and responded appropriately to their likely impact on the FHLBanks and the FHLBank System.

Risk Monitoring and Information Technology Support. The Finance Board made substantial progress in FY2007 toward updating its data management and information systems. New versions of the Call Report System (CRS.net) and AHP database were released, and the Data Reporting Manual was updated to include all current FHLBank reporting obligations. In FY2008, the agency plans to begin re-specifying and rebuilding the Membership system database as well as reviewing and augmenting policies and procedures for capture, maintenance, and distribution of information. In addition, the Finance Board will continue to develop off-site risk monitoring and reporting functions to build upon the information collected from the FHLBanks.

Quality Assurance. In FY2007, the Office of Supervision established a Quality Assurance Unit to provide objective assessments of the Office's supervisory and regulatory operations and to add value by identifying potential opportunities to improve or enhance existing practices. In FY2008, the Quality Assurance Unit will conduct its first formal review of Finance Board examinations to assess their quality, accuracy, completeness, organization, and conformance with agency policies. The Quality Assurance Unit will also finalize procedures for its future reviews of other Office of Supervision functions.

Training. In FY2007, the Finance Board developed and presented new staff orientation, AHP examiner training, and supervisory training. The new staff orientation sessions provided an overview of the history and functions of the Finance Board and the FHLBank System for those who joined the Finance Board within the past year. The primary intent of the AHP training was to give AHP examiners the tools to review the AHP implementation plans as part of their overall review of the program at each FHLBank. The supervisory training emphasized risk-focused supervision and included segments on market risk and market risk management and modeling, risk-focused examination methodologies and strategies, and the revised call report system (CRS.net).

KEY EXTERNAL FACTORS

External conditions beyond the control of the organization can affect the performance of the Finance Board and the FHLBanks. These factors include developments in capital and housing markets, broader macroeconomic forces affecting interest rates or national or regional activity, and regulatory and legislative initiatives that can change the environment in which the FHLBanks operate. Regardless of the source of the influences on FHLBank performance, the Finance Board must respond promptly to ensure that the FHLBanks meet these challenges.

Significant events, influences, and risks that may affect the Finance Board are:

Legislation. The House of Representatives has passed legislation to establish a single agency as the regulator for the government-sponsored enterprises that support the national housing market. This new agency would oversee the safety, soundness, and housing mission achievement of the FHLBanks, Fannie Mae, and Freddie Mac.

Developments in Banking and Financial Markets. Financial markets continue to evolve with new products and services, particularly hedging activities and their associated accounting. These developments have the potential to influence the demand for FHLBank products and services as well as the FHLBanks' financial performance. As the industry changes, the supervisory focus of the Finance Board must also change to ensure continuous effective supervision of the FHLBanks. Recent supervisory initiatives have included reviewing the FHLBanks' anti-predatory lending policies; requiring increased accountability of FHLBank officers and directors as called for by the Sarbanes-Oxley Act of 2002; monitoring housing prices and foreclosure activity, particularly in areas affected by natural disasters and economic downturns; monitoring consolidation of the financial services industry and its potential effects on the FHLBanks' membership and business; and reviewing the composition of FHLBank capital and adequacy of retained earnings.

In addition, the rapid pace of technological innovation, especially in telecommunications and electronic data processing, continues to have a substantial effect on U.S. financial services. Harnessing technological innovations will create opportunities to improve the Finance Board's efficiency across organizational units and functions.

Economic Variables. Adverse economic conditions such as high unemployment, softening real estate markets, and sharp or prolonged changes in interest rates have the potential to affect the financial condition of the FHLBanks. The Finance Board is responding by directing the FHLBanks to review and strengthen their risk management practices and business operations vulnerabilities.

Staffing. In the competitive financial services environment, highly skilled personnel are in great demand. This makes recruiting and retaining a highly skilled workforce a continuing challenge. The Finance Board's recruitment and retention efforts have focused on attracting and retaining examiners, economists, accountants, analysts, and attorneys with the requisite financial, legal, and technological skills to model, monitor, and assess the risks undertaken by the FHLBanks and the Office of Finance.

Continuity of Operations. Financial institutions must maintain the capability to resume business during and after a crisis. Ensuring preparedness for a crisis continues to be a priority for the Finance Board both for its own operations and those of the FHLBanks and the Office of Finance.

The Finance Board maintains an Emergency Operations Center that provides essential personnel with the necessary resources to continue agency operations. During a crisis, Finance Board employees can securely access the agency's information technology systems remotely. Secure remote access to IT systems was tested in FY2007 as part of the agency's implementation of a plan to address a pandemic flu emergency.

MANAGEMENT CHALLENGES

In accordance with Office of Management and Budget (OMB) Circular A-136, The Office of Inspector General has determined the most serious management and performance challenges facing the Finance Board and made an assessment of the agency's progress in addressing those challenges. The Office of Inspector General's position is based on the audit work that has been performed to date, which is listed below.

1. Ensuring Safe and Sound Operations at the FHLBanks and Office of Finance

The primary mission of the Finance Board is to ensure that the FHLBanks are safe and sound so they can serve as a reliable source of liquidity and funding for the nation's housing finance and community investment needs.

The agency's examination and supervisory function serves a critical role in helping to ensure the success of the Finance Board's mission. However, as noted last year, there continue to be questions as to whether the examination and supervisory function: 1) has an adequate number of staff, 2) has staff that possess the appropriate knowledge, skills, and abilities, 3) has staff that are provided with adequate guidance, and 4) has adequate monitoring capability.

Agency Progress: The Finance Board took very positive steps to enhance the examination and supervision functions. The Finance Board is committed to achieving a risk-based examination approach and made commendable strides to provide better guidance to examiners. The Finance Board also took commendable steps to hire more examination and supervisory staff and developed a strategic plan for fully staffing the examination and supervision functions.

Management Response: Significant changes included the creation of explicit performance standards for Office of Supervision employees, development of a supervisory training program, and publication of a revised Safety and Soundness Examination Manual that is more risk-focused and includes detailed guidance for, among other things, workpaper documentation standards. Examination procedures now require the completion of summary memoranda to support examiner evaluations, analyses, and conclusions. Employee performance standards for managers and examiners include complying with the standards for and the timely completion of workpapers that will be factored into an employee's annual rating and merit pay increase. Two modules of an employee training program were developed and held for supervisory staff, with additional modules currently being developed for delivery in FY 2008. In addition, a Quality Assurance Unit was established to provide ongoing assessments of operating practices and internal controls, including revised standards for collecting, transmitting, storing, and protecting personally identifiable information.

The Finance Board also took substantive steps to hire more examination and supervisory staff, including the development of a strategic plan for fully staffing the examination and supervision functions. At the close of FY2007, the Office of Supervision filled 97 of 99 authorized positions.

2. Developing, Documenting and Communicating Agency Policies and Procedures

Essential to effective and consistent agency operations is the communication of management ideas to all stakeholders - especially agency employees. The most effective method of communicating management ideas is through the development, documentation, and communication of agency policies and procedures. Our experience in reviewing Finance Board operations is that, too frequently, we have concluded that written policies are needed or existing policies are outdated or have not been properly vetted to receive stakeholders' input.

Agency Progress: Finance Board managers have generally been very responsive to the Office of Inspector General's audit recommendations to develop written policies and procedures and have taken a more proactive posture in developing and implementing written policies and procedures. However, more needs to be done to: 1) initiate the development or update of written policies and procedures, 2) consistently vet policies and procedures through the Office of General Counsel and other stakeholders, and 3) effectively communicate agency-wide policies and procedures to Finance Board staff.

Management Response: For the past few years, the Director of Office of Management met monthly with Office of Management staff to review the status of the agency's administrative policies, establish the priorities for updates, assign staff to tasks, and establish timeframes for completion.

Approximately two years ago, the Office of Management implemented a review process to include the Office of Supervision, the Office of General Counsel, and the Office of Board of Directors the opportunity to provide feedback that Office of Management reviews and incorporates into the draft as appropriate. Upon final approval, the Office of Management communicates the policy updates to all Finance Board employees via electronic mail and posting on the intranet.

The Information Services and Technology Support division has developed an action item to review and update existing information technology policies as part of their process to comply with annual requirements in the Federal Information Security Management Act. Currently, the division is reviewing the existing policies and governing regulations to identify the policies that require updates. In addition, the division is assessing the overall framework for managing the documentation and use of information technology policies at the Finance Board.

