

FEDERAL HOUSING FINANCE BOARD

OPEN MEETING

Wednesday, April 14, 2004
Washington, D.C.

The Board Meeting convened, pursuant to notice, at 10:18 a.m., at 1777 F Street, N.W., Second Floor Board Room, Washington, D.C.

MEMBERS PRESENT:

ALICIA R. CASTANEDA, Chairman

JOHN C. WEICHER, Director

ALLAN I. MENDELOWITZ, Director

FRANZ S. LEICHTER, Director

C O N T E N T S

AGENDA ITEM

Federal Home Loan Bank of Topeka Capital Plan Amendment,
Office of Supervision

P R O C E E D I N G S

CHAIRMAN CASTANEDA: I wanted to apologize for the delay. I understand the transcriptionist had some weather/traffic-related problems, but everything is okay now.

I call this meeting of the Federal Housing Finance Board to order. We have two items on the agenda today: first, proposed amendments to the Capital Plan of the Federal Home Loan Bank of Topeka, and, second, a closed portion to continue the Finance Board's consideration of various disclosure initiatives and supervisory issues regarding enhanced securities disclosure.

Before we move into these items, though, I would like to make a few comments. Today is a remarkable day for me, and a humbling one. President Bush has bestowed upon me not only his confidence but also a great honor in designating me as Chairman of the Federal Housing Finance Board. I will do my utmost to fulfill both his confidence and this tremendous honor by ensuring that this agency successfully carries out its oversight and responsibilities with diligence and dedication.

In the short time I have been on the Finance Board, I have come to realize the great strides the Finance Board has made in building its reputation as a professional

and dedicated financial regulator, continually strengthening its oversight of the Federal Home Loan Banks. My goal as Chairman will be to build upon that foundation and lead the Finance Board to the next level.

I'm very much a firm believer that the Finance Board is and must be a strong arm's-length regulator of the Federal Home Loan Banks, and I will work very hard to ensure that this agency has whatever regulatory tools, staffing, and resources it needs to fully discharge its safety and soundness and mission-related responsibilities, including the affordable housing program.

In the process, and subject, of course, to the necessary and proper constraints imposed on the relationship between the regulator and the regulated, I am hopeful that the Banks and their representatives will welcome our efforts to be a truly engaged and active regulator as in the best interests, and I strongly encourage them to engage with us in open, constructive, and ongoing dialogue so the Banks and the Board can have a healthy, productive working relationship.

I believe that this is always the best way for us to move forward together in the interest of both the Federal Home Loan Bank System and as stewards of the public interest of the public at large. Of course, in accomplishing this

first goal, I will rely heavily on the cooperation and participation of my colleagues on the Board and on the very dedicated Finance Board staff. I have great respect for each of you.

I would like to thank you for your tireless efforts in making this agency a serious and successful regulator of the Federal Home Loan Banks and for the hours you spend, the miles you travel, the work into which you pour yourselves.

I would also like to thank my Board colleagues for the warm reception they have given me since I joined the Board in January and for the productive relationship we have developed since then. I look forward to continuing this relationship. I am confident that I, my fellow directors, and the staff will work well together as a real team to carry out the important work of the Finance Board. We're going to accomplish great things together.

As many of you know, I came to this country 33 years ago not knowing, of course, what the future would hold but full of hope and confidence, for the United States was then, and it is today, a country of freedom and unlimited opportunities for immigrants. Through hard work, high aspirations, a lot of luck, and perhaps, more importantly, the loving support of a wonderful husband, I have been

fortunate to have lived my own version of the American Dream. Now I am also pleased and honored to be named Chairman of the Federal Housing Finance Board. I am profoundly grateful to this country for the opportunities it has granted me, and I promise to do my very best to uphold the great responsibilities placed upon me.

Thank you. Is there anybody else who would like to make some opening remarks? Director Mendelowitz?

DIRECTOR MENDELOWITZ: Thank you, Madam Chair. I just want to take a moment to congratulate you on assuming your new position and to extend to you my very best wishes for much success. I look forward to working with you and our colleagues on the Board as we turn a new page and move forward to do, in your words, great things. We have a lot of issues, and I'm confident that under your skilled and talented leadership we will all work together to try to do the right thing and do it in a collegial and respectful way.

Thank you.

CHAIRMAN CASTANEDA: Thank you, Director Mendelowitz, for your kind words.

Director Leichter?

DIRECTOR LEICHTER: Thank you, Madam Chair. I just want to say I think this is a historic moment for the Federal Housing Finance Board, because it's the first time

in the history of this Board and its predecessor that we have a female Chair, and I'm sure many people say it's about time. And I know that bringing to this position, as you do, a vast knowledge and experience in the world of banking, I think the System will welcome your leadership. I know that in the couple months that we've had a chance to work together, I've certainly gained by having the opportunity to listen to you and learn from you, and I look forward to continuing to work closely together. I think we've got some very challenging issues, but I don't think there's any issue that we can't deal with productively as long as we work together collaboratively. And I know that's what you're committed to, and certainly that's what I and I know my other Board members are committed to.

