

Office of Federal Housing Enterprise Oversight

Annual Performance Plan

FY 1999



November 20, 1998

OFHEO's FY 1999 ANNUAL PERFORMANCE PLAN

OVERVIEW

Introduction

The Office of Federal Housing Enterprise Oversight ("OFHEO" or the "Office") was established as an independent office within the Department of Housing and Urban Development by the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (Title XIII of P.L. 102-550). The Office is headed by a Director appointed by the President for a five-year term.

OFHEO is charged by law to ensure the capital adequacy and financial safety and soundness of two government-sponsored enterprises ("GSEs" or the "Enterprises") -- the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac). OFHEO is funded through assessments on Fannie Mae and Freddie Mac. Thus, its operations represent no direct cost to the taxpayer.

Fannie Mae and Freddie Mac are the nation's largest housing finance institutions. They buy mortgages from commercial banks, thrift institutions, mortgage banks, and other primary lenders, and either hold these mortgages in their own portfolios or package them into mortgage-backed securities for resale to investors. These secondary mortgage market operations play a major role in creating a ready supply of mortgage funds for American homebuyers. Combined assets and off-balance sheet obligations of Fannie Mae and Freddie Mac were \$1.7 trillion at the end of June, 1998.

Fannie Mae and Freddie Mac are congressionally chartered, publicly owned corporations whose shares are listed on the New York Stock Exchange. Under terms of their GSE charters, they are exempt from state and local taxation and from registration requirements of the Securities and Exchange Commission. The Secretary of the Treasury is authorized to extend up to \$2.25 billion in credit to each Enterprise. In addition, the market perceives there to be an implied government guarantee on the financial obligations of the Enterprises. OFHEO was established to ensure capital adequacy and financial safety and soundness of the Enterprises so that they could continue their public mission with minimum risk of cost to the taxpayer.

Development of the Annual Performance Plan

OFHEO primarily accomplishes its mission by conducting examinations of the Enterprises and by assessing their capital adequacy. These broad objectives may be difficult to quantify and measure. There are three primary reasons that this difficulty exists. First, OFHEO regulates two institutions, not hundreds or thousands. Thus, measuring our performance against our goals by reference to changes in the percent of institutions that meet a standard is not very meaningful for OFHEO. Second, OFHEO

was created less than six years ago during the reinvention era. As a relatively new office, OFHEO continues to develop its complete regulatory framework. Because of this, many of OFHEO's strategies and objectives focus on creating and developing certain activities and capabilities, rather than reengineering or eliminating them. Third, OFHEO's role as a regulator is to establish, monitor and enforce regulations and guidelines that the Director believes will ensure that both Enterprises are adequately capitalized and operate in a safe and sound manner. It is these regulations and guidelines, and the strategies and processes used to develop and implement them, that are included in OFHEO's Annual Performance Plan. Hence, OFHEO's overall performance can best be measured by whether or not its actions result in safe and sound operations and adequate capital levels at each Enterprise.

One of OFHEO's top priorities is to complete the risk-based capital regulation, which will enable the Office to apply risk-based capital standards to the Enterprises to determine capital adequacy. Once completed, the stress test will produce a risk-based capital level for each Enterprise and a valuable, measurable regulatory tool. Recognizing how significant this task is to continued effective oversight of the Enterprises, OFHEO has elevated completing the stress test and subsequently issuing the risk-based capital regulation -- activities which might otherwise be viewed as strategies themselves -- to the strategic objective level in both its Strategic and Annual Performance Plans.

Relationship Between the Strategic Plan and the Annual Performance Plan

Strategic Plan

There are four major components to OFHEO's Strategic Plan: (1) mission statement, (2) strategic goals, (3) strategic objectives and (4) strategies to achieve strategic goals.

OFHEO's *mission statement*, like its congressional mandate to ensure the safety and soundness of Fannie Mae and Freddie Mac, is very focused. The mission statement emphasizes protecting the taxpayer, contributing to the strength and vitality of the nation's housing finance system, and providing independent and fair regulation of the Enterprises. Since its inception, OFHEO has structured its regulatory activities around each of these tenets:

From its mission statement, the Office has developed three *strategic goals* which will enable it to accomplish its mission. These strategic goals provide long-term direction to the Office. OFHEO further defines its strategic goals with accompanying *strategic objectives*. The strategic objectives represent measurable goals that OFHEO plans to accomplish during the period covered by the Strategic Plan which are representative of the progress toward achieving its strategic goals. The final component of OFHEO's Strategic Plan is comprised of specific *strategies to achieve strategic goals*. The resulting Strategic Plan includes the four components mentioned above as well as external factors that may affect OFHEO's regulation of the Enterprises.

Annual Performance Plan

The FY 1999 Annual Performance Plan describes what OFHEO will do in FY 1999 with the resources available to achieve the goals and objectives described in the Strategic Plan. There are three major components to OFHEO's Annual Performance Plan: (1) strategic objectives which link to the Strategic Plan, (2) performance goals and (3) means and strategies which contain output goals and measures.

The *strategic objectives* and measures included in OFHEO's Strategic Plan are the starting point in the FY 1999 Annual Performance Plan. They provide a valuable link between the Strategic and Annual Performance Plans and help ensure that strategic goals and objectives as well as the resulting strategies, inputs, outputs, and outcomes are sufficiently integrated and tie into the mission.

The *performance goals* in the Annual Performance Plan link directly to each strategic objective included in OFHEO's Strategic Plan. The performance goals were chosen because they are intermediate outcomes or outputs necessary to achieve the strategic objectives which, in turn, lead to the accomplishment of a corresponding strategic goal. The Annual Performance Plan only includes those performance goals that OFHEO expects to achieve during FY 1999. In many cases, these represent incremental progress toward achieving the strategic objectives and goals. Their achievement also depends on OFHEO's achieving its FY 1999 performance goals.