FY2007 REPRESENTATIVE ACCOMPLISHMENTS

STRATEGIC GOAL 1: THE FEDERAL HOME LOAN BANKS OPERATE SAFELY AND SOUNDLY.	
Strategic Outcomes	Accomplishments
1. The FHLBanks effectively identify and manage risk	<ul style="list-style-type: none"> Completed all annual examinations and periodic visitations Implemented a program to assign an overall examination rating that summarizes the level of supervisory concern Replaced a written agreement with an FHLBank with a cease and desist order (by consent) and terminated a written agreement with another FHLBank
2. The FHLBanks remain adequately capitalized and able to raise funds in the capital markets	<ul style="list-style-type: none"> Each FHLBank exceeded its minimum regulatory capital requirements Approved capital plan amendments submitted by two FHLBanks Each FHLBank registered a class of equity securities with the U.S. Securities and Exchange Commission and is now subject to the reporting requirements of the Securities Exchange Act of 1934

STRATEGIC GOAL 2: The affordable housing and community investment programs of the FHLBanks operate effectively and efficiently.	
Strategic Outcomes	Accomplishments
1. The FHLBanks foster the development of owner-occupied and affordable rental housing for eligible very low-, low-, and moderate-income households	<ul style="list-style-type: none"> Reviewed advance and mortgage portfolios at each FHLBank for compliance with the Bank Act and Finance Board regulations Completed annual examinations of the AHP at 11 of the 12 FHLBanks As of June 30, 2007, the FHLBanks have awarded more than \$143 million in subsidies to assist 18,424 housing units

ALLOCATING RESOURCES TO MEET OUR GOALS

The Finance Board prepared its FY2007 Annual Performance Budget to link the agency's strategic and performance goals to the costs of achieving those goals. To achieve these goals, the Finance Board identifies and resolves safety and soundness issues, promulgates regulations to enhance the safety and soundness of the FHLBanks, monitors the FHLBanks' activities to serve the nation's housing finance and community investment needs, and aligns the agency's human capital and information technology initiatives to the Finance Board's mission, goals, and outcomes.

The tables below show that the agency continues to allocate the preponderance of available resources -- in both full-time equivalents and budgeted dollars -- to Strategic Goal 1, which reflects the primary duty of the Finance Board.

STRATEGIC GOAL 1				
THE FEDERAL HOME LOAN BANKS OPERATE SAFELY AND SOUNDLY				
Summary	FY2006 Actual	FY2007 Actual	FY2008	
			Budget	Change from FY2007
Program FTE	86.4	87.8	95.1	6.5%
Infrastructure & Support FTE	20.2	20.6	23.8	12.8%
Total FTE	106.6	108.4	118.9	7.7%
Program Expenses (\$M)	\$19.6	\$21.7	\$24.6	13.4%
Infrastructure & Support Expenses	\$4.6	\$5.1	\$6.2	19.2%
Total Budget	\$24.2	\$26.8	\$30.8	14.5%

STRATEGIC GOAL 2				
THE AFFORDABLE HOUSING AND COMMUNITY INVESTMENT PROGRAMS OF THE FEDERAL HOME LOAN BANKS OPERATE EFFECTIVELY AND EFFICIENTLY				
Summary	FY2006 Actual	FY2007 Actual	FY2008	
			Budget	Change from FY2007
Program FTE	21.0	20.1	24.5	9.6%
Infrastructure & Support FTE	4.9	4.7	6.1	17.3%
Total FTE	25.9	25.1	30.6	12.9%
Program Expenses (\$M)	\$4.8	\$5.3	\$6.3	18.9%
Infrastructure & Support Expenses	\$1.1	\$1.2	\$1.6	23.1%
Total Budget	\$5.9	\$6.5	\$7.9	19.7%

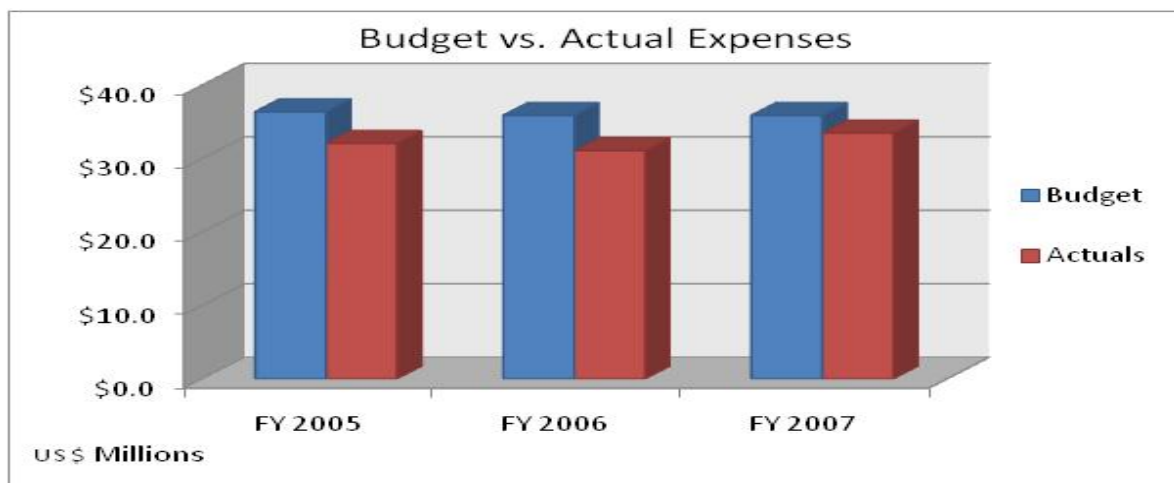
FINANCIAL PERFORMANCE OVERVIEW

As of September 30, 2007, the financial condition of the Finance Board was sound. There are sufficient funds to meet program needs and adequate controls in place to ensure that obligations do not exceed budget authority.

FINANCIAL HIGHLIGHTS

The Finance Board draws its financial resources from assessments levied upon the 12 FHLBanks. It receives no appropriations, and its funds are not Government funds or appropriated monies, or subject to appropriations.

The Finance Board’s budget for FY2007 was approximately \$35.9 million with 143.5 full-time equivalent budgeted staff. The FY2007 budget represented a decrease from FY2006 budget authority of \$21,505.



Actual expenditures in FY2007 were \$33.3 million with 133.5 full-time equivalent staff. As in the past, in FY2007, approximately 80 percent of the agency’s budget was allocated to supervision of the FHLBanks.

Financial Statement Key Comparison of FY2007 to FY2006

In US \$ millions	2007	2006
Total Assets	\$7.93	\$10.47
Total Liabilities	\$4.32	\$3.47
Total Net Position	\$3.60	\$7.00
Net Cost of Operations	\$4.46	\$0.62
Total Budgetary Resources	\$36.44	\$36.19

FINANCIAL STATEMENT MAJOR CHANGES

Major changes in the financial operations from FY2006 to FY2007 were caused by an increase in overall expenditures. This increase from FY2006 expenditures included the hiring of additional staff, an increase in the use of outside contractors, and net rent expenses. FY2006 net rent expenses were lower due to the application of tenant allowance to gross rent expenses. These higher expenditures are reflected in the increase in the Net Cost of Operations from FY2006 to FY2007.

The principal financial statements have been prepared to report the financial position and results of operations of the entity, pursuant to the requirements of 31 U.S.C. § 3515(b). While the statements have been prepared from the books and records of the Finance Board in accordance with GAAP for Federal entities and the formats prescribed by OMB, the statements are in addition to the financial reports used to monitor and control budgetary resources that are prepared from the same books and records.

MANAGEMENT ASSURANCES

The Finance Board provides reasonable assurance that its systems of internal accounting and administrative control fully comply with the requirements of the Federal Managers' Financial Integrity Act of 1982 (FMFIA) and OMB Circular A-123 (rev. December 21, 2004). The Finance Board provides this statement of reasonable assurance that the agency's management accountability and internal controls are adequate and effective, and there are no material weaknesses to report. The objectives of the system of internal control of the Finance Board are to provide reasonable assurance that:

- Programs achieve their intended results;
- Financial reporting is reliable;
- Resources are used consistent with the agency mission;
- Programs and resources are protected from waste, fraud, and mismanagement;
- Laws and regulations are followed; and
- Reliable and timely information is obtained, maintained, reported, and used for decision making.

The concept of reasonable assurance recognizes that the cost of management control should not exceed the benefits expected to be gained, and that the benefits consist of reductions in the risks of failing to achieve the stated objectives. Estimates and judgments are required to assess the expected benefits and related costs of control procedures. Furthermore, errors or irregularities may occur and not be detected because of inherent limitations in any system of management accountability and control, including those limitations resulting from resource constraints and other factors. The statement of assurance and determination are based on the following:

- An independent outside audit of the Finance Board's financial statements, which provided an unqualified opinion and found no weaknesses involving the Finance Board's internal control structure determined to be material.

- An internal evaluation of the internal controls covering the period from October 1, 2006, through September 30, 2007, was completed by the agency's senior program management and reviewed by the Office of the Inspector General. The evaluation found no material weaknesses and concluded that the Finance Board's internal controls are achieving their intended objectives.

