

FEDERAL HOUSING FINANCE BOARD MEETING

OPEN SESSION

Wednesday, September 13, 2006

ANDERSON COURT REPORTING  
706 Duke Street, Suite 100  
Alexandria, VA 22314  
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4           ALICIA R. CASTANEDA  
5           ALLAN I. MENDELOWITZ  
6           PAMELA PATENAUDE  
7           SHELIA S. WILLIS  
8           JOHN P. KENNEDY  
9           STEPHEN M. CROSS  
10          JUDITH HOFMANN  
11          MARK DAVID  
12          SHARON LIKE  
13          GWEN GROGAN  
14          CHRISTIE SCIACCA  
15          JIM SHANNON  
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## 1 P R O C E E D I N G S

2 (10:00 a.m.)

3 CHAIRMAN ROSENFELD: Before I call this  
4 meeting to order, I'd like to welcome two very  
5 special guests, one I just saw in the back, Franz  
6 Leichter, who has been an extraordinary force and  
7 the life of the Fair Housing Finance Board, and we  
8 welcome you back, Franz. We'll discuss your  
9 contributions a little bit later in the morning.

10 And I'd also like to welcome back Chris  
11 Morton, who has been very, very helpful I know to  
12 Franz and to the entire Board in terms of his  
13 efforts in furthering our agenda and our interest.  
14 So we welcome both of you.

15 I would also like to introduce to you  
16 Pamela Patenaude, who is the Assistant Secretary  
17 for Community Planning and Development at HUD.  
18 Today she is serving in the stead of Secretary  
19 Jackson, and we welcome you, Pamela.

20 DIRECTOR PATENAUDE: Thank you,  
21 Mr. Chairman.

22 JOHN KENNEDY: As a preliminary matter, do

1 you have a copy of the written designation?

2 DIRECTOR PATENAUE: I do, John.

3 CHAIRMAN ROSENFELD: Good morning,  
4 everyone. I call this meeting to order of the  
5 Board of Directors of the Federal Housing Finance  
6 Board. Today we will have an open session,  
7 followed immediately by a closed session where the  
8 Board will receive updates of examination and  
9 supervisory findings. We now need to vote to  
10 approve closing the latter portion of today's  
11 meeting, as required by the Sunshine Act and the  
12 Finance Board regulations. And since the closed  
13 portion of today's meeting will contain sensitive  
14 and confidential bank examination information, I  
15 would ask for a motion to seal the transcript of  
16 this portion of the meeting. Director Castaneda?

17 DIRECTOR CASTANEDA: Yes, Mr. Chairman.  
18 I move to close the portion of today's meeting at  
19 which we will receive updates of examination and  
20 supervisory findings, and further, that we  
21 determine that the record and transcript of this  
22 closed portion of the meeting be kept

1 confidential.

2 CHAIRMAN ROSENFELD: Thank you for the  
3 motion. Is there any discussion of the motion,  
4 any discussion? Do I have a second for the  
5 motion?

6 DIRECTOR CASTANEDA: Second.

7 DIRECTOR BACINO: Second.

8 CHAIRMAN ROSENFELD: Thank you,  
9 Mr. Bacino. Would the Secretary please call the  
10 roll on the motion?

11 MS. WILLIS: On the item before the Board, Director  
12 Bacino, how do you vote?

13 DIRECTOR BACINO: Yes.

14 MS. WILLIS: Director Castaneda?

15 DIRECTOR CASTANEDA: Yes.

16 MS. WILLIS: Director Mendelowitz?

17 DIRECTOR MENDELOWITZ: Yes.

18 MS. WILLIS: Director Patenaude?

19 DIRECTOR PATENAUDE: Yes.

20 MS. WILLIS: Chairman Rosenfeld?

21 CHAIRMAN ROSENFELD: Yes. The motion  
22 has carried and the subsequent portion of our

1 meeting will be closed and its transcript will  
2 remain closed and confidential. Thank you. Let  
3 us now turn to the public portion of today's  
4 meeting. The first item is the Fiscal Year 2007  
5 Agency Budget. Who will be making the  
6 presentation?

7 MS. HOFMANN: Mr. Chairman, Mark David,  
8 the Finance Board's Budget Officer, will be making  
9 the presentation on the Fiscal '07 budget.

10 MR. DAVID: Thank you, Judith. Good  
11 morning. I'd like to start off by just saying  
12 that we have worked closely with the individual  
13 offices to produce a budget that provides the  
14 necessary resources to carry out the agency's  
15 regulatory mission in a cost effective and  
16 efficient manner.

17 With that said, the proposed Fiscal Year  
18 2007 Budget for the Federal Housing Finance Board  
19 is \$35,852,260. The majority of the proposed  
20 budget is for salaries and benefits. This counts  
21 for 23.9 million or 67 percent of the total  
22 budget. This covers the salaries and benefits for

1 a total of 143.5 positions for fiscal year 2007.  
2 Ninety-nine of these positions are within the Office of  
3 Supervision, which is 69 percent of the agency's  
4 total staff. Eight point eight million or 25 percent of the  
5 budget is to cover rent, information technology,  
6 and travel. The majority of the travel is  
7 dedicated to support the supervision and  
8 examination function in fiscal year 2007.  
9 Combined salaries and benefits, rent, information  
10 technology, and travel make up 92 percent of the  
11 proposed budget request. The remaining 3.1  
12 million or 8 percent of the proposed budget is  
13 for the following: Professional services,  
14 training, the operating reserve, and other  
15 expenses.

16 This proposed budget is approximately  
17 \$\$22,000 less than the fiscal year 2006 budget. For  
18 fiscal year 2006, we're projected to underspend  
19 our budget because of two main reasons; first, we  
20 didn't fill all of the positions that we had  
21 budgeted for in fiscal year 2006, causing a  
22 surplus in the salaries and benefits category;

1 second, we used approximately 1.7 million in  
2 tenant allowances to pay for monthly rents in  
3 fiscal year 2006.

4 Combined, these two factors will cause  
5 us to underspend our current budget by  
6 approximately 15 percent. This covers the key  
7 components of the proposed fiscal year 2007  
8 budget. At this point, we'd like to answer any  
9 questions you might have.

10 CHAIRMAN ROSENFELD: Do any other Board  
11 members have any questions or comments? I would  
12 merely point out to those of you who follow the  
13 Home Loan Bank function of this Board, this budget  
14 is the third budget that I'm aware of, and the  
15 number every year is remarkably similar, which if  
16 nothing else, demonstrates that you can run this  
17 Board, under its authority, can run an  
18 organization in an appropriate business-like  
19 manner. And I commend my colleagues on the Board,  
20 as well as our professional staff for really doing  
21 an excellent job at running this entity in an  
22 intelligent, business-like fashion, so I commend

1 all of you. If there's nothing else, I would  
2 accept the motion to approve the resolution.

3 DIRECTOR CASTANEDA: Actually, I have a  
4 question, Mr. Chairman, if I may. I saw that in  
5 the budget, we are going to be doing a  
6 compensation review. What would be the scope of  
7 this review; will it cover all employees over  
8 certain grade, or can you tell me a little bit  
9 about it?