The third major component of the Annual Performance Plan consists of *means and strategies* and the associated *output goals and measures*. These are the key activities and actions that lead to the attainment of each performance goal. Although there are many other outputs and activities which occur during the process of achieving a given performance goal, the output goals and measures included in the Annual Performance Plan are the best indicators to OFHEO management that the Office is making progress to achieve its performance goals. As part of the means and strategies section, a narrative is provided that describes the linkages between the performance goal and strategic objective, the significance of the goal and, where significant, the processes and technologies used.

As required by the Government Performance and Results Act of 1993, OFHEO will submit a performance report for FY 1999 by March 31, 2000 to discuss the Office's actual performance as compared with the FY 1999 Annual Performance Plan. During the operating year, OFHEO will evaluate its performance internally, make appropriate adjustments, and continue to analyze and reallocate its budgetary resources in a manner which will enable the Office to achieve its annual performance goals.

Program Evaluations

OFHEO regularly evaluates its programs and progress towards achieving its goals in an ongoing manner throughout the year. The Office utilizes regular management meetings as well as management reports to communicate and discuss organizational goals and

objectives, and the status of activities which further their achievement. OFHEO management also uses the budget formulation and execution processes as opportunities to determine resource needs and reallocate Office resources to meet its strategic goals. In its review, OFHEO uses cost-effectiveness as one of the primary criteria for determining the overall effectiveness in the achievement of the Office's mission.

With respect to external evaluations, OFHEO's enabling statute requires the General Accounting Office (GAO) to conduct two audits of OFHEO's operations. GAO's first audit was conducted during FY 1995 and focused on OFHEO's development and implementation of its primary management systems. In its report, GAO concluded that OFHEO had made significant progress in establishing such systems and that the Office had initiated its primary mission-related programs -- assessing the capital adequacy of the Enterprises and conducting examinations of Enterprise operations. OFHEO has used this report to complement internal evaluations of its operations.

GAO's second audit was conducted in the summer of 1997 with the final report released in October 1997. This report focused on (1) identifying the reasons why OFHEO has not issued final risk-based capital standards for the Enterprises, and (2) assessing OFHEO's implementation of its safety and soundness examination responsibilities. GAO correctly identified the challenges OFHEO faces in completing the stress test. The major reason GAO cited for the delay was OFHEO's decision to develop its own modeling capabilities to implement the stress test. OFHEO has developed a Financial Simulation Model that is used to implement the stress test in the proposed risk-based capital regulation that has been drafted. OFHEO believes that it is necessary to independently evaluate the Enterprises' risks.

GAO also recommended that OFHEO move toward a more timely examination cycle, while suggesting that additional resources would be needed to accomplish this. OFHEO agreed with GAO's recommendation and had already planned to alter its examination cycle. Beginning in January 1998, OFHEO moved to a comprehensive risk-based annual examination and expects to deliver its first report of examination to the boards of directors of the Enterprises in February, 1999. Additional resources were allocated to the examination program to ensure that this could be accomplished.

In July, 1998, GAO followed up on OFHEO's progress in implementing their recommendations. Their letter noted that OFHEO had largely completed the development of the stress test but faced three significant challenges. First, OFHEO lost key senior staff in 1998, which GAO noted could delay the proposed rule's development. Second, the proposed plan to provide technical details to federal agency staff to facilitate the inter-agency clearance process was cancelled by OMB, which could lengthen the time it takes for OMB approval. Third, because Financial Simulation Model and the stress test are complex, the public comment process may be lengthened.

OFHEO agreed that the Office faced significant challenges. GAO recognized that OFHEO was addressing these first two immediately by distributing the responsibilities of the departing officials to the existing OFHEO staff and contractor personnel as

appropriate, advertising vacant positions, and working informally during the summer of 1998 with Treasury and HUD staff to explain the technical components of the stress test.

GAO also found that OFHEO made progress in implementing a revised financial safety and soundness examinations program for the Enterprises.

Verification and Validation

The Office is establishing a systematic way of monitoring and tracking progress in achieving its performance goals. OFHEO will maintain information, as described in the performance measures themselves, so that the Office's performance can be validated.

OFHEO's FY 1999 Budget

For FY 1999, OFHEO's enacted budget is \$16 million, and holds OFHEO constant at the FY 1998 level. With respect to personnel, OFHEO's full-time equivalent level of 82 includes 76 full-time permanent positions. These are the same as the FY 1998 levels.

The resources in OFHEO's FY 1999 budget will permit the Office to proceed effectively in all facets of the regulatory agenda assigned by Congress. These include financial safety and soundness examinations of the Enterprises; ongoing development and implementation of the risk-based capital standard and associated rulemaking; and other financial, analytical and policy tools required for effective regulatory oversight. In performing its various regulatory functions, OFHEO uses cross-functional teams comprised of staff members from various OFHEO offices, depending on the nature and complexity of the task. Thus, it is difficult to directly link OFHEO resource levels to specific performance goals.

Revised Final FY 1999 Performance Plan

This revised final FY 1999 Performance Plan retains all of the strategic goals and objectives of the FY 1999 Performance Plan that was originally submitted to Congress with the President's FY 1999 budget request in February 1998. This revised final plan recognizes changes in some of OFHEO's means and strategies, and modifies some performance goal statements and their targets. In all cases, the performance goals and associated means and strategies are aligned with OFHEO's FY 2000 Performance Plan.