The Finance Board is committed to a strong internal control program. The agency employs sound financial management techniques, has developed oversight procedures, and emphasizes the importance of a strong risk management and internal control program to meet its statutory, regulatory, and fiduciary responsibilities.

Since July 2005, the Finance Board outsourced the Finance Board accounting processes and related financial systems with the Bureau of Public Debt, an OMB designated Center of Excellence. The Bureau of Public Debt's financial management system was certified by the Financial Systems Integration Office and conforms to applicable accounting principles, standards, and other related requirements. In addition, the Finance Board's financial management system is integrated with the agency's travel and payroll system to maintain data integrity and improve process efficiencies.

PROGRAM PERFORMANCE

MEASURING AND REPORTING PERFORMANCE

This section presents information on the Finance Board's FY2007 key initiatives, major accomplishments, outcomes for established goals and measures, and evaluation results from completed studies.

PERFORMANCE MEASUREMENT SYSTEM

The Finance Board's planning, budgeting, and performance management process sets the strategic direction, determines planned activities and resources, measures and monitors performance throughout the year, and performs an annual performance assessment. These components reflect a continuous cycle of performance management centered on outcomes. The agency uses annual performance assessments to analyze performance and improve effectiveness and efficiency.

The Finance Board completed a triennial update of its Strategic Plan and review of its performance measures in 2006. The Finance Board continually seeks effective means to measure, report, and ultimately improve its performance. The update of the Strategic Plan for FY2007-2012 provided an opportunity to develop and implement effective practices in performance measurement, reporting, and management.

ALIGNING RESOURCES TO GOALS

Collectively, the outcome-based performance goals are the key indicators for successful progress in achieving the agency's strategic goals. The Finance Board plans, manages, and monitors programs and activities based on contributions to the achievement of these goals with the safety and soundness of the FHLBank System as the primary consideration. Ongoing program evaluations identify Finance Board success in achieving goals and indicate if revised or new initiatives are appropriate.

GOALS, OUTCOMES AND ANNUAL PERFORMANCE MEASURES

For each strategic goal, the agency established strategic outcomes that it expects to achieve and annual performance goals to provide indicators of progress by the Finance Board and the FHLBanks. Finally, in recognition of the fact that the goals the Finance Board set depend not only on the actions of the Finance Board but also on the actions of each of the FHLBanks, the Finance Board has adopted annual performance measures for Finance Board actions to ensure that the agency is doing the most it can to ensure that it meets the strategic goals and outcomes. The relationship between strategic goals, outcomes, annual performance goals, and measures is depicted on page 8 of this report.

STRATEGIC GOAL 1

THE FEDERAL HOME LOAN BANKS OPERATE SAFELY AND SOUNDLY

OUTCOMES

The following strategic outcomes serve as indicators of the degree to which the FHLBanks operate safely and soundly. To the extent that the FHLBanks are able to identify and manage risk, remain adequately capitalized, and raise funds in the capital markets, they are more likely to operate safely and soundly.

STRATEGIC OUTCOME 1: THE FHLBANKS EFFECTIVELY IDENTIFY AND MANAGE RISK.

2003	2004	2005	2006	2007
Achieved	Achieved	Achieved	Achieved	Achieved

The Finance Board has a risk-based supervisory program that focuses on programs, activities, and operations that present the highest risk to the safety and soundness of the FHLBanks. The following processes are central to the agency's application of a risk-based supervisory approach: (1) identification of market, credit, and operational risks; (2) use of common methods of evaluation to measure these risks; and (3) assessment of governance, *e.g.*, the policies, systems, and processes employed by each FHLBank and the Office of Finance in managing existing and prospective levels of risk.

STRATEGIC OUTCOME 2: THE FHLBANKS REMAIN ADEQUATELY CAPITALIZED AND ABLE TO RAISE FUNDS IN THE CAPITAL MARKETS.

2003	2004	2005	2006	2007
Achieved	Achieved	Achieved	Achieved	Achieved

By regulation the FHLBanks are required to establish risk-based capital structures that address minimum capital standards and establish the amount of FHLBank stock members must hold. Eleven of the 12 FHLBanks have implemented their Finance Board approved capital structure plans. In FY2007, the Finance Board approved two capital plan amendments submitted by two FHLBanks.

STRATEGIC GOAL 1- ANNUAL PERFORMANCE MEASURES

ANNUAL PERFORMANCE MEASURE 1: CONDUCT ALL SAFETY AND SOUNDNESS ACTIVITIES, INCLUDING ANNUAL EXAMINATIONS, QUARTERLY VISITATIONS, AND OFF-SITE MONITORING. BASIS.

2003	2004	2005	2006	2007
Achieved	Achieved	Achieved	Achieved	Achieved

DESCRIPTION: The FHLBanks provide wholesale credit to members and certain nonmembers for mortgage lending and related activities such as advances and mortgage purchase programs. As a result of these activities, the FHLBanks assume market, credit, and operational risks. The FHLBanks must evaluate and manage these varied and complex risks in accordance with their condition and earnings. The Finance Board’s supervisory program evaluates and monitors whether the risk management processes at each FHLBank effectively reflect and control the level of risk undertaken.

RESULTS: The Finance Board completed on-site safety and soundness examinations at all 12 FHLBanks using the FHLBank (Examination) Risk Rating System implemented in FY2007. Using this system, the Finance Board assigned each FHLBank a composite rating based on evaluation of various aspects of its operations. This rating is based upon the level of credit, market, and operational risk undertaken, the adequacy of the FHLBank’s risk management practices, its financial condition and operating performance, the adequacy of its capitalization, the quality of its corporate governance, and the administration of its affordable housing and community investment programs.

STRATEGIC GOAL 1- ANNUAL PERFORMANCE MEASURES

ANNUAL PERFORMANCE MEASURE 2: REVIEW SAFETY AND SOUNDNESS EXAMINATION FINDINGS WITH THE FHLBANKS SEMI-ANNUALLY TO ENSURE THE FHLBANKS ARE MAKING PROGRESS TO REMEDY IDENTIFIED SHORTCOMINGS.

2003	2004	2005	2006	2007
New Metric				Achieved

DESCRIPTION: Finance Board staff monitors the FHLBanks on an ongoing basis through the analysis of CRS data, audited financial statements, strategic business plans, and other reports. It monitors FHLBank operations, financial condition, and performance, legal compliance, and actions taken in response to previously identified deficiencies through off-site monitoring and system-wide or “horizontal” reviews that focus on a specific FHLBank activity, function, or program.

RESULTS: The agency strengthened its supervisory program through the implementation of risk-based examinations and with additional monitoring programs and tools. Under this redesign, the examination team develops the supervisory strategy immediately after finalizing an examination to ensure that salient matters are addressed in a timely manner. In addition, Finance Board financial analysts and economists analyze the results of safety and soundness examinations by evaluating the quality of risk modeling at the FHLBanks and analyzing the financial condition, performance, and systemic trends affecting the FHLBanks and FHLBank System. In August 2007, in response to financial market difficulties stemming from the subprime and non-traditional loan segments, the Finance Board started weekly monitoring of trends at the FHLBanks, particularly their advance volumes.

In response to emerging issues in the mortgage industry, the Finance Board conducted a survey of the FHLBanks to assess their exposures to subprime and nontraditional mortgage loans. Survey results indicated that the FHLBanks are able to reasonably estimate their exposures and that the level of those exposures is manageable.

In FY2007, the Finance Board amended and terminated outstanding formal agreements and issued the first cease and desist order (by consent of the board of directors of the FHLBank of Chicago) in the Finance Board’s history.

STRATEGIC GOAL 1- ANNUAL PERFORMANCE MEASURES

ANNUAL PERFORMANCE MEASURE 3: CONDUCT ON-SITE EXAMINATION OF THE OFFICE OF FINANCE AND REVIEW ANNUAL AND QUARTERLY COMBINED STATEMENTS ISSUED BY THE OFFICE OF FINANCE FOR COMPLIANCE WITH DISCLOSURE REQUIREMENTS.

2003	2004	2005	2006	2007
New Metric				Achieved

DESCRIPTION: The Finance Board conducts an annual on-site examination of the Office of Finance to (1) follow up on issues identified through pre-examination analysis and planning; (2) test systems, controls, and reports for adequacy and accuracy, including the internal audit function; (3) assess the risk profile and operational soundness; (4) identify issues that may affect the risk or operating profile; (5) evaluate the quality of corporate governance; and (6) test for compliance with laws, regulations, and policies, including sales suitability practices by participating underwriters and broker-dealers.