So I enter this new era of the Finance Board with a great deal of optimism.

Thank you.

CHAIRMAN CASTANEDA: Thank you, Director Leichter. I do appreciate your kind words, too. That's very nice. Yes?

DIRECTOR WEICHER: I would like to make it unanimous. I congratulate you and welcome you to the Chairmanship of the Board, and I'm also looking forward very much to working with you and to move ahead. We have

important issues to deal with, and we have the fundamental and ongoing responsibility of regulating large and important financial institutions with hundreds of billions of dollars of obligations that are treated in some circles as obligations of the Government of the United States, and we will have our hands full. And I'm looking forward to digging in.

CHAIRMAN CASTANEDA: Thank you. Thank you to all of you.

Now, we should start with a motion to approve the closed portion of this meeting which will follow the open portion of the meeting dealing with the Topeka Capital Plan Amendments. The Government in the Sunshine Act requires a public vote to approve the closed portion of this meeting. As the announced agenda states, the closed portion deals with the further consideration of various disclosure initiatives and supervisory issues regarding enhanced securities disclosure. This consideration includes Bank examination and supervisory information that is sensitive and confidential, and the general counsel has certified that a closed meeting is proper.

The transcript of this portion of the meeting will, of course, contain information that may be withheld from publication, so at this point I would like to ask for a

motion both to close this portion of the meeting and to seal the transcript and record.

DIRECTOR LEICHTER: If I may--

CHAIRMAN CASTANEDA: Director Leichter?

DIRECTOR LEICHTER: --assume this honor, this responsibility, under the Government in the Sunshine Act and the Finance Board's implementing regulation, the General Counsel has certified that it is proper to close to public observation and seal the record of the agenda item entitled "Further Consideration of Various Disclosure Initiatives and Supervisory Issues Regarding Enhanced Securities Disclosure."

Based on the subject matter and reliance on his certification, I move to close this portion of the meeting and withhold the record from the public.

CHAIRMAN CASTANEDA: Thank you for the motion. Is there any discussion of the motion?

(No response.)

CHAIRMAN CASTANEDA: Seeing none, the Secretary will please call the roll of the motion.

MS. GOTTLIEB: Director Leichter?

DIRECTOR LEICHTER: Yes.

MS. GOTTLIEB: Director Mendelowitz?

DIRECTOR MENDELOWITZ: Yes.

MS. GOTTLIEB: Director Weicher?

DIRECTOR WEICHER: Aye.

MS. GOTTLIEB: Chairman Castaneda?

CHAIRMAN CASTANEDA: Yes. The motion is carried, and the subsequent portion of our meeting will be closed to public observation and the transcript, therefore, will remain closed and confidential. Thank you.

Now, for the open portion of the meeting, our first agenda item is consideration of proposed Capital Plan Amendments for the Federal Home Loan Bank of Topeka. The presentation comes from Scott Smith of the Office of Supervision and Tom Joseph of the Office of General Counsel. If Scott is ready to start, please?

MR. SMITH: I'm ready. Good morning, Madam Chair, and Members of the Board. The Federal Home Loan Bank of Topeka's capital plan was approved by the Finance Board on July 10, 2002. The Bank's approved plan authorized the capital structure to include both Class A and Class B stock.

In the approved plan, Class A stock would be used to meet the asset-based or membership stock purchase requirement initially set at 0.1 percent of total assets and capped at \$500,000.

The Class B stock would be used to meet the activity-based stock purchase requirements initially set at

4.5 percent for advances, 5 percent for the outstanding balance held by the Bank for AMA, 0.5 percent for letters of credit, and 2 percent for the notional amount of exchange agreements. The total of required stock to be held by a member would be the sum of the membership and activity-based requirements.

According to an analysis provided by the Banks and based on data from June 30, 2003, the approved plan would have required 237 different members to buy additional stock totaling \$25.2 million. Excess stock at conversion would have totalled about \$370 million. On December 19th of 2003 and again on April 9th of this year, the Bank's Board of Directors considered and approved a number of amendments to the Bank's capital plan and submitted them to the Finance Board for approval. According to Bank management, the reason for proposing the amendments is that the approved plan is now viewed as inconsistent with the Bank's long-term objectives for growth and profitability. The most significant change in the amended plan is a greater reliance on excess stock to capitalize long-term assets, and the Bank has already begun to issue stock rather than cash dividends to increase the amount of excess stock outstanding.

The Bank projects that excess stock will account for about 28 percent of total stock by 2006. We note that

this business plan is in keeping with that of other Federal Home Loan Banks, as approved by the Finance Board.

Since there are a number of amendments, we have grouped them into four categories for purposes of discussion.

First, stock purchase requirements. The proposed plan would double the membership requirement and the cap to 0.2 percent of total assets and a cap of \$1 million. The activity-based stock purchase requirement for advances would be increased from 4.5 to 5 percent, and for AMA it would be reduced to 2 percent, but of the outstanding balance sold to the Bank instead of that held by the Bank, the activity-based stock purchase requirements for letters of credits and exchange agreements would be set at zero, and there would be conforming changes to the ranges for all stock purchase requirements.