Each of the performance goals in the FY 1999 Performance Plan is vital to the Office's achieving its mission. Although OFHEO's FY 1999 budget of \$16 million is 3.4% less than the \$16.55 million requested, in revising the final plan, OFHEO did not eliminate any performance goals. It will, however, be more difficult for OFHEO to achieve its goals. The breadth and depth of resources and expertise that OFHEO can devote to achieving each goal will be lessened. Rather than sacrifice any of its goals, OFHEO will adjust its efforts during the year to best accomplish them. As a consequence, at this time, the degree to which the achievement of any of these goals may be affected is unclear.

Internal Management and Administrative Support to Achieve Performance Goals

OFHEO's success in achieving its performance goals depends on the effective management of its resources and seamless financial and administrative support functions. As a small office, OFHEO relies on staff and management to accomplish its goals through matrix management of cross-organizational teams, timely information for decision-making, and coordination.

OFHEO's staff are its most valuable resources. The Office relies on those with cutting-edge professional skills and a breadth and depth of knowledge in their fields. Their technical competence, effective teamwork and focused performance are crucial to OFHEO's achieving its goals. OFHEO will continue to attract and maintain a high performance workforce.

OFHEO also depends on maintaining information technologies that are effective, and comparable to those used by other organizations with similar analytical requirements. Without these technologies, OFHEO would not be able to provide independent analysis of safety and soundness issues to accomplish its mission.

During FY 1999, OFHEO will have systems in place to monitor actual performance against the Performance Plan. Because OFHEO's appropriation is for a single account, and management has access to real time budget information, management will be able to redirect resources timely, if necessary, to accomplish our goals.

Staff performance appraisals and merit pay increases will reflect the accomplishment of OFHEO's performance goals. Staff will become knowledgeable of the OFHEO Performance Plan, and their own role in achieving the goals. Through the Performance Evaluation Management System, achievement of the Plans will be reflected in the performance standards upon which evaluations are based.

OFHEO will continue to invest in staff through skill-based training. Staff will keep current on up-to-date trends and maintain a skill level of excellence through training. After an evaluation of family-friendly/worker-friendly programs such as day care/elder care, flexi-place and flexible work schedules during FY 1998, OFHEO will implement appropriate policies in FY 1999.

In order to provide effective information technology resources office-wide, OFHEO's Information Technology Resource Management Working Group will develop a five-year Strategic Plan with input from the system owners of various OFHEO systems. After approval by the Director, OFHEO will integrate these into the budget, Strategic and Performance Plans. The Office will continue to implement cost-effective opportunities to improve the efficiency of the research database (data warehouse) and applications software, including the Financial Simulation Model (FSM). By FY 1999, OFHEO will be testing all systems to ensure that they are Year 2000 compliant, and will monitor compliance by cross-servicing providers and will develop contingency plans if necessary.

Strategic Goal 1: To effectively regulate the Enterprises by ensuring that they are adequately capitalized and operate in a safe and sound manner.

The statutory duty of the Director of OFHEO is to “ensure that the Enterprises are adequately capitalized and operating safely.” OFHEO was given two primary regulatory tools to accomplish these statutory responsibilities. The first is the authority to develop and enforce capital standards for the Enterprises. In FY 1999, OFHEO will be working to finalize the risk-based capital standard which is expected to be the binding capital requirement for the Enterprises. The second regulatory tool is the authority to conduct on-site safety and soundness examinations of the Enterprises’ operations. In FY 1999, OFHEO will be finishing its first annual (calendar year 1998) comprehensive risk-based examination of the Enterprises and will be working on its calendar year 1999 examination. OFHEO has identified five strategic objectives with supporting performance goals for FY 1999 that will enable the Office to reach this strategic goal.

Strategic Objective 1.1: To issue and implement the risk-based capital requirements to ensure that the Enterprises are adequately capitalized.

Measure: Promulgation of risk-based capital regulation.

Performance Goal 1.1(a): To publish Notice of Proposed Rulemaking (NPR) for risk-based capital by the end of the second quarter.

Performance Measure: NPR in Federal Register by end of second quarter.

Target: By end of second quarter.

Means and Strategies: Output Goals and Performance Goal Explanation (1.1(a))

1. To have OMB interagency review of the NPR completed in a timely manner.

Output Measure: NPR interagency review completed by OMB.
Target: By end of second quarter.

2. Publish NPR in the Federal Register.

Output Measure: NPR in the Federal Register.
Target: By end of second quarter.

Strategic Goal 1: To effectively regulate the Enterprises by ensuring that they are adequately capitalized and operate in a safe and sound manner.

Strategic Objective 1.1: To issue and implement the risk-based capital requirements to ensure that the Enterprises are adequately capitalized.

Measure: Promulgation of risk-based capital regulation.

Explanation: OFHEO sent its proposed rule on risk-based capital to OMB for interagency review on October 30, 1998. OFHEO will work closely with OMB, Treasury and HUD with the goal of completing interagency review within OMB's 90-day target.

Performance Goal 1.1(b): To maximize the understanding of the stress test and public participation in the rulemaking process.

Performance Measure: Number of comments received on the NPR.

Target: Greater than 17. (The number of comments received on OFHEO's first NPR on risk-based capital.)

Means and Strategies: Output Goals and Performance Goal Explanation (1.1(b))

1. Complete plan for informing the public about the NPR.

Output Measure: Completion of briefing materials to be used during public comment period.

Target: By end of second quarter.

2. Percent of targeted groups presented to on a timely basis during public comment period.

Output Measure: Percent of targeted groups presented to within two months of NPR publication.

Target: 90 percent.