RESULTS: The Finance Board completed an on-site examination of the Office of Finance, assigning a composite rating based on the risk rating system implemented in FY2007. In addition, the Finance Board reviewed each of the FHLBank System's combined financial statements, which are prepared by the Office of Finance, both for the 2005 and 2006 reporting periods. These reviews provide the Finance Board with information related to supervisory programs that could affect the scope of examinations and other supervisory actions.

In November 2005, the Office of Finance issued an audited 2005 annual combined financial report, thereby making their annual filings current for the first time since mid-2004. Subsequently, the Office of Finance issued the 2006 annual combined financial report on time, and has resumed timely filing. The Finance Board reviewed and provided comments to the Office of Finance on both of these reports. Final comments on the 2006 report were issued in October 2007.

STRATEGIC GOAL 2
THE FEDERAL HOME LOAN BANKS' AFFORDABLE HOUSING AND
COMMUNITY INVESTMENT PROGRAMS OPERATE
EFFECTIVELY AND EFFICIENTLY

OUTCOMES

STRATEGIC OUTCOME 1: THE FHLBANKS FOSTER THE DEVELOPMENT OF OWNER-OCCUPIED AND AFFORDABLE RENTAL HOUSING FOR ELIGIBLE VERY LOW-, LOW-, AND MODERATE-INCOME HOUSEHOLDS.

2003	2004	2005	2006	2007
Achieved	Achieved	Achieved	Achieved	Achieved

Congress established the FHLBank System in 1932 to restore confidence in the nation's financial institutions and to improve the supply of funds to local lenders to finance loans for home purchases. In 1989, Congress established the AHP and CIP through which the FHLBanks provide funding to support the affordable housing and community investment activities of their members.

The AHP subsidizes the cost of affordable owner-occupied and rental housing. The subsidy may be in the form of a grant or a below-cost or subsidized interest rate on an FHLBank advance to a member. The Bank Act requires each FHLBank to contribute at least 10 percent of its net earnings from the previous year to the AHP, subject to a minimum annual combined contribution by all 12 FHLBanks of \$100 million.

STRATEGIC GOAL 2 – ANNUAL PERFORMANCE MEASURES

ANNUAL PERFORMANCE MEASURE 1: CONDUCT ALL AFFORDABLE HOUSING ACTIVITIES, INCLUDING ANNUAL EXAMINATIONS AND OFF-SITE MONITORING.

2003	2004	2005	2006	2007
New Metric				Achieved

DESCRIPTION: The Bank Act requires each FHLBank to establish an AHP, the purpose of which is to enable members to provide long-term subsidized financing for very-low, low- and moderate-income, owner-occupied and affordable housing. The Finance Board supports the Bank Act's affordable housing and community investment objectives by maintaining an effective program of annual on-site examinations for the AHP, CIP, and, as applicable, other CICA programs.

RESULTS: In FY2007, the Finance Board updated and enhanced its collection of AHP data from the 12 FHLBanks, monitored the level of AHP awards at the 12 FHLBanks, reviewed the Advisory Committee reports and analyses of the low- and moderate-income housing and community lending activity of the 12 FHLBanks, and conducted examinations at 11 of the 12 FHLBanks. The AHP examination of the 12th FHLBank was deferred in order to focus examination resources on areas of heightened supervisory concern. At the end of each examination, the Finance Board assigned a composite rating based on the FHLBank (Examination) Risk Rating System the Finance Board implemented in FY2007. Under this System, each FHLBank is assigned a composite rating based on evaluation of various aspects of its operations including analysis of the overall condition and effectiveness of its AHP activities.

In FY2007, the Office of Supervision conducted AHP training as part of its goal to improve the supervision of the FHLBanks’ AHP and community investment activities through more transparent, consistent, and better documented processes. In particular, the supervisory training was developed to give AHP examiners the tools to review the AHP implementation plans as part of their overall review of the program at each FHLBank. The implementation plan is the pivotal document ensuring that the FHLBanks operate a compliant and effective AHP. As such, a key element of the examiner’s job is to be able to perform a reasonably comprehensive assessment of the implementation plan.

The agency uses the AHP data collection system to conduct off-site monitoring of AHP activities; however, until recently, the system had serious limitations. In FY2006, the agency adopted a new AHP data collection system, which was incorporated into the agency’s Data Reporting Manual. In FY2007, the agency collected reliable data in the new AHP Competitive Program database, as well as the aggregate AHP and CICA databases. In FY2008, the agency will begin to collect data for the AHP set-aside program and the CICA member-level projects.

STRATEGIC GOAL 2 – ANNUAL PERFORMANCE MEASURES

ANNUAL PERFORMANCE MEASURE 2: REVIEW AFFORDABLE HOUSING AND COMMUNITY INVESTMENT EXAMINATION FINDINGS WITH THE FHLBANKS SEMI-ANNUALLY TO ENSURE THE FHLBANKS ARE MAKING PROGRESS TO REMEDY IDENTIFIED SHORTCOMINGS.

2003	2004	2005	2006	2007
New Metric				Achieved

DESCRIPTION: The Finance Board’s FY2007 operating budget included \$6.6 million to perform the AHP and community investment supervisory program. The examiners conducted on-site reviews of the AHP, CIP, and other CICA programs. Examiners reviewed policies, procedures, and controls that address board of directors and management oversight, the subsidy award process, uses of funds, and recipient eligibility.

RESULTS: The AHP examiners resolved concerns identified during the examination of the AHP, CIP, and other CICA programs through discussion with FHLBank management and the board of directors. On a regular basis, the agency will monitor an FHLBank’s progress in resolving such concerns and will confirm that the issues have been corrected. Where warranted, the Finance Board can require an FHLBank to take additional remedial action, such as suspending or debarring a member, project sponsor, or project owner from participation in the program. In the case of an FHLBank’s CIP and other CICA programs, an examiner may require an FHLBank to reclassify advances not adhering to applicable statutory and regulatory requirements.

STRATEGIC GOAL 2 – ANNUAL PERFORMANCE MEASURES

ANNUAL PERFORMANCE MEASURE 3: USE EXAMINATIONS TO REVIEW PROGRAM EFFECTIVENESS AS WELL AS COMPLIANCE WITH THE BANK ACT, FINANCE BOARD REGULATIONS, AND FHLBANK POLICIES.

2003	2004	2005	2006	2007
New Metric				Achieved

DESCRIPTION: The Finance Board remains strongly committed to ensuring that the FHLBanks carry out effective affordable housing and community investment programs, and will continue to monitor program effectiveness in their supervision of the affordable housing and community investment programs.

RESULTS: In 2007, the Finance Board implemented AHP, CIP, and CICA regulatory initiatives. These initiatives are designed to enhance the AHP, CIP, and CICA program supervisory function. The Finance Board approved amendments to the AHP regulation in September 2006. The revised regulation removed certain prescriptive requirements, clarified specific operational requirements, provided additional discretionary authority in certain areas, and streamlined and reorganized the AHP regulation. The rule was became effective January 1, 2007.

During FY2007, AHP policy analysts began organizing, cataloging, and reassessing policy determinations rendered over the years. As these reviews are completed, relevant documents will be posted on the agency’s computer network to be shared with examiners as a pertinent reference tool to enhance their knowledge of the AHP regulation and their ability to perform their supervisory responsibilities.

In FY2007, the Finance Board completed a preliminary draft of the AHP manual and related work programs. The manual reflects the agency’s risk-focused and performance-based approaches to on-site reviews of the AHP, CIP, and CICA programs. The manual explains examination objectives and procedures, addresses subjects that examiners most often encounter, provides guidance on examination workpaper requirements, and promotes examination consistency.

PROGRAM EVALUATION

The Finance Board uses program evaluations to improve and enhance its mission performance and support strategic and performance planning efforts. These evaluations take many forms, and are performed by organizations both inside and outside the agency. Staff members evaluate and implement recommendations, as appropriate. The principal evaluations include:

SUPERVISORY PROGRAM

Government Accountability Office Evaluations: The Government Accountability Office conducts program- and program-support related evaluations of the agency's supervisory program.

Office of Inspector General Evaluations: The Office of Inspector General evaluates the agency's supervisory program and program support operations.

Quality Assurance: The Office of Supervision established a Quality Assurance Unit to provide recommendations to facilitate more efficient and effective operations. The Quality Assurance Unit will conduct reviews of all Office of Supervision programs and may include ongoing evaluation of work processes, policy development, and decision-making processes.

FINANCIAL MANAGEMENT

Financial Audits: Annually, the Office of Inspector General contracts with a public accounting firm to audit the Finance Board's financial statements. This audit is conducted in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in Government Auditing Standards.

INFORMATION TECHNOLOGY

Federal Information Security Management Act: The Office of Inspector General annually reviews and evaluates the agency's information technology systems for compliance with the Act. This includes evaluating information technology controls for financial management systems.

Network Penetration: The Finance Board annually contracts with an outside company of security experts to perform network penetration testing of our information technology systems.