10 MS. HOFMANN: It's going to be a  
11 compensation study that's going to look at our,  
12 not only salaries, but our benefit package also in  
13 total. By statute, we're required to be  
14 competitive with the other FIRREA agencies, and  
15 so --

16 DIRECTOR CASTANEDA: So by law, we have  
17 to be competitive?

18 MS. HOFMANN: Yes; and we have not done  
19 one -- we did one in 2002 that was completed in  
20 2003, so we've not done one since then. So it's  
21 going to be a comparison of our total compensation  
22 to ensure that we are competitive and can retain

1 qualified staff that we need to. We are in the  
2 process right now of drawing up the request for a  
3 proposal to go out to hire a contractor to do the  
4 survey. And I will be working with primarily  
5 Steve Cross and Christie in terms of what some of  
6 the issues are we're going to look at and the key  
7 positions. We will probably not survey every  
8 position, but concentrate on the key ones that we  
9 need to look at.

10 DIRECTOR CASTANEDA: Okay. Well, given  
11 the trouble then we had had filling the accounting  
12 and other positions in the past, I have to say  
13 that I'm very glad to see in the budget and this  
14 Board will conduct this compensation review,  
15 again, to make sure that we are -- our salaries  
16 here are comparable with other agencies.

17 I know I always sound like a broken  
18 record, but I'm always concerned the accounting  
19 side, because I know the banks have had their own  
20 problems in registering with the SEC, but we have  
21 had some of our own problems here.

22 In the past, I have always encouraged to

1 put some money aside, not only to have staff  
2 resources, but also to obtain outside expertise on  
3 a contract basis, if needed, to help us get  
4 through the transition SEC registration process.

5 And I know we still have a few remaining  
6 issues out there, none the least of which is  
7 getting the system back to publish the complete  
8 and accurate combined financial statement, so I  
9 was very pleased to hear about this compensation  
10 review. That's my comment, Mr. Chairman.

11 DIRECTOR PATENAUE: Mr. Chairman --

12 CHAIRMAN ROSENFELD: Pamela.

13 DIRECTOR PATENAUE: Thank you. Judith,  
14 how will the reduction in FTE's impact the Board?

15 MS. HOFMANN: It's actually an increase  
16 from the actual.

17 DIRECTOR PATENAUE: From 2006 levels?

18 MS. HOFMANN: Yeah, it's an increase from  
19 the 2006 actual level. We're approximately 20  
20 positions under what we'll finish the fiscal year  
21 at, so we do have an increase. It's a decrease  
22 from what had been in the budget last year. But a

1 number of offices -- because positions hadn't been  
2 filled.

3 For instance, the Board of Directors has  
4 a decrease of two positions, my office has a  
5 decrease of two positions, the Office of General  
6 Counsel has a decrease of one position. So we  
7 just looked at what had been in the budget  
8 proposed that had not been filled during the  
9 fiscal year.

10 DIRECTOR PATENAUDE: Thank you.

11 DIRECTOR MENDELOWITZ: I just want to  
12 comment that this is probably the best budget  
13 submission that I've seen in the time that I've  
14 been on the Board of Directors of the Finance  
15 Board. It's the most complete, it's the most  
16 carefully developed, and it has, I think without  
17 exception, all of the information necessary to  
18 both support and justify the budget request and to  
19 explain how the money is being spent, so that when  
20 the Board votes on it, we have all of the  
21 information necessary. And I just want to express  
22 my appreciation and commend the staff for doing an

1 absolutely outstanding job this year.

2 MR. DAVID: Thank you, sir.

3 MS. HOFMANN: Thank you, Allan. And that  
4 credit really does go to Mark David, our Budget  
5 Officer. He's put in a tremendous amount of  
6 effort in revising the process that was here when  
7 he came on as the Budget Officer.

8 CHAIRMAN ROSENFELD: If there's nothing  
9 else, I will accept the motion to approve the  
10 resolution.

11 DIRECTOR PATENAUDE: Second.

12 CHAIRMAN ROSENFELD: Does anybody have  
13 a --

14 DIRECTOR PATENAUDE: Oh, I'm sorry.

15 CHAIRMAN ROSENFELD: Mr. Mendelowitz?

16 DIRECTOR MENDELOWITZ: I so move.

17 CHAIRMAN ROSENFELD: Do I have a second?

18 DIRECTOR PATENAUDE: I'm sorry. I can  
19 second it now?

20 CHAIRMAN ROSENFELD: Would the Secretary  
21 please call the roll?

22 MS. WILLIS: On the item before the

1 Board, Director Bacino, how do you vote?

2 DIRECTOR BACINO: Yes.

3 MS. WILLIS: Director Castaneda?

4 DIRECTOR CASTANEDA: Yes.

5 MS. WILLIS: Director Mendelowitz?

6 DIRECTOR MENDELOWITZ: Yes.

7 MS. WILLIS: Director Patenaude?

8 DIRECTOR PATENAUDE: Yes.

9 MS. WILLIS: Chairman Rosenfeld?

10 CHAIRMAN ROSENFELD: Yes. The motion is  
11 adopted. The second item is the Strategic Plan  
12 and Annual Performance Budget. Who will be making  
13 that presentation?

14 MR. CROSS: Mr. Chairman, Gwen Grogan,  
15 Associate Director in the Office of Supervision,  
16 will give this presentation.

17 MS. GROGAN: Good morning. The  
18 Government Performance and Results Act, GPRA,  
19 requires federal agencies to prepare a Strategic  
20 Plan covering a period of not less than 5 years  
21 and requires that it be updated and revised at  
22 least every 3 years. The Finance Board's

1 first Strategic Plan was approved in 1997. The  
2 Agency has revised its Strategic Plan in 2001,  
3 2003, and 2004.

4 For your consideration, there's a  
5 Strategic Plan covering the years 2007 through  
6 2012. This Strategic Plan serves as a road map  
7 for the Agency's Risk Focused Supervisory Program.  
8 Rather than simply rolling forward the previous  
9 Strategic Plan, we took a fresh look.

10 Given that the Finance Board has a  
11 single program, the supervision of the Federal  
12 Home Loan Banks and the Office of Finance, we  
13 believe that we should further refine our  
14 strategic goals, and outcomes, means, and  
15 strategies, and performance goals.

16 The development of this Strategic Plan  
17 was a collaborative effort. A cross office and  
18 cross divisional working group was formed last  
19 winter to develop ideas for revising the plan.  
20 Based on the working groups' input and the Office  
21 of Supervision Executive Management's  
22 participation, a draft document was circulated to

1 key personnel within the Office of the General  
2 Counsel and the Office of Management.

3           This Strategic Plan sets forth the  
4 Agency's mission, vision, and values. These  
5 remain unchanged from the previous Strategic Plan.  
6 The proposed Strategic Plan sets forth two  
7 strategic goals and the means and strategies that  
8 determine the processes, skills, technologies, and  
9 resources that the Finance Board will use to  
10 achieve its strategic goals.