3. Close public comment period.

Output Measure: Public comment period closing date.

Strategic Goal 1: To effectively regulate the Enterprises by ensuring that they are adequately capitalized and operate in a safe and sound manner.

Strategic Objective 1.1: To issue and implement the risk-based capital requirements to ensure that the Enterprises are adequately capitalized.

Measure: Promulgation of risk-based capital regulation.

Target: Four months after NPR is published in the Federal Register.

Explanation: FY 1999 efforts will focus on facilitating the interagency review of the regulation conducted by OMB and, after publication in the Federal Register following the fifteen day mandatory Congressional review, communicating the substance of the regulation to the public in order to stimulate public comment. OFHEO will provide Congress, the Enterprises and all of the relevant industry groups with intensive, detailed briefings. If OFHEO receives requests for a longer comment period after interested parties have an opportunity to read the rule, the office will re-evaluate the four month time period planned for public comments.

Performance Goal 1.1(c): To analyze public comments on the risk-based capital regulation (NPR1 and NPR2).

Performance Measure: Brief Congress periodically on status of plan to publish final risk-based capital regulation.

Target: September 1999.

Means, Strategies, and Performance Goal Explanation (1.1(c))

Once the NPR comment period closes, OFHEO will begin analyzing the comments to determine the plan that will lead to the publication of the final risk-based capital regulation.

Performance Goal 1.1(d): To streamline the risk-based capital calculation process.

Performance Measure: Reduce time from receipt of Enterprise data to calculation of risk-based capital requirement.

Strategic Goal 1: To effectively regulate the Enterprises by ensuring that they are adequately capitalized and operate in a safe and sound manner.

Strategic Objective 1.1: To issue and implement the risk-based capital requirements to ensure that the Enterprises are adequately capitalized.

Measure: Promulgation of risk-based capital regulation.

Target: Reduction of 50% from benchmark calculated at the end of FY 1998.

Means, Strategies and Explanation for Performance Goal 1.1(d)

1. *Complete the first set of data normalization structures for the data warehouse. Data normalization is the process of making a common data set.*

Output Measure: Complete data normalization for retained mortgage-backed securities, and single family and multifamily loan data for both Enterprises in the Data Warehouse; rework FSM modules to access data from new data formats.

Target: September 1999.

2. *Complete development of a streamlined data control process.*

Output Measure: Reduce turn around time for preparing Enterprise data for input to the FSM by 50%.

Target: September 1999.

3. *Complete documentation of the version of the Financial Simulation Model (FSM) used in the proposed risk-based capital regulation.*

Output Measure: FSM module documentation.

Target: September 1999.

Explanation: These developments will allow OFHEO to compute risk-based capital more efficiently and provide the documentation to facilitate developing a streamlined model in the future. Updating the documentation will be necessary if the comments incorporated during the interagency review process warrant substantial changes to the data variables, the mathematical equations or the computer code.

Strategic Goal 1: To effectively regulate the Enterprises by ensuring that they are adequately capitalized and operate in a safe and sound manner.

Strategic Objective 1.1: To issue and implement the risk-based capital requirements to ensure that the Enterprises are adequately capitalized.

Measure: Promulgation of risk-based capital regulation.

OFHEO expects to complete final documentation and testing of the version of the FSM that would be used for the final regulation after receiving and considering comments on the NPR.

Strategic Goal 1: To effectively regulate the Enterprises by ensuring that they are adequately capitalized and operate in a safe and sound manner.

Strategic Objective 1.2 To require the Enterprises to meet applicable capital standards.

Measure: Comparison of actual capital to required capital on at least a quarterly basis.

Performance Goal 1.2(a): To require the Enterprises to meet applicable capital standards on at least a quarterly basis.
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Performance Measure: Comparison of actual capital to required capital standard on at least a quarterly basis.

Target: Ratio of 1 or greater.

Performance Measure: Percent of time acceptable capital plans are obtained from the Enterprises when standards are not met.

Target: 100 percent.

Means and Strategies: Output Goals and Performance Goal Explanation (1.2(a))

1. Complete quarterly capital classifications within required timeframes.

Output Measure: Classification letters to the Enterprises.

Target: Within timeframes established in OFHEO's capital regulations.

Explanation: For FY 1999, capital classifications will be made using the minimum capital standards, as required by law. Each Enterprise submits information necessary for OFHEO to determine the appropriate capital level for that Enterprise within 30 days after each quarter-end date. OFHEO computes the required capital level for each Enterprise based on its on-balance sheet assets and off-balance sheet obligations, and then compares the required capital level with the actual level held by each Enterprise. An Enterprise is deemed "adequately capitalized" if its actual capital level exceeds the required capital level determined by OFHEO. In accordance with the minimum capital regulation, OFHEO then notifies each Enterprise of its proposed capital classification. The Enterprises have up to 30 days to notify OFHEO of any

Strategic Goal 1: To effectively regulate the Enterprises by ensuring that they are adequately capitalized and operate in a safe and sound manner.

Strategic Objective 1.2 To require the Enterprises to meet applicable capital standards.

Measure: Comparison of actual capital to required capital on at least a quarterly basis.

discrepancies they may have with the classification. Once OFHEO either receives notification from the Enterprises that they have no disagreement with the classifications or the 30 days elapse, OFHEO makes final the capital classifications for the Enterprises for that quarter.

Strategic Goal 1: To effectively regulate the Enterprises by ensuring that they are adequately capitalized and operate in a safe and sound manner.

Strategic Objective 1.3: To implement a comprehensive, risk-based examination of each Enterprise to ensure that each operates in a safe and sound manner.

Measure: Completion of an annual examination report for each Enterprise which covers all risk areas.