Customer Satisfaction Survey: The Finance Board conducts an annual survey to obtain opinions on the quality of the agency's information technology products and services. This provides a better understanding of user needs and results in improved service.

HUMAN CAPITAL MANAGEMENT

Human Capital Management Survey: The Finance Board participates in the Office of Personnel Management's Human Capital Management Survey to give employees the opportunity to evaluate how well their agencies are managing human capital. . The Federal Human Capital Survey results provide valuable insight into the challenges agency leaders face in ensuring the Finance Board improves the quality of leadership, sustains a results-oriented performance culture, and promotes continuous workforce improvement.

Training and Development Program: The Finance Board has approved funding to hire a Training Officer in FY 2008. In today's dynamic working environment, it is imperative that our employees have the necessary skills and tools needed to perform their jobs. The agency's training officer will be able to assess the knowledge, skills and abilities needed by Finance Board employees and develop a program designed to meet those needs.

Workplace Improvement Committee: Representatives from offices within the Finance Board meet to identify and pursue improvements to the work environment.

Equal Employment Opportunity: The Finance Board is committed to equal employment opportunity and the implementation of a strong program to promote employment and advancement opportunities without regard to race, sex, sexual orientation, religion, color, national origin, age, or disability. In addition, the Finance Board is committed to continuing to take advantage of employment programs that integrate veterans, disabled, and other populations into the public-sector workforce. As required by the Notification and Federal Anti-Discrimination and Retaliation Act of 2002, the Finance Board provided training designed to instruct employees about their rights and remedies available under the antidiscrimination, retaliation, and whistleblower protection laws. The Finance Board completed this requirement in FY2007 with 100 percent participation. The training was conducted via internet using an interactive online course that consisted of a series of audio-visual scenarios.



Federal Housing Finance Board

**FEDERAL HOUSING FINANCE BOARD
FINANCIAL STATEMENTS
AND
INDEPENDENT AUDITOR'S REPORT**

**FOR THE FISCAL YEARS ENDED
SEPTEMBER 30, 2007 AND 2006**

REPORT NUMBER: 07-A-06-OM

Prepared By:

**Brown & Company CPAs, PLLC
9200 Basil Court, Suite 400
Largo, Maryland 20774
November 15, 2007
Revised**

BROWN & COMPANY CPAS, PLLC



BROWN & COMPANY CPAs, PLLC

CERTIFIED PUBLIC ACCOUNTANTS AND MANAGEMENT CONSULTANTS

INDEPENDENT AUDITOR'S REPORT ON THE FINANCIAL STATEMENTS

Office of the Inspector General
Board of Directors
Federal Housing Finance Board
Washington, D.C.

We have audited the accompanying balance sheet of the Federal Housing Finance Board (the Finance Board) as of September 30, 2007 and the related statements of net cost, changes in net position, and budgetary resources for the year then ended. We also audited the balance sheet as of September 30, 2006 and the related statements of revenue, expenses and changes in net position and cash flows for the year then ended. These financial statements are the responsibility of the Finance Board's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in U.S. Government Auditing Standards, issued by the Comptroller General of the United States; and, Office of Management and Budget (OMB) Bulletin No. 07-04, *Audit Requirement for Federal Financial Statements*. Those standards and OMB Bulletin No. 07-04 require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Federal Housing Finance Board as of September 30, 2007 and 2006, and its net costs, changes in net position, and budgetary resources for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with U.S. Government Auditing Standards and OMB Bulletin No. 07-04, we have also issued a report dated November 15, 2007 on our consideration of the Finance Board's internal control over financial reporting and its compliance with provisions of laws and regulations. Those reports are an integral part of an audit performed in accordance with U.S. Government Auditing Standards and should be read in conjunction with this report in considering the results of our audit.

The information in "Management's Discussion & Analysis" is presented for the purpose of additional analysis and is required by OMB Circular No. A-136, revised *Financial Reporting Requirements*. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and, accordingly, express no opinion on it.

Largo, Maryland
November 15, 2007

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CERTIFIED PUBLIC ACCOUNTANTS AND MANAGEMENT CONSULTANTS

**INDEPENDENT AUDITORS REPORT ON
INTERNAL CONTROL OVER FINANCIAL REPORTING**

Office of Inspector General
Board of Directors
Federal Housing Finance Board
Washington, D.C.

We have audited the financial statements of the Federal Housing Finance Board (the Finance Board) as of and for the year ended September 30, 2007 and have issued our report thereon dated November 15, 2007. We conducted our audit in accordance with auditing standards generally accepted in the United States of America; and the standards applicable to financial audits contained in U.S Government Auditing Standards, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*.

In planning and performing our audit, we considered the Finance Board's internal control over financial reporting by obtaining an understanding of the Finance Board's internal control, determined whether internal controls had been placed in operation, assessed control risk, and performed tests of controls in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements. We limited our internal control testing to those controls necessary to achieve the objectives described in OMB Bulletin No. 07-04. We did not test all internal controls relevant to operating objectives as broadly defined by the Federal Managers' Financial Integrity Act of 1982, such as those controls relevant to ensuring efficient operations. The objective of our audit was not to provide an opinion on internal control and therefore, we do not express an opinion on internal control.

Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be reportable conditions. Under standards issued by the American Institute of Certified Public Accountants and OMB Bulletin No. 07-04, Significant Deficiency is a deficiency in internal control, or a combination of deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected. Material Weakness is a significant deficiency, or combination of significant deficiencies, that result in a more than remote likelihood that a material misstatement of the financial statements will not be prevented or detected. Because of inherent limitations in internal controls, misstatements, losses, or non-compliance may nevertheless occur and not be detected. However, we noted no matters involving the internal control and its operation that we considered to be material weaknesses as defined above.

In addition, with respect to internal control objective related to the performance measures included in the "Management's Discussion & Analysis," we obtained an understanding of the design of internal controls relating to the existence and completeness assertions, and determined whether they have been placed in operation as required by OMB Bulletin No. 07-04. Our procedures were not designed to


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provide opinion on internal control over reported performance measures, and, accordingly, we do not express an opinion on such controls.

This report is intended solely for the information and use of the management of the Federal Housing Finance Board, OMB, and Congress, and is not intended to be and should not be used by anyone other than these specified parties.



Largo, Maryland
November 15, 2007



BROWN & COMPANY CPAs, PLLC

CERTIFIED PUBLIC ACCOUNTANTS AND MANAGEMENT CONSULTANTS

**INDEPENDENT AUDITOR'S REPORT ON
COMPLIANCE WITH LAWS AND REGULATIONS**

Office of the Inspector General
Board of Directors
Federal Housing Finance Board
Washington, D.C.

We have audited the financial statements of the Federal Housing Finance Board (the Finance Board) as of and for the year ended September 30, 2007, and have issued our report thereon dated November 15, 2007. We conducted our audit in accordance with auditing standards generally accepted in the United States of America, and the standards applicable to financial audits contained in U.S. Government Auditing Standards, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*.

The management of the Finance Board is responsible for complying with laws and regulations applicable to the Finance Board. As part of obtaining reasonable assurance about whether the Finance Board's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of financial statement amounts, and certain other laws and regulations specified in OMB Bulletin No. 07-04. We limited our tests of compliance to these provisions and we did not test compliance with all laws and regulations applicable to the Finance Board.

The results of our tests of compliance disclosed no reportable instances of noncompliance with other laws and regulations discussed in the preceding paragraph that are required to be reported under U.S. Government Auditing Standards or OMB Bulletin No. 07-04.

Providing an opinion on compliance with certain provisions of laws and regulations was not an objective of our audit, and, accordingly, we do not express such an opinion. However, we noted no noncompliance with laws and regulations, which could have a direct and material effect on the determination of financial statement amounts.

This report is intended solely for the information and use of the management of the Finance Board, OMB, and Congress, and is not intended to be and should not be used by anyone other than these specified parties.