11           The proposed plan identifies two  
12 strategic goals for the Agency. The Office of  
13 Management and Budget's guidance requires that an  
14 agency's strategic goals be outcome related; that  
15 is, the goals described, the intended result in  
16 carrying out the program's activity.

17           With the Office of Management and  
18 Budget's guidance in mind, the strategic goals  
19 support achievement of the Agency's mission, which  
20 is to ensure that the Federal Home Loan Banks are  
21 safe and sound, so that they serve as a reliable  
22 source of liquidity and funding for the nation's

1 housing and finance community investment needs.  
2 We established one strategic goal as the Federal  
3 Home Loan banks operate safely and soundly. The  
4 second strategic goal we established is the  
5 Affordable Housing and Community Investment  
6 Program so the Federal Home Loan Banks operate  
7 effectively and efficiently. Encompassed within  
8 these strategic goals are the Finance Board's  
9 statutory duties and mission, as articulated in  
10 the Bank Act, those being, to ensure that the  
11 Federal Home Loan Banks operate in a financially  
12 safe and sound manner, carry out their housing  
13 finance mission, and remain adequately capitalized  
14 and able to raise funds in the capital markets.

15 Consistent with these strategic goals,  
16 we developed strategic outcomes. The strategic  
17 outcomes are that the banks effectively identify  
18 and manage risk, remain adequately capitalized,  
19 and foster the development of owner occupied  
20 affordable rental housing for eligible very low,  
21 low, and moderate income households.

22 Consistent with the strategic plan, we

1 have also prepared for your consideration the 2007  
2 annual Performance Budget. In the 2007  
3 Performance Budget, roughly five-sixths of the  
4 Finance Board's resources are allocated to the  
5 first strategic goal, that the banks operate  
6 safely and soundly, while the remaining one-sixth  
7 of the Finance Board's resources are allocated to  
8 the second strategic goal. Using performance  
9 metrics set forth in the 2007 Performance Budget,  
10 we will measure our success in achieving the  
11 strategic goals and outcomes set forth in the  
12 Strategic Plan.

13 We have established three performance  
14 measures with respect to the first strategic goal.  
15 The first performance measure is that the  
16 principal examination findings are addressed to  
17 the satisfaction of the Finance Board prior to the  
18 next examination. At a minimum, a bank must  
19 develop an action plan to correct issues  
20 identified by principal examination findings prior  
21 to the start of the next examination.

22 Thereafter, the Finance Board will

1 monitor the Federal Home Loan Banks' progress in  
2 implementing the action plan through follow-up  
3 reviews and the subsequent annual on-site  
4 examinations.

5           Where warranted, the Finance Board may  
6 enter into supervisory agreements with Federal  
7 Home Loan banks and its boards of directors.  
8 Supervisory agreements are signed or revised after  
9 October 1, 2006, will include specific action  
10 plans and time frames to remedy deficiencies.

11           The second performance measure, namely  
12 that, the supervisory or compliance issues  
13 resulting in supervisory agreements are corrected  
14 by the Federal Home Loan Banks within required  
15 time frames gauges the success of the supervisory  
16 agreement.

17           The third performance measure, that the  
18 Finance Board completes assessment of the new  
19 business activity and capital plan amendment  
20 request within an average of 45 days of receipt of  
21 a complete proposal, is intended to instill  
22 additional discipline, in our supervision of the

1 Federal Home Loan Banks by reducing our review  
2 time on average to 45 days, which is down from 60  
3 days currently in an effort to be a responsive  
4 regulatory and/or practicable to reduce regulatory  
5 burden and costs to the Federal Home Loan Banks.

6 With respect to the second strategic  
7 goal, which addresses the Federal Home Loan Banks  
8 Affordable Housing and Community Investment  
9 Programs, we have established as a single  
10 performance measure that the affordable housing  
11 funds are distributed as approved in the  
12 affordable housing program application.

13 This measure is intended to address the  
14 timely and appropriate use of affordable housing  
15 program subsidy, which will provide funds for the  
16 creation and rehabilitation of housing for  
17 eligible, very low, low, and moderate income  
18 households. These are all new performance  
19 measures, and as such, will apply to activities  
20 occurring after October 1, 2006.

21 Our success in achieving the measures  
22 will be addressed in the Finance Board's 2007

1 Performance and Accountability Report.

2 We believe that the proposed Strategic  
3 Plan and the proposed 2007 Performance Budget  
4 provides the context for a strong supervisory  
5 program that is risk focused, effective, and  
6 efficient. We are happy to answer any questions.

7 CHAIRMAN ROSENFELD: Do any of the other  
8 Board members wish to comment?

9 DIRECTOR CASTANEDA: I -- no, please. I  
10 always have something to say.

11 DIRECTOR BACINO: No, go ahead, please.

12 DIRECTOR CASTANEDA: Mr. Chairman, I  
13 really would like to commend Gwen and Meg for  
14 doing a fine job, improving and streamlining our  
15 Strategic Plan and other GPRA reports. Did I  
16 pronounce it right? Okay. These documents read  
17 clearly and I think are really to the point  
18 emphasizing first, what it is and this agency is  
19 and should be all about it, second, that we will  
20 do what we will do to work toward our strategic  
21 goals, and finally, how we will measure how well  
22 we're doing.

1           The other thing then, I think we have  
2 done very, rightfully so this year, is that the  
3 initiative to post draft virturance on our web  
4 site. We have never done it before, right?

5           MS. GROGAN: We have done it at least  
6 one time.

7           DIRECTOR CASTANEDA: Okay. Well, I  
8 think that's very important so the public can  
9 review and comment on it. I thought that was a  
10 good innovation, and I always believe that we need  
11 to do anything we can to be more transparent in  
12 making sure that the people know what we're doing  
13 at these agencies, so we need to keep that. Thank  
14 you so much.

15           CHAIRMAN ROSENFELD: Director Bacino?

16           DIRECTOR BACINO: Well, kind of building  
17 on a little what Board member Castaneda said, we  
18 did post on the internet, correct, for comments?  
19 Did we take any other steps to kind of vet this to  
20 the banks or any other interested parties?

21           MS. HAWLEY: We work with (inaudible)  
22 from the Chairman's office to distribute the draft

1 in July to interested parties, and he has a global  
2 email that he sends out to --

3 DIRECTOR BACINO: (inaudible) I know,  
4 everybody.

5 MS. HAWLEY: To the press, as well as --

6 DIRECTOR BACINO: Okay. I mean really  
7 what I want to make sure, instead of kind of  
8 building on that question, is making sure that we  
9 get comments from everybody who might be  
10 interested or thinks they're interested or would  
11 want to be interested, and provided we do that, I  
12 think we're doing our job in that area.