Performance Goal 1.3(a): To complete a comprehensive, risk-based annual examination for each Enterprise for CY 1998.

Performance Measure: Deliver the CY 1998 report of examination to each Board of Directors.

Target: February 1999.

Means and Strategies: Output Goals and Performance Goal Explanation (1.3(a))

1. Complete field work on 1998 examination.

Output Measure: Completed field work.
Target: December 1998.

Explanation: OFHEO conducts its annual examinations on a calendar year basis. During FY 1999, OFHEO will complete its annual comprehensive risk-based examination of the Enterprises for CY 1998 and will be working on the CY 1999 examination. To ensure effective communication between OFHEO examiners and Enterprise management, OFHEO conducts quarterly meetings with Enterprise management to discuss interim findings, conclusions and recommendations associated with ongoing examination work. Field work on the annual examination is completed in December, and thereafter a Report of Examination is prepared and presented to the Board of Directors of each Enterprise.

Performance Goal 1.3(b): To conduct a comprehensive, risk-based annual examination for each Enterprise for CY 1999.

Performance Measure: Develop and communicate CY 1999 examination strategies and objectives to the Enterprises.

Target: January 1999.

Strategic Goal 1: To effectively regulate the Enterprises by ensuring that they are adequately capitalized and operate in a safe and sound manner.

Strategic Objective 1.3: To implement a comprehensive, risk-based examination of each Enterprise to ensure that each operates in a safe and sound manner.

Measure: Completion of an annual examination report for each Enterprise which covers all risk areas.

Performance Measure: Communicate interim findings and conclusions to each Enterprise.

Target: Following quarter end.

Means and Strategies: Output Goals and Performance Goal Explanation (1.3(b))

1. Finalize and share the CY 1999 examination strategies with each Enterprise.

Output Measure: Conduct meetings to discuss the examination strategies.
Target: January 1999.

2. Communicate with each Enterprise on the status of the annual risk-based examination.

Output Measure: Conduct meetings to maintain an open dialogue on the status of the 1999 examinations.
Target: At least quarterly.

Explanation: Based upon ongoing monitoring, tracking and analysis of Enterprise financial data, information obtained during the previous examination, and frequent discussions with Enterprise management, examination strategies and objectives for the CY 1999 examination will be developed and communicated to the Enterprises in January 1999. Examination objectives will reflect OFHEO's assessment of risk at each Enterprise, and will therefore differ for each Enterprise.

OFHEO conducts its annual examination on a calendar year (CY) basis. During FY 1999, OFHEO will finalize its CY 1999 risk-based examination plan for each Enterprise. Also during FY 1999, OFHEO will conduct 75% of the field work for the CY 1999 risk-based examinations. To ensure effective communication between OFHEO examiners and Enterprise management and the Boards of Directors, OFHEO

Strategic Goal 1: To effectively regulate the Enterprises by ensuring that they are adequately capitalized and operate in a safe and sound manner.

Strategic Objective 1.3: To implement a comprehensive, risk-based examination of each Enterprise to ensure that each operates in a safe and sound manner.

Measure: Completion of an annual examination report for each Enterprise which covers all risk areas.

engages in routine meetings to discuss the upcoming examination plan, as well as interim findings and evaluations associated with ongoing examination work.

Performance Goal 1.3(c): To conduct surveillance and monitoring, risk assessment, and analysis.

Performance Measure: Prepare and issue surveillance and monitoring reports.

Target: At least quarterly.

Output Goals and Measures:

1. Development of application software to automate surveillance and monitoring reports.

Output Measure: Test working software.

Target: September 1999.

Explanation for Performance Goal 1.3(b)

OFHEO performs surveillance and monitoring of the Enterprises' businesses to complement and focus the work performed by examination staff. Surveillance and monitoring includes reviewing publicly available and proprietary financial data released by the Enterprises and other sources, reviewing minutes from board meetings and examining for risks related to certain Enterprise activities. OFHEO's Financial Simulation Model (FSM) will be an important tool for examining for risks at the Enterprises. OFHEO plans to consolidate the information obtained for surveillance and monitoring purposes into an automated system which is readily accessible to OFHEO staff members. To do so, OFHEO staff and contract support will develop application software to facilitate the input, retrieval, and reporting of information for the surveillance and monitoring system.

Strategic Goal 1: To effectively regulate the Enterprises by ensuring that they are adequately capitalized and operate in a safe and sound manner.

Strategic Objective 1.4: To ensure that the Enterprises respond appropriately to examination findings.

Measure: Percent of examination findings identified for follow-up that receive the appropriate dialogue and response.

Performance Goal 1.4(a): To promote timely responses and corrective measures for findings in the examination that warrant follow-up.

Performance Measure: Percent of examination findings identified for follow-up and discussed in the annual Report of Examination that are not being appropriately addressed.

Target: 0%

Means and Strategies: Output Goals and Performance Goal Explanation (1.4(a))

1. *Complete transparency of the examination program including an active and timely dialogue, with Enterprise representatives, relating to the examination work and products.*

Output Measure: Percent of issues being considered during the examination which are discussed with the appropriate Enterprise representatives.

Target: 100%

Explanation: OFHEO believes the most effective way to evaluate the safe and sound operations of an Enterprise is to maintain continuous dialogue between OFHEO's examination personnel and the Enterprises. Throughout the annual examination, OFHEO explains its position and seeks input on its findings. Such discussions routinely occur during the examination program. In addition to routine discussions covering the examination work, OFHEO will regularly meet with senior Enterprise representatives to ensure a constructive dialogue is maintained at all levels. Through these regular communications, the Enterprises will be apprised of any developing issues or thinking by OFHEO's examiners at the earliest stage, thus allowing prompt response to any potential concerns, issues, or opportunities identified to enhance the Enterprise's operations. With OFHEO's continuous on-site examination work, any follow-up initiatives are monitored.