Largo, Maryland
November 15, 2007

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FEDERAL HOUSING FINANCE BOARD
BALANCE SHEET
For the Fiscal Years Ended September 30, 2007 and 2006
(In Dollars)

	<u>2007</u>	<u>2006</u>
Assets:		
Intragovernmental:		
Fund Balance With Treasury (Note 2)	\$ 6,727,173	\$ 8,942,840
Total Intragovernmental	6,727,173	8,942,840
Accounts Receivable (Note 1)	2,189	3,358
General Property, Plant and Equipment, Net (Note 3)	1,186,745	1,498,423
Other	<u>10,671</u>	<u>29,030</u>
Total Assets	<u>\$ 7,926,778</u>	<u>\$ 10,473,651</u>
Liabilities:		
Intragovernmental:		
Accounts Payable (Note 4)	\$ 225,033	\$ 65,298
Other (Note 4)	<u>134,627</u>	<u>128,794</u>
Total Intragovernmental	359,660	194,092
Accounts Payable (Note 4)	1,459,183	778,832
Other (Note 4)	<u>2,503,516</u>	<u>2,498,611</u>
Total liabilities	<u>\$ 4,322,359</u>	<u>\$ 3,471,535</u>
Net Position:		
Cumulative Results of Operations - Other Funds	<u>\$ 3,604,419</u>	<u>\$ 7,002,116</u>
Total Net Position	<u>3,604,419</u>	<u>7,002,116</u>
Total Liabilities and Net Position	<u>\$ 7,926,778</u>	<u>\$ 10,473,651</u>

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

FEDERAL HOUSING FINANCE BOARD
STATEMENT OF NET COST
For the Fiscal Years Ended September 30, 2007 and 2006
(In Dollars)

	2007	2006
Program Costs:		
Review of Federal Home Loan Banks		
Gross Costs (Note 6)	\$ 35,568,057	\$ 32,200,748
Less: Earned Revenue	31,111,239	31,582,813
Net Program Costs	4,456,818	617,935
 Net Cost of Operations	 \$ 4,456,818	 \$ 617,935

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

FEDERAL HOUSING FINANCE BOARD
STATEMENT OF CHANGES IN NET POSITION
For the Fiscal Years Ended September 30, 2007 and 2006
(In Dollars)

	2007	2006
Cumulative Results of Operations:		
Beginning Balances	\$ 7,002,116	\$ 6,628,175
Beginning Balances, as Adjusted	\$ 7,002,116	\$ 6,628,175
Other Financing Sources (Non-Exchange):		
Imputed Financing Sources (Note 7)	\$ 1,059,121	\$ 991,876
Total Financing Sources	1,059,121	991,876
Net Cost of Operations	4,456,818	617,935
Net Changes	\$ (3,397,697)	\$ 373,941
Cumulative Results of Operations	3,604,419	7,002,116
Net Position	\$ 3,604,419	\$ 7,002,116

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

FEDERAL HOUSING FINANCE BOARD
STATEMENT OF BUDGETARY RESOURCES
For the Fiscal Years Ended September 30, 2007 and 2006
(In Dollars)

	2007	2006
Budgetary Resources:		
Unobligated Balance Brought Forward, October 1:	\$ 4,742,569	\$ 4,307,516
Recoveries of Prior Year Unpaid Obligations	589,351	299,492
Budget Authority –Collected	31,111,239	31,583,288
Total Budgetary Resources	\$ 36,443,159	\$ 36,190,296
 Status of Budgetary Resources:		
Obligations Incurred		
Reimbursable	\$ 34,292,116	\$ 31,447,727
Unobligated Balance		
Exempt From Apportionment	2,151,043	4,742,569
Total Status of Budgetary Resources	\$ 36,443,159	\$ 36,190,296
 Change in Obligated Balance:		
Obligated Balance, Net		
Unpaid Obligations, Brought Forward, October 1	\$ 4,200,271	\$ 3,683,944
Obligations Incurred Net	34,292,116	31,447,727
Less: Gross Outlays	33,326,906	30,631,908
Less: Recoveries of Prior Year Unpaid		
Obligations, Actual	589,351	299,492
Total, Unpaid Obligated Balance, Net, End of Period	\$ 4,576,130	\$ 4,200,271
 Net Outlays:		
Net Outlays:		
Gross Outlays	\$ 33,326,906	\$ 30,631,908
Less: Offsetting Collections	31,111,239	31,583,288
Net Outlays	\$ 2,215,667	\$ (951,380)

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

**FEDERAL HOUSING FINANCE BOARD
NOTES TO THE FINANCIAL STATEMENTS
FOR THE FISCAL YEARS ENDED SEPTEMBER 30, 2007 and 2006**

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Basis of Presentation

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 the Federal Housing Finance Board (Finance Board). The statements are a requirement of the Chief Financial Officers Act of 1990, the Government Management Reform Act of 1994, the Accountability of Tax Dollars Act of 2002 and the Office of Management and Budget (OMB) Bulletin Number 07-04, *Audit Requirements for Federal Financial Statements*. They have been prepared from, and are fully supported by, the books and records of the Finance Board in accordance with the hierarchy of accounting principles generally accepted in the United States of America, standards approved by the principals of the Federal Accounting Standards Advisory Board (FASAB), OMB Circular No. A-136, *Financial Reporting Requirements* and the Finance Board accounting policies which are summarized in this note. These statements, with the exception of the Statement of Budgetary Resources, are different from financial management reports, which are also prepared pursuant to OMB directives that are used to monitor and control the Finance Board's use of budgetary resources.

The statements consist of the Balance Sheet, Statement of Net Cost, Statement of Changes in Net Position, and Statement of Budgetary Resources. In accordance with OMB Circular No. A-136, the financial statements and associated notes are presented on a comparative basis. Unless specified otherwise, all dollar amounts are presented in dollars.

B. Reporting Entity

The Finance Board is an independent non-appropriated funded Agency in the Executive Branch. The Finance Board ensures that Federal Home Loan Banks, which are privately capitalized, government-sponsored enterprises, operate in a safe and sound manner, carry out the housing and community development finance mission, and remain adequately capitalized and able to raise funds in the capital markets. The Federal Home Loan Bank System raises its money through the Office of Finance that acts as the central debt issuance facility for all 12 Federal Home Loan Banks.

The Federal Home Loan Bank System was created in 1932 to promote home ownership and a strong home-finance industry. It is a network of 12 district banks that provide lending, deposit, and other services to mortgage-lending institutions. The members of the Federal Home Loan Bank System originate and hold a significant portion of the nation's home mortgages. Membership includes the thrift institutions, commercial banks, credit unions, and a small number of insurance companies.

Each Federal Home Loan Bank and the Office of Finance operates with its own staff and funding. Accordingly, the accompanying financial statements summarize only the financial activities of the Finance Board.

**FEDERAL HOUSING FINANCE BOARD
NOTES TO THE FINANCIAL STATEMENTS
FOR THE FISCAL YEARS ENDED SEPTEMBER 30, 2007 and 2006**

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The Finance Board is located in Washington, DC, where it operates with a staff of approximately 130 employees under the direction of a five member Board of Directors, four of whom are appointed from the private sector by the President. The fifth is the Secretary of Housing and Urban Development or designee. Operation of the Finance Board is funded by the collection of assessments from each of the Federal Home Loan Banks. These assessments are used to fund the salaries and expenses of staff engaged in supervision and compliance activities, policy development, strategic planning, and administration. These funds are neither appropriated nor subject to apportionment.

C. Basis of Accounting

Transactions are recorded on both an accrual accounting basis, consistent with accounting principles generally accepted in the United States of America, and a budgetary basis. Under the accrual method, revenues are recognized when earned, and expenses are recognized when a liability is incurred, without regard to receipt or disbursement of cash. Budgetary accounting facilitates compliance with legal requirements on the use of federal funds.

D. Revenues & Other Financing Sources

Operating revenues of the Finance Board are obtained through assessments of the 12 Federal Home Loan Banks. The banks are collectively assessed based on amounts needed to fund the Finance Board's annual budget. The agency's Board of Directors, prior to the start of a new fiscal year, approves the budget. Each Federal Home Loan Bank's share is based upon the dollar value of its capital stock relative to the combined dollar value of all Federal Home Loan Banks' capital stock. The Finance Board's expenses are met through assessments paid by the Federal Home Loan Banks, which totaled \$31,109,690 and \$31,224,539 for the fiscal years ended September 30, 2007 and 2006, respectively.

The Finance Board recognizes as an imputed financing source the amount of accrued pension and post-retirement benefit expenses for current employees paid on the Finance Board's behalf by the Office of Personnel Management (OPM).

E. Taxes

The Finance Board, as a federal entity, is not subject to federal, state, or local income taxes, and, accordingly, no provision for income taxes has been recorded in the accompanying financial statements.

F. Fund Balance with Treasury

The U.S. Treasury processes cash receipts and disbursements. Funds held at the Treasury are available to pay agency liabilities. The Finance Board does not maintain cash in commercial bank accounts or foreign currency balances.

Significant receipts are transmitted to this account monthly by the 12 Federal Home Loan Banks which are assessed amounts necessary to cover the Finance Board's expected operating needs for the fiscal year.

**FEDERAL HOUSING FINANCE BOARD
NOTES TO THE FINANCIAL STATEMENTS
FOR THE FISCAL YEARS ENDED SEPTEMBER 30, 2007 and 2006**

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Disbursements are made as necessary to fund the biweekly payroll and administrative costs of the organization. Due to of the nature of the Finance Board's program, disbursements do not vary significantly from month to month.