13 MS. HAWLEY: We do know that people read  
14 it; we do not receive comments.

15 DIRECTOR BACINO: That's fine, too,  
16 that's always the best. You read it, I didn't  
17 hear about it.

18 CHAIRMAN ROSENFELD: Director  
19 Mendelowitz?

20 DIRECTOR MENDELOWITZ: Yeah, thank you,  
21 Mr. Chairman. GPRA is one of those pieces of  
22 legislation which, in principal, I think is right

1 on the mark. The objectives, the goals, the  
2 principals are absolutely correct. For too long,  
3 those in government responsible for spending  
4 public funds looked at the money being spent as  
5 the outcome rather than what was accomplished  
6 through the program and the expenditure monies.

7 And one of the reasons why I believe in  
8 the principals of GPRA is that it's consistent  
9 with what I learned in the seventh grade in  
10 science, and in seventh grade science, I learned  
11 that if you push on a boulder all day, if at the  
12 end of the day, no matter how tired you are, no  
13 matter how perspired, no matter how dirty from  
14 your effort, if the boulder hasn't moved, you  
15 haven't done any work.

16 And it's the same thing in government,  
17 no matter how much money you spend, if you don't  
18 have an outcome, you haven't accomplished  
19 anything. So the principals are great, but like  
20 many complex and laudatory piece of legislation  
21 that have good goals and good principals in  
22 execution, there are many times problems.

1           And one of the big problems with GPRA is  
2           that the emphasis on measurement pushed agencies  
3           to put down goals and things to be measured that  
4           were easy to measure rather than things that  
5           should be measured because there were important  
6           outcomes, and it's understandable.

7           I mean if you look at the national  
8           income and product accounts, government is really  
9           handled in a totally inappropriate way. All  
10          sectors of the economy except government get  
11          measured on the basis of outcome. You know, you  
12          don't measure the value of a car on the basis of,  
13          for national income and product account purposes,  
14          for how much people spend building the car, you  
15          measure it by the value of the car, and that value  
16          is measured by what people pay to buy it, and  
17          that's the output, that's the outcome. And so,  
18          you know, I like it, and I also appreciate the  
19          challenge that every agency, including the Finance  
20          Board, faces when trying to come up with  
21          measurable outcomes that are both significant and  
22          important and measurable.

1           And in that light, I would like just one  
2 clarification that relates to the measurement of  
3 goal one. It says on page 12, in the last  
4 paragraph, "Where warranted, the Finance Board may  
5 enter into a supervisory agreement with an FHL  
6 bank and its board of directors. Supervisory  
7 agreement signed or revised after October 1, 2006  
8 will include specific action plan and time frames  
9 to remedy deficiencies."

10           And I'm really looking for a  
11 clarification on this, because when I look back on  
12 the supervisory agreement that we've signed with a  
13 couple of banks, and they're all in the public  
14 domain, so I'm not releasing any secret  
15 supervisory information, but many of those  
16 conditions and provisions and the written  
17 agreements say that the bank in question will hire  
18 an outside consultant to look at risk management  
19 by a certain date and complete the results by a  
20 certain date, and the bank will hire a consultant  
21 to look at the quality of their risk management  
22 people, hire a consultant to look at the quality

1 of the bank's executive management.

2 And a lot of the provisions in the  
3 written agreements really went to hiring outside  
4 experts to assess the appropriateness of policies,  
5 procedures, and the qualifications of people  
6 implementing those policies and procedures. And  
7 is there anything about the way this measurable  
8 goal is written that suggests we might change the  
9 form of the written agreements?

10 Where it says, include specific action  
11 plans and time frames, because I would say that if  
12 we define specific action plan as a requirement to  
13 hire a consultant to assess something and then do  
14 it by a certain date, that's a specific action and  
15 a time frame, but it's not a remedy of the  
16 deficiency, it's the outcome of the study that's a  
17 remedy deficiency.

18 So is there an intent here to change the  
19 written agreement form that we've used in the  
20 past, or is what we've done in the past perfectly  
21 consistent with how this is described?

22 MR. CROSS: Let me start, because we've

1 had a lot of discussions about precisely the issue  
2 I think you were getting at in your remarks,  
3 Director Mendelowitz, which is that GPRA requires  
4 that we focus on outcomes, and of course, what  
5 part of the problem is, there are a lot of  
6 factors, not just what the Finance Board does,  
7 that influences the outcome, so how do we get  
8 something that is meaningful in what we do and  
9 sort of conforms to the spirit of GPRA?

10 At one level, I think that what we have  
11 done in the past will largely, but not completely  
12 satisfy this goal. As you've stated, we have  
13 often had time frames for certain actions to take  
14 place, and we would expect to continue to have  
15 that as part of this goal. Our intent, however,  
16 is to try to get at the outset of the discussion  
17 with our Board and with the bank's board to one  
18 other issue, which is, so how long is this bank  
19 going to be under a written agreement? Is this a  
20 problem that can be solved in 24 months, 36  
21 months, or 48 months?

22 Try to get an idea, not just what will

1 be done in the first six months, but will the work  
2 of the first six months give rise to correctives  
3 over time, and will there be, in effect,  
4 milestones that will give us a sense of whether  
5 the reports that the consultants have prepared and  
6 the actions that the bank has taken, often subject  
7 to our approval, are actually beginning to bear  
8 fruit, and at what time frame should they bear  
9 fruit.

10 To be honest with you, we discussed  
11 whether we should say, in our goal, a bank should  
12 be out from under a written agreement within 24  
13 months or 36 months of when it was adopted, and we  
14 felt that that was inappropriate, not knowing what  
15 the nature of the enforcement action is or the  
16 specifics of the case.

17 But I believe that our intent was that  
18 given the specifics of the case and the nature of  
19 the enforcement action, when we go to the bank and  
20 talk about all of the immediate remedies, that we  
21 have to have an idea, and the bank has to have an  
22 idea of when will this bear fruit, when will this

1 bank be prepared to, if everything goes according  
2 to plan, be relieved of its obligations under the  
3 written agreement.

4           So my short answer, to summarize, is  
5 that I think a written agreement in the future  
6 would have the elements that we have seen up to  
7 this point, as well as some understanding of the  
8 likely time frame by which this bank and our Board  
9 can expect that the bank will be out from under  
10 the written agreement, which has not been in place  
11 in the past.

12           DIRECTOR MENDELOWITZ: Okay.

13           CHAIRMAN ROSENFELD: Thank you.

14           DIRECTOR PATENAUDE: Mr. Chairman, I  
15 have a question. For what period of time was the  
16 Strategic Plan posted for public comment?

17           MS. HAWLEY: It went out in the middle  
18 of July; it was for 30 days.

19           DIRECTOR PATENAUDE: Posted for 30 days?

20           MS. GROGAN: Well, it's actually still  
21 up there, and we would have certainly welcomed  
22 comments up until --

1 DIRECTOR PATENAUDE: Today?

2 MS. GROGAN: Today, yes.

3 DIRECTOR PATENAUDE: Okay. Thank you.

4 CHAIRMAN ROSENFELD: Okay. If there's  
5 nothing else, I would accept a motion to approve  
6 the resolution. Director Mendelowitz?