Strategic Goal 1: To effectively regulate the Enterprises by ensuring that they are adequately capitalized and operate in a safe and sound manner.

Strategic Objective 1.4: To ensure that the Enterprises respond appropriately to examination findings.

Measure: Percent of examination findings identified for follow-up that receive the appropriate dialogue and response.

Performance Goal 1.4(b): To communicate examination conclusions to the Boards of Directors and require their appropriate response, including any directives provided to the Enterprises' management.

Performance Measure: Obtain response from Boards of Directors to conclusions shared in the annual Report of Examination.

Target: Within 30 days of the Board meeting date, subsequent to the issuance of the annual Report of Examination.

Means and Strategies: Output Goals and Performance Goal Explanation (1.4(b))

1. Issue the annual Report of Examination timely.

Output Measure: Issuance of the annual Report of Examination
Target: February 1999

2. Meet with the Board of Directors to discuss the conclusions in the annual Report of Examination.

Output Measure: Meeting with the Board to discuss examination conclusions.
Target: First regularly scheduled Board meeting subsequent to the issuance of the annual Report of Examination.

3. Track and evaluate follow-up efforts

Output Measure: Tracking reports.
Target: Ongoing

Explanation: OFHEO provides a copy of its annual Report of Examination to the Board of Directors of each Enterprise which covers the conclusions from the annual

Strategic Goal 1: To effectively regulate the Enterprises by ensuring that they are adequately capitalized and operate in a safe and sound manner.

Strategic Objective 1.4: To ensure that the Enterprises respond appropriately to examination findings.

Measure: Percent of examination findings identified for follow-up that receive the appropriate dialogue and response.

risk-based examination. Since the annual Report of Examination will be shared with the Board of Directors, the formal response is provided by the Board that includes a summary of any directives given to Enterprise management in response to examination issues.

Performance Goal 1.4(c): To enhance the effectiveness of communications between OFHEO's examination staff and Enterprise officials.

Performance Measure: Survey the Enterprises on qualitative aspects of the examination program.

Target: Achieve a "high" performance level for the quality of communications with the examination staff, using the survey's rating scale.

Means and Strategies: Output Goals and Performance Goal Explanation (1.4(c))

1. Design and Administer survey to the Enterprises.

Output Measure: Completed surveys.
Target: March 1999.

Explanation: To complement ongoing efforts to promote effective and open communication with the Enterprises, OFHEO will complete development and administer a survey. The purpose of the survey is to solicit qualitative feedback from the Enterprises regarding the effectiveness of the examination program and the quality of communications. OFHEO will continue to evaluate surveys conducted by other federal regulators, other federal organizations as well as those used by certain private sector entities, as we revise our own survey.

Strategic Goal 1: To effectively regulate the Enterprises by ensuring that they are adequately capitalized and operate in a safe and sound manner.

Strategic Objective 1.5: To ensure that future changes in risk do not impair the ability of the Enterprises to perform their missions in a safe and sound manner.

Measure: Maintenance of ongoing monitoring and evaluation of Enterprise risks and activities through new program reviews, as well as periodic reports and studies.

Performance Goal 1.5(a): To ensure that new programs do not risk significant deterioration of the Enterprises' financial conditions.

Performance Measure: Number of new programs approved which cause significant deterioration of the Enterprises' financial conditions.

Target: Zero.

Means and Strategies: Output Goals and Performance Goal Explanation (1.5(a))

1. Letters from the OFHEO Director to the Secretary of HUD.

Output Measure: Issuance of letters.
Target: Within 45 days of program request.

Explanation: The HUD Secretary has the authority to approve new programs in which the Enterprises wish to engage. Until OFHEO's risk-based capital standard is in place, OFHEO has the statutory responsibility to examine new programs for safety and soundness considerations. Specifically, if the Director determines that a new program would risk significant deterioration of the financial condition of an Enterprise, this determination would serve as a basis for the HUD Secretary to disapprove the program. OFHEO and HUD have developed a good working relationship in examining issues surrounding new program requests from the Enterprises.

Strategic Goal 1: To effectively regulate the Enterprises by ensuring that they are adequately capitalized and operate in a safe and sound manner.

Strategic Objective 1.5: To ensure that future changes in risk do not impair the ability of the Enterprises to perform their missions in a safe and sound manner.

Measure: Maintenance of ongoing monitoring and evaluation of Enterprise risks and activities through new program reviews, as well as periodic reports and studies.

Performance Goal 1.5(b): To ensure that OFHEO is knowledgeable of all the relevant risks for safety and soundness that impact the Enterprises.

Performance Measure: In depth profiles for Enterprises that incorporate a comprehensive assessment of the risks (both from the business operations and the external operating environment) that pose a potential concern for financial safety and soundness.

Target: Quarterly.

Means and Strategies: Output Goals and Performance Goal Explanation (1.5(b))

1. In depth profiles – Overall assessment of the risk environment confronting the Enterprises that draws from the work conducted across OFHEO.

Output Measure: Risk assessments and examination findings.
Target: Quarterly.

Output Measure: Capital assessments.
Target: Quarterly.

Output Measure: Production of OFHEO House Price Index (HPI).
Target: Quarterly.

2. Annual Report to Congress.

Output Measure: Production of Annual Report to Congress.

Strategic Goal 1: To effectively regulate the Enterprises by ensuring that they are adequately capitalized and operate in a safe and sound manner.