G. Accounts Receivable

Accounts receivable consists of amounts owed to the Finance Board by other federal agencies and the public. Amounts due from federal agencies are considered fully collectible. Accounts receivable from the public include reimbursements from employees. An allowance for uncollectible accounts receivable from the public is established when either (1) based upon a review of outstanding accounts and the failure of all collection efforts, management determines that collection is unlikely to occur considering the debtor's ability to pay, 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. As of September 30, 2007 and 2006 the balance in accounts receivable from the public was \$2,189 and \$3,358 respectively.

H. Property and Equipment, Net

Equipment acquisitions greater than or equal to \$25,000 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 \$100,000 or more.

Applicable standard governmental guidelines regulate the disposal and convertibility of agency property, plant and equipment. The useful life classifications for capitalized assets are as follows:

<u>Description</u>	<u>Useful Life (years)</u>
Furniture, Fixtures, and Equipment	6
Electronic Data Processing Systems	3
Data Handling Equipment (Excluding computers)	6
Software and Computer Programs	3
Real Property Improvements	30

Leasehold Improvement's useful life is equal to the remaining lease term or the estimated useful life of the improvement, whichever is shorter.

**FEDERAL HOUSING FINANCE BOARD
NOTES TO THE FINANCIAL STATEMENTS
FOR THE FISCAL YEARS ENDED SEPTEMBER 30, 2007 and 2006**

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

I. 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. As of September 30, 2007 and 2006 prepaid expenses were \$10,671 and \$29,030, respectively.

J. Liabilities

Liabilities covered by budgetary or other resources are those liabilities for which funding is available to pay amounts due.

Intragovernmental liabilities are claims against the Finance Board by other federal agencies. Additionally, the Government, acting in its sovereign capacity, can abrogate liabilities.

K. Accounts Payable

Accounts payable consists of amounts owed to other federal agencies and the public.

L. Employee Leave and Benefits

Accrued Leave: Finance Board 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. Senior employees may accrue annual leave consistent with the rules for SES level employees. 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 CSRS plan employees is creditable as additional time in service for the purpose of calculating an employee's retirement annuity. For FERS plan employees, unused sick leave is held indefinitely and may be used if rehired.

Health Benefits and Life Insurance: The Finance Board, through programs established for all agencies by the federal government, offers its employees health and life insurance coverage. The cost of each is shared by the Finance Board and its employees. The Finance Board's fiscal year 2007 contribution to health and life insurance coverage was \$1,022,594. The fiscal year 2006 contribution was \$967,172. In addition, all employees have 1.45% of gross earnings withheld to pay for future Medicare coverage.

M. Accrued Workers' Compensation

A liability is recorded for actual and estimated future payments to be made for workers' compensation pursuant to the Federal Employees' Compensation Act (FECA). The actual costs incurred are reflected as a liability because the Finance Board will reimburse the Department of Labor (DOL) two years after the actual payment of expenses. The liability consists of (1) the net present value of estimated future payments calculated by the DOL, and (2) the unreimbursed cost paid by DOL for compensation to recipients under the FECA.

FEDERAL HOUSING FINANCE BOARD
NOTES TO THE FINANCIAL STATEMENTS
FOR THE FISCAL YEARS ENDED SEPTEMBER 30, 2007 and 2006

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

N. Retirement Plans

Finance Board employees participate in either the Civil Service Retirement System (CSRS) or the Federal Employees' Retirement System (FERS). The employees who participate in CSRS are beneficiaries of Finance Board's matching contribution, equal to 7% of pay, distributed to the employee's annuity account in the Civil Service Retirement and Disability Fund.

FERS went into effect on January 1, 1987. FERS and Social Security automatically cover most employees hired after December 31, 1983. Employees hired prior to January 1, 1984 elected to join either FERS and Social Security, or remain in CSRS. FERS offers a Thrift Savings Plan to which the Finance Board automatically contributes 1% of pay and matches any employee contribution up to an additional 4% of pay. For FERS participants, the Finance Board also contributes the employer's matching share of Social Security.

FERS employees and certain CSRS reinstatement employees are eligible to participate in the Social Security program after retirement. In these instances, the Finance Board remits the employer's share of the required contribution.

The Finance Board recognizes the imputed cost of pension and other retirement benefits during the employees' active years of service. OPM actuaries determine pension cost factors by calculating the value of pension benefits expected to be paid in the future and communicates these factors to the Finance Board for current period expense reporting. OPM also provides information regarding the full cost of health and life insurance benefits. The Finance Board recognized the offsetting revenue as imputed financing sources to the extent these expenses will be paid by OPM.

The Finance board 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 the OPM.

The Finance Board's 401(K) is administered by T. Rowe Price. Eligible employees may contribute up to 10% of salary on a pre-tax basis while the Finance Board will match contributions up to 3% of the employee's salary. Qualified employees may participate in both the Federal Thrift Savings Plan and/or the Finance Board's 401(K) Savings Plan, up to the Internal Revenue Code limitations established for salary deferral and annual additions.

O. Use of Estimates

Management has made certain estimates when reporting assets, liabilities, revenue, and expenses, and in the note disclosures. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**FEDERAL HOUSING FINANCE BOARD
NOTES TO THE FINANCIAL STATEMENTS
FOR THE FISCAL YEARS ENDED SEPTEMBER 30, 2007 and 2006**

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

P. Imputed Costs/Financing Sources

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. The Finance Board recognized imputed costs and financing sources in fiscal years 2007 and 2006 to the extent directed by OMB.

Q. Contingencies

Liabilities are deemed contingent when the existence or amount of the liability cannot be determined with certainty pending the outcome of future events. The Finance Board recognizes contingent liabilities, in the accompanying balance sheet and statement of net cost, when it is both probable and can be reasonably estimated. The Finance Board discloses contingent liabilities in the notes to the financial statements when the conditions for liability recognition are not met or when a loss from the outcome of future events is more than remote.

Equal Employment Opportunity Complaints:

At the Agency: As of the end of the period beginning on October 1, 2006 and ending on October 10, 2007, there was no cases pending before the Finance Board.

At the Equal Employment Opportunity Commission (EEOC): As of the end of the period beginning on October 1, 2006 and ending on October 10, 2007, there was one case pending before the EEOC, Agency Case Number 2006-01. Case Number 2006-01 was filed on October 13, 2005, and remanded to the Finance Board for processing by a decision of the EEOC's Office of Federal Operations dated June 5, 2006. On August 17, 2006, the Finance Board's EEO Director dismissed Case Number 2006-01. The Complainant appealed the dismissal to the EEOC by a form dated August 26, 2006. On September 25, 2006, the Finance Board filed its opposition to the Complainant's appeal of the dismissal and the EEOC has not yet issued a decision. On October 2, 2007, the Finance Board filed a motion to dismiss the appeal based on the Complainant's election to proceed in the U.S. District Court for the District of Columbia. This case has a potential loss ranging from \$0 to \$300,000. An unfavorable outcome is considered highly unlikely.

On June 28, 2007, the EEOC's Office of Federal Operations upheld the decision issued by an EEOC administrative judge granting the Finance Board's motion for summary judgment. On September 24, 2007, the Complainant elected to proceed in the U.S. District Court for the District of Columbia. The EEOC no longer has jurisdiction over this matter.

**FEDERAL HOUSING FINANCE BOARD
NOTES TO THE FINANCIAL STATEMENTS
FOR THE FISCAL YEARS ENDED SEPTEMBER 30, 2007 and 2006**

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

At the United States District Court: As of the end of the period beginning on October 1, 2006 and ending on October 10, 2007, there were two civil actions pending in the U.S. District Court for the District of Columbia, both filed by the same plaintiff who also is the Complainant in the EEOC cases described above. In the first case, on September 26, 2005, the court granted in part and denied in part the Finance Board's motion to dismiss the case. The plaintiff filed the second case on September 24, 2007. Following a status conference on October 1, 2007, the Finance Board anticipates that the cases will be consolidated and that it will file a dispositive motion with regard to all claims that have not already been dismissed. Each case has a potential loss ranging from \$0 to \$300,000. An unfavorable outcome is considered unlikely.

Other Cases: On June 15, 2007, the U.S. Court of Appeals for the District of Columbia Circuit in a per curiam decision dismissed the Petition for Review filed by a former employee of a Federal Home Loan Bank alleging that the Finance Board had an obligation to act on her complaints against the Bank. The appeal period has elapsed.

R. Reclassification

Certain fiscal year 2006 balances have been reclassified, retitled, or combined with other financial statement line items for consistency with current year presentation. Under SFFAS 7, OMB has reclassified the Statement of Financing to be presented in a note as Reconciliation of Net Cost of Operations to Budget.