7 DIRECTOR MENDELOWITZ: I so move it.

8 CHAIRMAN ROSENFELD: Do I have a second?

9 DIRECTOR BACINO: Second.

10 CHAIRMAN ROSENFELD: Director Bacino,  
11 okay. Would the Secretary please call the roll?

12 MS. WILLIS: On the item before the  
13 board, Director Bacino, how do you vote?

14 DIRECTOR BACINO: Yes.

15 MS. WILLIS: Director Castaneda?

16 DIRECTOR CASTANEDA: Yes.

17 MS. WILLIS: Director Mendelowitz?

18 DIRECTOR MENDELOWITZ: Yes.

19 MS. WILLIS: Director Patenaude?

20 DIRECTOR PATENAUDE: Yes.

21 MS. WILLIS: Chairman Rosenfeld?

22 CHAIRMAN ROSENFELD: Yes; the motion is

1 adopted. The third item on the agenda is a  
2 request by the Office of Supervision to submit for  
3 publication in the Federal Register a notice  
4 requesting comments a proposed Federal Home Loan  
5 Bank Rating System. Who will be making that  
6 presentation?

7 MR. CROSS: Mr. Chairman, Tony Cornyn,  
8 who is an Associate Director in the Office of  
9 Supervision.

10 MR. CORNYN: Thank you, Mr. Chairman.  
11 Today we are seeking the Board's approval for a  
12 comment on a proposed Federal Home Loan Bank  
13 Rating System. The proposed rating system would  
14 be used in rating the financial condition and  
15 performance of the 12 Home Loan banks and the  
16 Office of Finance. We believe that the rating  
17 system will enhance communications between the  
18 Office of Supervision and the banks, as well as  
19 the Office of Finance by making the examination  
20 process more transparent.

21 An important by-product of the proposed  
22 rating system is that it shall also promote

1 greater consistency and discipline to the  
2 examination process itself. Under the rating  
3 system, each bank would be assigned a composite  
4 rating of one to four. A one rating indicates the  
5 lowest degree of supervisory concern, while a four  
6 rating indicates the highest degree of supervisory  
7 concern.

8 The composite rating of each bank would  
9 be based on an evaluation and rating of five key  
10 components; they are corporate governance, market  
11 risk, credit risk, operational risk, and financial  
12 condition and performance.

13 Each of the five components would also be assigned  
14 be a rating of one to four. The rating of each of  
15 the five components would be used to compile the  
16 composite rating. The composite rating of an  
17 institution would reflect the underlying  
18 components, but it would not be a simple  
19 arithmetic average of the component ratings.

20 Instead, the relative importance of each  
21 component would be determined on a case by case  
22 basis by examiner judgement. As I mentioned, we

1 will also assign a rating to the Office of  
2 Finance.

3 The composite rating for the Office of  
4 Finance would be based on two of the five  
5 components, corporate governance and operational  
6 risk. In summary, the proposed rating system is  
7 intended to provide for greater transparency  
8 regarding our examination conclusions, better  
9 communication between the Office of Supervision  
10 and the banks and the Office of Finance, and more  
11 discipline and consistency in the examination  
12 process.

13 Mr. Chairman, we recommend that the  
14 Board publish a proposed rating system for a 30  
15 day comment period. And it is our intention to  
16 finalize the rating system by year end so that we  
17 can implement the system in 2007.

18 CHAIRMAN ROSENFELD: Thank you very  
19 much. Any other Board members wish to comment?

20 DIRECTOR BACINO: I have one question.  
21 Tony, I'm glad that we're moving toward a system  
22 that would take into account the unique nature of

1 our Home Loan banks, and obviously, always for  
2 greater transparency. What measures are you guys  
3 taking that would ensure consistency among the  
4 examination teams?

5 MR. CORNYN: Well, the rating system  
6 itself outlines the factors that we will consider  
7 in rating each of the components. And, for  
8 example, it discusses what factors to look at to  
9 determine the level of risk for market risk or  
10 operational risk or credit risk, as well as what  
11 factors to look at to determine the quality of  
12 risk management, and we think that guidance will  
13 promote greater consistency.

14 MR. CROSS: Could I just add briefly; in  
15 our submitted and now approved budget, there will  
16 be a unit that would report directly to me that  
17 would be responsible for quality assurance  
18 reviews. That unit will be primarily focused, but  
19 not exclusively focused, on reviewing our  
20 examination work papers and the support they lend  
21 to both the identification of areas that will be  
22 scoped into the examination and the conclusions

1 the examiners reach with respect to those areas.

2 It will not be a second guessing  
3 operation, but it will be an operation that says,  
4 did you ask reasonable questions and were you  
5 analytical in your evaluation of the answers you  
6 receive to those questions. Part and parcel of  
7 that necessarily must be, do the findings and  
8 conclusions in the work papers and as expressed in  
9 the report of examination support the ratings  
10 assigned by area on a composite basis. So that's  
11 another aspect of what we are going to do.

12 That will be done out of my office on an  
13 after the fact basis. In addition, Tony, working  
14 on the operations side, and Carrie Walter and her  
15 staff working on the supervisory policy side, will  
16 have an ongoing quality control program in which  
17 some of that work, individual examiners work will  
18 be reviewed in the process of preparing the final  
19 report and assigning the ratings.

20 DIRECTOR BACINO: Okay, great, thanks.  
21 That's all I have.

22 CHAIRMAN ROSENFELD: Director Castaneda.

1           DIRECTOR CASTANEDA: Tony, I just have a  
2 couple of comments. I heard you use the word  
3 transparency and discipline, and I couldn't agree  
4 more with you. I think in the interest of  
5 transparency, I think it's a good practice for  
6 this agency to put the proposed rating system out  
7 for comment so that people know more about what  
8 we're doing here and have a chance to provide  
9 constructive feedback. I know we didn't have to  
10 put it in the Federal Register as a legal matter.

11           Again, I do believe in transparency as a  
12 guiding practice, and what's good for the banks  
13 regulate is also good for us as a regulator. And  
14 second, and perhaps this is the most important  
15 fact of this rating system, is implementing a  
16 system that will be adding discipline to our  
17 staff, and we will be imposing on itself in  
18 developing the individual bank ratings. So I  
19 think -- I was very pleased. I definitely will be  
20 voting yes on this.

21           CHAIRMAN ROSENFELD: Okay. Any other  
22 comments? Director Mendelowitz.

1                   DIRECTOR MENDELOWITZ: Yeah; we  
2                   currently have in place a rating system that lacks  
3                   the transparency that this has, and instead of  
4                   providing numeric grades, there are summary  
5                   descriptors, and there are four different words  
6                   used to describe the consensus of what the exam  
7                   report represents. And the highest rating you can  
8                   get under the current system is satisfactory. And  
9                   when you read the exact wording in this proposed  
10                  rating system, the word "satisfactory" shows up  
11                  most often with respect to a rating of two, the  
12                  second highest rating. And does that mean that  
13                  the new system -- anybody who got a satisfactory  
14                  under the old system, if they got the same  
15                  examination report, would expect to get a two, or  
16                  are we changing the metrics? I'm just trying to  
17                  get some sort of clarification with respect to  
18                  this.