Strategic Objective 1.5: To ensure that future changes in risk do not impair the ability of the Enterprises to perform their missions in a safe and sound manner.

Measure: Maintenance of ongoing monitoring and evaluation of Enterprise risks and activities through new program reviews, as well as periodic reports and studies.

Target: April of each year.

3. Internal and external papers and reports.

Output Measure: Production of papers and reports on relevant issues.
Target: 3 per quarter.

Explanation: In support of OFHEO's regulatory and supervisory authority and its specific authorities to conduct examinations and develop and implement capital regulations, OFHEO has established a sophisticated economic, financial and policy research capability. The ability to conduct such research allows the Office to maintain its independence in the evaluation of technical questions related to the safety and soundness of the Enterprises. Congress recognized the need for OFHEO to develop its own research capability by explicitly authorizing the Director to conduct research and financial analysis, and requiring the Enterprises to provide the necessary data.

In FY 1999, OFHEO will continue to explore the application of its research in credit scoring and Enterprise purchases of subprime mortgages to the stress test, and will pursue research in other priority areas that OFHEO identifies as relevant to the safety and soundness of the Enterprises. The development and exchange of analysis and findings from examinations, capital assessments and ongoing monitoring and research among OFHEO staff and management ensure that OFHEO remains knowledgeable of the risks that face the Enterprises.

Strategic Goal 2:	To promote an efficient secondary mortgage market through an independent and balanced approach to regulatory oversight of the Enterprises.
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OFHEO continues to evolve in its relationships with the Enterprises and Congress, as well as relevant interest groups. In order for OFHEO to be effective at regulating the Enterprises, it is important that OFHEO be viewed as providing independent and balanced regulatory oversight. Fairness translates into providing an opportunity for all interested parties to comment on OFHEO's regulatory actions. Independent analysis of regulatory issues provides credibility to the actions taken by OFHEO and ensures that all points of view are examined. OFHEO has identified two strategic objectives with supporting FY 2000 performance goals that will enable the Office to reach this strategic goal.

Strategic Objective 2.1:	To maintain OFHEO's independence in its relationships with the Enterprises.
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<u>Measure:</u>	Use of internal modeling capacity to regularly analyze Enterprise risks. Use of examiners from other financial institution regulatory agencies.
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Performance Goal 2.1(a):	To use internal modeling capacity to regularly analyze Enterprise risks.
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<u>Performance Measure:</u>	Use the Financial Simulation Model to assist OFHEO in developing risk profiles for the Enterprises.
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<u>Target:</u>	Run specific simulations on an as needed basis.
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Means, Strategies, and Performance Goal Explanation (2.1(a))

OFHEO's Financial Simulation Model is a model used for simulating Enterprise financial performance under a variety of economic environments, including stressful ones. The Financial Simulation Model is OFHEO's principal tool for developing and running the stress test. In addition, both as a whole and in its parts, the Financial Simulation Model supports a wide range of research and financial analysis relating to credit and interest rate risk, and performance trends at the Enterprises. As part of OFHEO's ongoing monitoring of the Enterprises, the Financial Simulation Model will be used by our examination program to assist in evaluating the credit and interest rate risk profiles for each Enterprise, as well as to assist OFHEO in the timely analysis of issues as they arise.

Strategic Goal 2:	To promote an efficient secondary mortgage market through an independent and balanced approach to regulatory oversight of the Enterprises.
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Strategic Objective 2.1: To maintain OFHEO's independence in its relationships with the Enterprises.

Measure: Use of internal modeling capacity to regularly analyze Enterprise risks. Use of examiners from other financial institution regulatory agencies.

OFHEO's Research Systems Environment is used to support the operation of the Financial Simulation Model. It provides the necessary computer hardware, software and other systems necessary to apply the Financial Simulation Model. To develop and maintain the Financial Simulation Model, OFHEO uses a mix of in-house economists, financial analysts, computer specialists, and contract support. These resources make it possible for OFHEO to regularly and independently analyze the Enterprises' risks using the Financial Simulation Model, separately from its use in the stress test.

Performance Goal 2.1(b):	To maintain the objectivity of the examinations process, OFHEO will participate with other financial regulators on safety and soundness examinations at large financial institutions and be involved in other regulatory forums.
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Performance Measure: To participate in examinations at large financial institutions with the other financial regulators to broaden examiners' expertise and maintain objectivity.

Target: At least two detailed assignments.

Performance Measure: To participate in examination related forums with the other financial regulators.

Target: At least eighteen.

Strategic Goal 2: To promote an efficient secondary mortgage market through an independent and balanced approach to regulatory oversight of the Enterprises.

Strategic Objective 2.1: To maintain OFHEO's independence in its relationships with the Enterprises.

Measure: Use of internal modeling capacity to regularly analyze Enterprise risks. Use of examiners from other financial institution regulatory agencies.

Means, Strategies, and Performance Goal Explanation (2.1(b))

Maintaining the objectivity and expertise of the examination cadre remains a priority for OFHEO. In the past, OFHEO has contracted with other financial regulators for examiners to support the examination work force. Given the down-sizing initiatives at the other regulators, these examiners are no longer available. Therefore, OFHEO will participate with other regulators in examination of large financial institutions to gain its own increased expertise and remain informed on developments both within the financial services industry and risk-based examination techniques. Additionally, OFHEO will participate in relevant interagency forums to remain current on regulatory issues and developments. These forums include the Federal Financial Institutions Examinations Council (FFIEC) and the new GSE Regulators Examinations Working Group.

Strategic Goal 2: To effectively regulate the Enterprises by providing independent and fair oversight.