The amendments also include a significant change to the determination of a member's total of required stock. The total of required stock to be held by a member would now be the greater of the membership and the activity-based requirements, where Class A stock would still be required to be held for up to the membership requirement and B stock for all amounts that the activity-based total is in excess of the membership total.

The net consequence of all these changes to the stock purchase requirements is an assignment of stock requirements among members that is more closely aligned with the current stock purchase requirements. Again, based on data from June 30, 2003, at conversion only 98 members would have to buy additional stock totaling \$9.5 million, only about one-third of the adjustment required under the approved plan.

Second, withdrawal and orderly liquidation provisions. These amendments would clarify that upon termination of a membership, former members must hold either Class A or Class B stock to satisfy any activity-based stock purchase requirement until the activity rolls off. The Bank would have the discretion to require that the requirement be met with either A or B stock and could implement an exchange of stock, A for B or the reverse, to achieve that.

Third, the opt-out date. The amendments would reset the opt-out date from 90 calendar days before the effective date of the plan to 30 calendar days. This is in line with the opt-out dates and other capital plans approved by the Finance Board.

Fourth, stock repurchase. The amendments would simplify the stock redemption and request provisions so that all such requests would be considered a redemption request,

and the Bank would have the discretion upon appropriate notice to repurchase any excess stock for which a redemption request has been filed at any time prior to the end of the redemption period.

In general, we have not found any of the amendments, individually or in total, to constitute a capital structure that is inconsistent with those approved by the Finance Board for other Banks. Furthermore, based upon our review of the material submitted by the Bank to support approval of the amendments and conversations with Bank management, we have not identified any problems in the plan or the amendments that would prevent the Bank from maintaining sufficient capital to comply with the statutory and regulatory requirements and to continue to operate in a safe and sound manner.

We would be happy to answer any questions.

CHAIRMAN CASTANEDA: Thank you, Scott, for your presentation and for walking us through the Topeka Bank proposed amendments. It is my understanding that the Bank and its management from the president, Andy Jetter, on down cooperated openly and fully with the Finance Board staff when working through and analyzing the proposal. So I would like also to commend and thank the Bank for taking such a helpful approach to this issue.

Any questions for Scott on the proposal?

DIRECTOR MENDELOWITZ: I just wanted a clarification to make sure I understood correctly. The total stock purchase requirement at the end of the day would be the greater of either the membership requirement or the activity-based requirement. Is that correct?

MR. SMITH: That's correct.

DIRECTOR MENDELOWITZ: Thank you.

CHAIRMAN CASTANEDA: Any other comments?

(No response.)

CHAIRMAN CASTANEDA: Okay. There are two resolutions required for approval of the Topeka Capital Plan Amendment. The first resolution deals specifically with the amendments to the capital plan. The second resolution waives the six months withdrawal notice requirement. This is consistent with the procedure used to approve the other Banks' capital amendments. Board resolutions are found in the Board's materials for today's meeting. We can approve both resolutions with a single motion.

Is there a motion to approve the two resolutions concerning the Topeka Bank Capital Plan Amendments?

DIRECTOR MENDELOWITZ: Madam Chair, I so move.

CHAIRMAN CASTANEDA: Thank you.

Director Mendelowitz has moved and approved of the two resolutions concerning the Topeka Bank Capital Plan Amendments. Is there any discussion on the motion?

(No response.)

CHAIRMAN CASTANEDA: Hearing none, the Secretary--

DIRECTOR MENDELOWITZ: I would like to--the fact that there is no discussion is not a reflection that we haven't done our appropriate due diligence. Staff provided a really good analysis, and they answered all the questions I had, and I was quite comfortable with their written material.

CHAIRMAN CASTANEDA: Excellent point. Yes, we did have a meeting last week, and we weighed very thoroughly all the plan's issues.

Are there any other discussions of the motion?

(No response.)

CHAIRMAN CASTANEDA: Hearing none, the Secretary will please call the roll.

MS. GOTTLIEB: Director Leichter?

DIRECTOR LEICHTER: Yes.

MS. GOTTLIEB: Director Mendelowitz?

DIRECTOR MENDELOWITZ: Yes.

MS. GOTTLIEB: Director Weicher?

DIRECTOR WEICHER: Aye.

MS. GOTTLIEB: Chairman Castaneda?

CHAIRMAN CASTANEDA: Yes. Thank you. The motion is carried. The two resolutions concerning the Capital Plan Amendments of the Federal Home Loan Bank of Topeka are approved.

That now concludes the open portion of the meeting. Pursuant to the motion adopted earlier today, I now close the open portion of the meeting. I will call the closed portion of the meeting to order. Let's give everybody a moment to clear the room, and why don't we take a five-minute recess, and we will reconvene promptly in closed session at a quarter of 11:00.

(Whereupon, at 10:37 a.m., the open session of the meeting concluded.)