19                  MR. CROSS: Could I start the answer?  
20                  That's an accurate and good observation and  
21                  question. I can give a short answer to that. The  
22                  answer is, no, a bank that has received a

1 conclusionary rating of satisfactory under our  
2 current system would not be rated a two under this  
3 system because the word satisfactory is used in  
4 the descriptor of a two rating.

5 A number of us in the Office of  
6 Supervision, including executive management and  
7 examiners, felt that we needed to acknowledge that  
8 a well run organization should be characterized as  
9 something better than satisfactory, and that a  
10 satisfactory, in effect, what is characterized as  
11 satisfactory under the current system would get  
12 the appropriate descriptor, which is good or  
13 excellent. What has been characterized as fair  
14 under the current system will get a descriptor of  
15 satisfactory.

16 DIRECTOR MENDELOWITZ: This agenda item  
17 was originally on the agenda for the August  
18 meeting, and it was pulled from the agenda, and  
19 when it was pulled, you read a statement related  
20 to why it was pulled, and people reporting on what  
21 happened at the meeting felt that they had to try  
22 to read the tea leaves, and they were trying to

1 read into your statement, Mr. Chairman, what  
2 exactly the meeting was, and they called various  
3 people on the Board of Directors asking what was  
4 going on, trying to divine some sort of secret  
5 agenda or something, and my understanding was, the  
6 wording you used when the agenda item was pulled  
7 was simply formulaic, in other words, if we have  
8 an agenda item and we pull it, that's just the  
9 standard wording; is that correct? Okay.

10 So there was nothing to read into the  
11 statement other than the fact that this is the  
12 formulaic wording used when an agenda item is  
13 pulled. And secondly, the only reason why it was  
14 pulled was that the Board of Directors, members of  
15 the Board of Directors felt they needed more time  
16 to work on the proposed write-up to get some  
17 revisions and enhancements, and there was nothing  
18 more to it than that.

19 So I really wanted to get that on the  
20 record, because I know there was a lot of  
21 questions, and a number of members of the Board of  
22 Directors have been called as if there was

1 something sort of secret and nefarious going on,  
2 and it was -- it was a very simple story.

3 DIRECTOR CASTANEDA: And if I may add  
4 Director Mendelowitz had very good points and suggestions  
5 to make this final proposal.

6 DIRECTOR MENDELOWITZ: Thank you.

7 CHAIRMAN ROSENFELD: If there's nothing  
8 else, I would accept the motion to approve the  
9 request by the Office of Supervision and to allow  
10 staff to make technical and conforming changes to  
11 the notice.

12 DIRECTOR BACINO: So moved.

13 CHAIRMAN ROSENFELD: Is there a second?

14 DIRECTOR PATENAUDE: Second.

15 CHAIRMAN ROSENFELD: Thank you, Director  
16 Patenaude. Would the Secretary please call the  
17 roll?

18 MS. WILLIS: On the item before the  
19 Board, Director Bacino, how do you vote?

20 DIRECTOR BACINO: Yes.

21 MS. WILLIS: Director Castaneda?

22 DIRECTOR CASTANEDA: Yes.

1 MS. WILLIS: Director Mendelowitz?

2 DIRECTOR MENDELOWITZ: Yes.

3 MS. WILLIS: Director Patenaude?

4 DIRECTOR PATENAUDE: Yes.

5 MS. WILLIS: Chairman Rosenfeld?

6 CHAIRMAN ROSENFELD: Yes; the motion is  
7 adopted. The fourth item for consideration is a  
8 final regulation incorporating amendments to the  
9 Affordable Housing Program. Who will be making  
10 the presentation?

11 MR. CROSS: Mr. Chairman, Gwen Grogan  
12 will be giving the presentation, representing the  
13 Office of Supervision, and Sharon Like will be  
14 party to the presentation, representing the Office  
15 of General Counsel.

16 MS. GROGAN: Good morning again. We're  
17 here before you to recommend the adoption of  
18 amendments to the Finance Board's regulation  
19 governing the operation of the Affordable Housing  
20 Program. The Affordable Housing Program, the  
21 final rule for your consideration revises the  
22 current Affordable Housing Program regulations by

1 removing certain prescriptive requirements,  
2 clarifying certain operational requirements,  
3 providing additional discretionary authority to  
4 the Federal Home Loan Banks in certain areas,  
5 removing certain authorities, and otherwise  
6 streamlining and reorganizing the regulations.

7           Former Director Leichter, while he was a  
8 member of this Board, helped to lead the  
9 initiative to revise the current Affordable  
10 Housing Program regulation. In so doing, our  
11 objectives were to make the regulation more user  
12 friendly in the organization of program features  
13 and to streamline the regulatory requirements to  
14 focus on outcomes rather than processes.

15           Our ultimate goals were to provide  
16 greater clarity and flexibility to the regulation  
17 so that the Federal Home Loan Banks could carry  
18 out their programs more effectively and  
19 efficiently. The Affordable Housing Program has  
20 played an important role in facilitating the  
21 Federal Home Loan Banks support of their members  
22 efforts to meet the housing needs of very low,

1 low, and moderate income households in their  
2 communities. The strength of the Affordable  
3 Housing Program lies in its capacity to leverage  
4 additional public and private resources for  
5 housing.

6 The Affordable Housing Program subsidies  
7 have proven effective in financing projects that  
8 present underwriting challenges, such as projects  
9 for the homeless and special needs populations,  
10 which may include persons with disabilities and  
11 the elderly.

12 The Affordable Housing Program has also  
13 been used effectively in conjunction with low  
14 income housing tax credits by filling financing  
15 gaps for these projects that are such an important  
16 source of rental housing for very low income  
17 households.

18 The Affordable Housing Program  
19 regulation has generally reflected a prescriptive  
20 approach, which is appropriate for rules  
21 implementing a newly created program. As the  
22 program has matured, however, the Finance Board

1 periodically has revised the regulations, in part  
2 to provide greater authority to the Federal Home  
3 Loan banks in managing their individual programs,  
4 and in part to codify lessons learned through  
5 oversight of the Federal Home Loan Banks'  
6 operations. Based on the horizontal reviews of  
7 the Federal Home Loan Banks' Affording Housing  
8 Programs conducted in 2003 and 2004, areas were  
9 identified in the regulation that could be revised  
10 to provide additional enhancement to the program.  
11 Accordingly, on December 28, 2005, the Finance  
12 Board published amendments to the Affordable  
13 Housing Program for 120 comment period. The  
14 Finance Board received 59 comment letters  
15 addressing 79 proposed changes and issues. Staff  
16 considered all the comments received.

17 Many of the comments expressed support  
18 for the proposed changes to the program as set  
19 forth in the proposed regulation. A number of  
20 revisions have been made to the rule based on the  
21 proposed regulation and the comments received on  
22 the proposed rule. I would like to highlight some

1 of the key revisions.