Strategic Objective 2.2: To ensure a balanced approach to regulation by providing the Enterprises and all other stakeholders the appropriate opportunity for input on regulatory activities.

Measure: Number of opportunities for public comment on proposed regulations.

Performance Goal 2.2(a): To place all proposed regulations on the OFHEO website to enhance opportunities for input.
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Performance Measure: Percent of proposed regulations issued placed on website within two weeks of publication in the Federal Register.

Target: 100 percent.

Means, Strategies, and Performance Goal Explanation (2.2(a))

OFHEO established a website on October 30, 1998. OFHEO will publish all of its proposed regulations on its web page and solicit comments from interested parties. Such access should broaden the awareness of OFHEO's proposed regulations and provide more opportunities for public input.

Strategic Goal 3: To effectively regulate the Enterprises by ensuring that they comply with all laws under our jurisdiction.

As the safety and soundness regulator for the Enterprises, OFHEO has the responsibility to ensure that they comply with all laws under our jurisdiction. As a result of their government-sponsored status, the Enterprises have been given many benefits that enable them to fulfill their public purpose. OFHEO will work to ensure that the Enterprises' actions and operations comply with the provisions of their Charter Acts and other applicable laws within our jurisdiction. OFHEO has identified two strategic objectives with supporting FY 2000 performance goals that will enable the Office to reach this strategic goal.

Strategic Objective 3.1: To prohibit excessive executive compensation at the Enterprises.

Measure: Percent of executive officer termination agreements acted upon by OFHEO. Percent of instances of excessive executive compensation acted upon by OFHEO.

Performance Goal 3.1(a): To prohibit excessive executive compensation at the Enterprises.

Performance Measure: Percent of instances of excessive executive compensation acted upon by OFHEO.

Target: 100 percent.

Performance Measure: Timely review of termination agreements for Enterprise executives.

Target: Within 90 days of receipt of request and all necessary materials from Enterprise.

Means, Strategies, and Performance Goal Explanation (3.1(a))

OFHEO's statute requires the Director to prohibit the Enterprises from providing excessive compensation to any executive officer. Specifically, the statute provides that compensation must be reasonable and comparable with compensation paid by other similar businesses to executives having similar duties and responsibilities. "Similar businesses" include publicly held financial institutions or major financial services companies. Additionally, the Enterprises' Charter Acts require the Enterprises to obtain prior approval of OFHEO's Director before entering into or changing termination agreements with their executive officers. The Charter Acts

Strategic Goal 3: To effectively regulate the Enterprises by ensuring that they comply with all laws under our jurisdiction.

Strategic Objective 3.1: To prohibit excessive executive compensation at the Enterprises.

Measure: Percent of executive officer termination agreements acted upon by OFHEO. Percent of instances of excessive executive compensation acted upon by OFHEO.

provide that the Director of OFHEO may not approve any such agreement unless the Director determines that the benefits provided under such agreements are comparable to those of officers of other public and private entities involved in financial services and housing interests who have comparable duties and responsibilities.

OFHEO, with the assistance of an executive compensation consulting firm, completed an extensive study of executive compensation at the Enterprises in FY 1998. This study resulted in the identification of a comparable peer group and methodology for tracking and monitoring changes to executive compensation at the Enterprises on an ongoing basis. In FY 1999, OFHEO will monitor changes to executive compensation at the Enterprises to ensure that they do not exceed the parameters that were established in our study. OFHEO intends to conduct an in-depth review that will reassess the peer group and methodology for monitoring executive compensation every three years. OFHEO also reviewed Enterprise policies for termination agreements and severance packages. Individual termination agreements will be reviewed and acted upon as they are developed for specific executives.

Strategic Goal 3: To effectively regulate the Enterprises by ensuring that they comply with all laws under our jurisdiction.

Strategic Objective 3.2: To prohibit the Enterprises from violating other provisions of their Charter Acts or of OFHEO's statute.

Measure: Percent of supervisory actions to remedy Charter Act and other violations that are successful.

Performance Goal 3.2(a): To prohibit the Enterprises from violating other provisions of their Charter Acts or of OFHEO's statute.

Performance Measure: Percent of successful supervisory actions to remedy Charter Act and other violations.

Target: 100 percent.

Means and Strategies: Output Goals and Performance Goal Explanation (3.2(a))

1. *Analyze activities undertaken by an Enterprise as appropriate to determine whether they violate the Charter Act or provisions of OFHEO's statute.*

Output Measure: Decision paper.
Target: As needed.

2. *Report on appropriate action (e.g., informal communication, examination recommendation, supervisory agreement, other enforcement action) taken to address the violation and follow up to effect full compliance.*

Output Measure: Annual Enforcement Action Report to Congress.
Target: March 15, 2000.

Explanation: The Director has authority under the Act to take enforcement actions for matters involving the Enterprises' capital levels, safety and soundness, and violations of certain laws and regulations. For matters other than safety and soundness or capital-related issues, the Director's authority to bring an enforcement action is subject to the approval of the HUD Secretary. OFHEO's enforcement powers include traditional enforcement tools such as cease-and-desist orders, supervisory agreements and civil money penalties.

Strategic Goal 3: To effectively regulate the Enterprises by ensuring that they comply with all laws under our jurisdiction.

Strategic Objective 3.2: To prohibit the Enterprises from violating other provisions of their Charter Acts or of OFHEO's statute.

Measure: Percent of supervisory actions to remedy Charter Act and other violations that are successful.

OFHEO will also continue to address issues related to their charter authorities, working with HUD when appropriate. Such issues periodically arise as the Enterprises develop new financial products or engage in new types of activities.