NOTE 2. FUND BALANCE WITH TREASURY

Fund balance with Treasury account balances as of September 30, 2007 and 2006 were:

Fund Balances:

	<u>2007</u>	<u>2006</u>
Total Other Fund Types	<u>\$6,727,173</u>	<u>\$8,942,840</u>

Status of Fund Balance with Treasury:

	<u>2007</u>	<u>2006</u>
Unobligated Balance - Available	\$2,151,043	\$4,742,569
Obligated Balance Not Yet Disbursed	<u>4,576,130</u>	<u>4,200,271</u>
Total	<u>\$6,727,173</u>	<u>\$8,942,840</u>

FEDERAL HOUSING FINANCE BOARD
NOTES TO THE FINANCIAL STATEMENTS
FOR THE FISCAL YEARS ENDED SEPTEMBER 30, 2007 and 2006

NOTE 3. GENERAL PROPERTY AND EQUIPMENT

Property and equipment account balances as of September 30, 2007 and 2006 were as follows:

Schedule of Property and Equipment as of September 30, 2007

<u>Description</u>	<u>Acquisition Cost</u>	<u>Accumulated Depreciation</u>	<u>Net Book Value</u>
Software	\$ 3,237,769	\$ 2,820,907	\$ 416,862
Furniture & Equipment	2,247,170	1,543,342	703,828
Internal-Use Software In Development	66,055		66,055
Total	<u>\$ 5,550,994</u>	<u>\$ 4,364,249</u>	<u>\$ 1,186,745</u>

Schedule of Property and Equipment as of September 30, 2006

<u>Description</u>	<u>Acquisition Cost</u>	<u>Accumulated Depreciation</u>	<u>Net Book Value</u>
Software	\$ 3,325,582	\$ 3,107,491	\$ 218,091
Furniture & Equipment	2,734,985	1,816,400	918,585
Internal-Use Software In Development	361,747		361,747
Total	<u>\$ 6,422,314</u>	<u>\$ 4,923,891</u>	<u>\$ 1,498,423</u>

NOTE 4. LIABILITIES

The accrued liabilities for the Finance Board are comprised of program expense accruals, payroll accruals, and funded annual leave earned by employees. Program expense accruals represent expenses that were incurred prior to month-end but were not paid. Similarly, payroll accruals represent payroll expenses that were incurred prior to month-end but were not paid.

	<u>2007</u>	<u>2006</u>
Intragovernmental		
Accounts Payable	\$ 225,033	\$ 65,298
Payroll Taxes Payable	134,627	128,794
Total Intragovernmental	<u>359,660</u>	<u>194,092</u>
Accounts Payable	1,459,183	778,832
Accrued Payroll and Benefits	803,187	863,074
Capital Lease Obligations	6,097	10,886
Funded Annual Leave	1,694,232	1,624,651
Total Liabilities	<u>\$ 4,322,359</u>	<u>\$ 3,471,535</u>

All liabilities are current liabilities.

FEDERAL HOUSING FINANCE BOARD
NOTES TO THE FINANCIAL STATEMENTS
FOR THE FISCAL YEARS ENDED SEPTEMBER 30, 2007 and 2006

NOTE 5. LEASES

Capital Leases

The Finance Board leases a copier under a lease-to-own agreement. The lease term is 60 months. The minimum future lease payments and the present value of the net minimum lease payments are as follows:

<u>Fiscal Year</u>	<u>Amount</u>
2008	\$ 5,951
2009	458
Total Future Minimum Lease Payments	<u>6,409</u>
Less: Imputed Interest	312
Present Value of the Net Minimum Lease Payments	<u>6,097</u>
Less: Current Portion	5,642
Lease Obligation – Long Term	<u>\$ 455</u>

Operating Leases

The Finance Board leases office space at 1625 Eye Street, Washington D.C., under a non-cancelable long-term lease that expires on June 30, 2015, and requires monthly payments. Total rental payments for the fiscal years ended September 30, 2007 and 2006 were \$3,290,278 and \$1,601,508, respectively. The rental payments for the fiscal year ending September 30, 2007 were reduced by a tenant improvement allowance in the amount of \$166,453. The minimum future payments at 1625 Eye Street, as required by the lease, are as follows:

<u>Fiscal Year</u>	<u>Amount</u>
2008	3,322,310
2009	3,388,799
2010	3,475,652
2011	3,602,273
2012	3,674,395
Thereafter	<u>10,480,884</u>
Total	<u>\$ 27,944,313</u>

**FEDERAL HOUSING FINANCE BOARD
NOTES TO THE FINANCIAL STATEMENTS
FOR THE FISCAL YEARS ENDED SEPTEMBER 30, 2007 and 2006**

NOTE 6. OPERATING/PROGRAM COSTS

Costs by major budgetary object classification as of September 30, 2007 and 2006 are as follows:

<u>Budgetary Object Classifications</u>	<u>2007</u>	<u>2006</u>
Personnel Compensation	\$17,131,753	\$16,197,400
Personnel Benefits	6,221,904	5,844,193
Benefits to Former Employees	3,231	-
Travel	1,157,875	1,586,637
Transportation	20,456	16,521
Rents, Communication & Utilities	4,006,525	2,415,394
Printing and Reproduction	248,930	64,415
Other Services	6,067,179	4,897,619
Supplies and Materials	258,488	313,086
Equipment	451,716	865,483
Total	<u>\$35,568,057</u>	<u>\$32,200,748</u>

NOTE 7. IMPUTED FINANCING SOURCES

The Finance Board recognizes as imputed financing the amount of accrued pension and post-retirement benefit expenses for current employees. The assets and liabilities associated with such benefits are the responsibility of the administering agency, OPM.

For the fiscal years ended September 30, 2007 and 2006, respectively, imputed financing was \$1,059,121 and \$991,876.

NOTE 8. 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 (SBR) and the actual balances published in the Budget of the United States Government (President's Budget). However, the President's Budget that will include FY07 actual budgetary execution information has not yet been published. The President's Budget is scheduled for publication in February 2008 and can be found at the OMB Web site: <http://www.whitehouse.gov/omb>. The 2008 Budget of the United States Government, with the Actual column completed for 2006, has been reconciled.

**FEDERAL HOUSING FINANCE BOARD
NOTES TO THE FINANCIAL STATEMENTS
FOR THE FISCAL YEARS SEPTEMBER 30, 2007 and 2006**

NOTE 9. UNDELIVERED ORDERS AT THE END OF THE PERIOD

Beginning with FY 2006, the format of the Statement of Budgetary Resources has changed and the amount of the amount of undelivered orders at the end of the period is no longer required to be reported on the face of the statement. Statement of Federal Financial Accounting Standards No. 7, Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting, states that the amount of budgetary resources obligated for undelivered orders at the end of the period should be disclosed. For the fiscal years ended September 30, 2007 and 2006, undelivered orders amounted to \$253,772 and \$728,736, respectively.

NOTE 10. RECONCILIATION OF NET COST OF OPERATIONS TO BUDGET

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

	<u>2007</u>	<u>2006</u>
Resources Used to Finance Activities:		
Budgetary Resources Obligated		
Obligations incurred	\$ 34,292,116	\$ 31,447,727
Less: Spending Authority From Offsetting Collections and Recoveries	<u>31,700,590</u>	<u>31,882,780</u>
Obligations Net of Offsetting Collections and Recoveries	<u>2,591,526</u>	<u>(435,053)</u>
Net Obligations	<u>2,591,526</u>	<u>(435,053)</u>
Other Resources		
Imputed Financing From Costs Absorbed By Others	<u>1,059,121</u>	<u>991,876</u>
Net Other Resources Used to Finance Activities	<u>1,059,121</u>	<u>991,876</u>
 Total Resources Used to Finance Activities	 <u>\$ 3,650,647</u>	 <u>\$ 556,823</u>
 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	\$ (493,323)	\$ 433,114
Resources That Finance the Acquisition of Assets	<u>-</u>	<u>(388)</u>
 Total Resources Used to Finance Items Not Part of the Net Cost of Operations	 <u>(493,323)</u>	 <u>432,726</u>
 Total Resources Used to Finance the Net Cost of Operations	 <u>\$ 4,143,970</u>	 <u>\$ 124,097</u>
 Components of the Net Cost of Operations That Will Not Require or Generate Resources in the Current Period		
Components Not Requiring or Generating Resources:		
Depreciation and Amortization	\$ 510,838	\$ 823,585
Revaluation of Assets or Liabilities	5,383	33,619
Other	<u>(203,373)</u>	<u>(363,366)</u>
Total Components of Net Cost of Operations That Will Not Require or Generate Resources	 <u>312,848</u>	 <u>493,838</u>
 Total Components of Net Cost of Operations That Will Not Require or Generate Resources In The Current Period	 <u>312,848</u>	 <u>493,838</u>
 Net Cost of Operations	 <u>\$ 4,456,818</u>	 <u>\$ 617,935</u>