2 First, the final rule incorporates  
3 additional definitions into the regulation. These  
4 definitions establish precise meanings to key  
5 terms contained in the regulation. For example,  
6 the final rule expands the definition of sponsor  
7 to include revolving loan funds and entities that  
8 operate loan pools.

9 These definitions are added to address  
10 the expansion of the competitive application  
11 program to include as eligible sponsors revolving  
12 loan funds and loan pools.

13 Second, the rule reorganizes the  
14 regulatory text so that the operational provisions  
15 of the competitive application program and the  
16 home ownership set aside program are separate and  
17 distinct. Separate sections of the regulation  
18 have been established for the operational  
19 provisions of these distinct programs. Third, the  
20 final rule authorizes the Federal Home Loan Banks,  
21 at their discretion, to provide opportunities for  
22 revolving loan funds and loan pools to apply under

1 the competitive program in more expanded ways.  
2 While both types of entities have been eligible in  
3 the past to apply for affordable housing subsidies  
4 through members. Under the final rule, both  
5 revolving loan funds and loan pools, at a Federal  
6 Home Loan bank's discretion, would be permitted to  
7 relend repayments of such subsidy in the case of  
8 revolving loan funds and pre-payments of loans in  
9 the case of loan pools.

10 In the past, any payments received were  
11 required to be returned to the Federal Home Loan  
12 banks for redistribution to other eligible  
13 projects. Given this new authority for revolving  
14 loan funds which may raise operational and other  
15 issues in the course of its implementation by the  
16 Federal Home Loan Banks, the Finance Board intends  
17 to conduct a program review of the use of the new  
18 revolving loan fund authority to assess how the  
19 program is working and to address any issues that  
20 have arisen.

21 Fourth, the final rule eliminates the  
22 existing discretionary authority for Federal Home

1 Loan banks to prohibit application for subsidy for  
2 projects located outside their districts. The  
3 Federal Home Loan Bank Act does not establish the  
4 Affordable Housing Program as a geographically  
5 targeted program; rather, it requires each Federal  
6 Home Loan bank to establish a program to provide  
7 subsidized funding to its members. The authority  
8 to restrict projects to a Federal Home Loan Banks'  
9 district, if exercised, would limit a member's  
10 ability to support competitive projects in certain  
11 communities that it serves if those communities  
12 are outside the boundaries of the Federal Home  
13 Loan bank's district. In light of mergers and  
14 acquisitions, often across state lines, this has  
15 become an issue for some Federal Home Loan Banks.

16 The proposed rule also prohibited a  
17 Federal Home Loan Bank from allocating scoring  
18 points under the competitive program in district  
19 projects. However, the final rule, in response to  
20 comments received, retains the current  
21 discretionary scoring preference for in district  
22 projects under the first district priority and

1 retains the existing language allowing a bank, in  
2 its discretion, to adopt a scoring preference for  
3 in district projects under the second district  
4 priority.

5           However, the Finance Board intends that  
6 a Federal Home Loan Bank should not use the  
7 scoring criteria as a means of excluding out of  
8 district projects from the competitive application  
9 program.

10           Fifth, in response to comments received,  
11 the final rule retains the Federal Home Loan Banks  
12 authority to draw on Affordable Housing Program  
13 funds from the subsequent year to fund the current  
14 year's Affordable Housing Program, but limits the  
15 amount that may be drawn to an amount up to the  
16 greater of two million dollars or 20 percent of  
17 the Federal Home Loan Banks annual required  
18 affordable housing contribution for the current  
19 year, which the Federal Home Loan Bank would then  
20 deduct from the annual required affordable housing  
21 contribution for the subsequent year.

22           This change from the proposed rule,

1       which would have eliminated the authority,  
2       responds to the fact that the Federal Home Loan  
3       banks at times have found this authority to be  
4       useful in addressing housing needs.

5               Finally, the final rule replaces certain  
6       prescriptive monitoring requirements in the  
7       regulation which detail specific monitoring and  
8       control processes with which a Federal Home Loan  
9       bank must comply. With broadly stated monitoring  
10      objectives to be accomplished through the banks  
11      adoption and implementation of written monitoring  
12      policies for its competitive application and home  
13      ownership set aside programs.

14              The regulation requires each bank to  
15      establish initial monitoring requirements for all  
16      projects under the competitive application program  
17      and establish risk based monitoring programs for  
18      long term monitoring of rental projects.

19              In addition, the final rule permits  
20      monitoring by entities that are responsible for  
21      compliance with federal low income housing tax  
22      credit projects to meet the long term monitoring

1 requirements under the Affordable Housing Program  
2 in cases in which the Affordable Housing Program  
3 subsidies are used in conjunction with federal low  
4 income housing tax credits. We believe that this  
5 final rule will enable the Federal Home Loan Banks  
6 to carry out the Affordable Housing Program more  
7 effectively and efficiently and to be responsive  
8 to their individual needs.

9 We recommend that the Board adopt the  
10 final rule contained in the Board books. As we  
11 normally do prior to submission to the Federal  
12 Register, we will closely scrutinize the text to  
13 ensure regulatory citations are correct and all  
14 text conforms to the substantive elements of the  
15 final rule.

16 We would ask the Board for permission to  
17 make technical and conforming changes to the rule  
18 and preamble in preparing the final rule for  
19 publication in the Federal Register. Changes such  
20 as the addition and correction to legal citations,  
21 removal of redundant language, and wording  
22 clarifications have already been identified,

1 including in some instances by members of the  
2 Board or Board assistants.

3 We will provide the Board with a red  
4 line copy identify all those changes in advance of  
5 submitting it to the Federal Register. We're  
6 happy to answer all questions.

7 CHAIRMAN ROSENFELD: Thank you very  
8 much. Gwen, just to make a comment, if there's  
9 any correlation between the length of the  
10 presentation and the number of letters, I would  
11 suggest that all of you in the audience, as well  
12 as the Board members, bring a lunch when we talk  
13 about the capital rule.

14 DIRECTOR CASTANEDA: Dinner perhaps.

15 CHAIRMAN ROSENFELD: Okay. Do any of  
16 the Board members wish to comment?

17 DIRECTOR BACINO: I just have one  
18 comment. I think it's appropriate that we take up  
19 the AHP program. When Franz Leichter is here, I  
20 know that he was kind of the father of this  
21 program and was very gracious when he and I met  
22 before I came here in kind of filling me in about

1 this, and so I think it matches very well with the  
2 date we've got.

3 DIRECTOR MENDELOWITZ: Yeah; under the  
4 old rule, a bank could prohibit the use of AHP for  
5 out of district projects, and at least one bank  
6 availed itself of that option. Under the new  
7 rule, banks are prohibited from automatically  
8 denying out of district projects from eligibility  
9 for AHP funds, but the rule does permit a handicap  
10 for out of district projects, so that if you're an  
11 in district project, you can get a few extra  
12 points that give you an advantage over an out of  
13 district project.

14 Now, the preamble makes clear that no  
15 one should interpret this change in the rule as  
16 permitting a bank to, in effect, exclude out of  
17 district projects from AHP eligibility through the  
18 use of the handicap extra point process. But how,  
19 in fact, are we going to ensure that that doesn't  
20 happen?

21 MR. CROSS: Well, we cannot ensure  
22 before the fact that it never happens. But our

1 examination program will include an evaluation of  
2 the basis upon which the bank has established its  
3 first and second district priorities, which is  
4 where that will occur. And if there -- and it  
5 will also include evaluation of the input of  
6 Affordable Housing Advisory Counsel and members on  
7 the selection of those first and second district  
8 priorities and their reasonableness in light of  
9 the circumstances of the bank.

10 Just as we do in safety and soundness  
11 examinations, we will criticize a bank if we  
12 believe that they -- if they have worked at cross  
13 purposes with the intention of this change, the  
14 intention being to recognize that there may be  
15 circumstances in which a bank wishes to address,  
16 because of the nature of its membership or the  
17 nature of the communities within its borders or  
18 the extent of its business relationships with  
19 banks that work exclusively within the region, we  
20 felt that it was appropriate, in light of the  
21 comments we received to provide the bank with some  
22 latitude in that regard.

1           We would revisit this provision if we  
2           found instances of abuse, and particularly if the  
3           bank didn't take corrective action in response to  
4           one of our findings. But I mean it's -- I will  
5           tell you, this is an issue about which I think we  
6           all have some mixed emotions or mixed thinking,  
7           but at the end of the day, I was persuaded that  
8           the weight of the comments favored having at least  
9           some latitude under some circumstances, and so  
10          that's why the proposal is there, but it is not  
11          without some risk.

12                   DIRECTOR MENDELOWITZ: Let me sort of  
13          put a numerical example on the table. For  
14          arguments sake, let's say that an in district  
15          application gets an automatic ten point preference  
16          over an out of district application, and when you  
17          look at the allocation of AHP funds, it turns out  
18          that the point spread between the highest scoring  
19          winning project and the lowest scoring winning  
20          project is nine points, and as a result of that,  
21          100 percent of the projects are in district,  
22          because the ten point disadvantage guarantees out

1 of district projects are not eligible, haven't  
2 been able to win; is that something that the exam  
3 staff would view as a prima facia evidence of an  
4 effort to rig the outcome to eliminate out of  
5 district projects?

6 MR. CROSS: Well, I can't yet speak for  
7 the exam staff and their experience. I would  
8 say -- I would be hard pressed to say that there  
9 is any prima facia set of facts that were not  
10 egregious, truly egregious, that would persuade  
11 me, that without looking deeper, we should draw  
12 that conclusion.

13 In the instance you talked about, let me  
14 offer you a couple of reasons why I would not.  
15 The winning projects in 100 point scale don't  
16 normally score from 100 to 91, they might be  
17 scoring from 90 to 81. As such, the fact that  
18 there is only a nine point range between the top  
19 and the bottom winning project wouldn't  
20 necessarily preclude a project that did not have  
21 the in district feature from having enough points.  
22 I would want to -- the fact that there was a bank

1 that had members that had substantial business  
2 across district lines, were substantially involved  
3 in the business of the bank, yet had all of its  
4 funds year after year go only to projects within  
5 district, that would be something I would want to  
6 look into.

7 I don't know that I would say, without  
8 further investigation, we would criticize the  
9 bank, but that would certainly be a red flag that  
10 we would look at. So I guess my short answer is,  
11 I'm not sure anything on its face would be enough  
12 for me to conclude that the bank was working at  
13 cross purposes with the rule.

14 There are certain things that I would  
15 look at, particularly if repeated over a period of  
16 time, or if answers to questions about how the  
17 priorities were set were unsatisfactory that would  
18 cause me to criticize the bank.

19 I would think that, particularly in the  
20 early stages of this rule, we should be looking at  
21 the two areas where this could arise, first and  
22 second district priorities, and ask the bank the

1 basis upon which they selected those priorities,  
2 what analysis went into it, and what their  
3 assessment of the effects of it will be, and we  
4 should be satisfied with that before we give them  
5 a pass.

6 DIRECTOR MENDELOWITZ: Well, you know,  
7 what I'm concerned about is that if we send the  
8 signal today that it's going to be very hard to  
9 demonstrate through the exam process that the  
10 point advantage within district projects doesn't,  
11 in effect, prove a de facto barrier to out of  
12 district projects, that we're going to see more of  
13 it, and I am concerned about that.

14 And you're quite correct to point out  
15 that, you know, the winning scores may come  
16 between 81 and 91 rather than between one and 100,  
17 obviously. And the concern I have is that if you  
18 rate all the project based on the distribution of  
19 points for evaluation of the project and the  
20 extent to which the project meets priorities, and  
21 you do that before you allocate the extra ten  
22 points for out of, you know, in district, the

1 concern I have is that if it turns out that on the  
2 merits, all the winning projects fall between 81  
3 and 90, and there's a ten point advantage to being  
4 in district, then by definition, any project out  
5 of district will be automatically eliminated.

6           And when you give an advantage for in  
7 district projects that is enough of a point  
8 advantage to overcome the spread between the  
9 highest qualifying project and lowest qualifying  
10 project, you're creating a circumstance where out  
11 of district projects are automatically eliminated,  
12 and I would consider that to be inconsistent with  
13 the spirit of the reg and where we intend to go  
14 with the reg. We have prohibited in the reg a  
15 prohibition against out of district projects.  
16 This means that it's clear from the wording of the  
17 reg that we intend out of district projects to  
18 have a fair chance of winning any evaluative  
19 competition for any particular bank. And I think  
20 it's clear that we do not expect the banks to use  
21 the ability to assign extra points for in district  
22 projects to be an alternative way of getting

1 around the prohibition on, you know, funding out  
2 of district projects.

3 And I hope that when we do our exams, we  
4 give, particularly in the first cycle of exams,  
5 after the passage, final passage of this rule,  
6 that we give very careful, very close evaluation  
7 to what's going on with respect to the selection  
8 of in district and out of district projects.

9 MR. CROSS: I absolutely agree with the  
10 principal that you espoused, and you have my  
11 commitment, absent objection from the rest of the  
12 Board, that in our first round of examinations  
13 beginning in 2007, we will ensure that that factor  
14 is a part of the scope of every one of the AHP  
15 examinations.

16 DIRECTOR MENDELOWITZ: The second  
17 question; there's a lot of increased latitude  
18 provided by this rule for innovative and creative  
19 ways within which to use AHP funds, including  
20 revolving loan funds, which I think is great, and  
21 other options.

22 There is one thing that I think is not

1 covered here that I would have liked to have seen  
2 included, and that is the ability to use AHP funds  
3 to enhance credit enhanced loan pools. From the  
4 perspective of having the biggest impact, I like  
5 to think of using AHP funds in a form of a set of  
6 financial jujitsu, which is, you use the AHP funds  
7 to leverage a much larger impact than you could  
8 get with the AHP funds alone. So if the AHP funds  
9 represent five percent of the project, the project  
10 couldn't happen without the AHP funds, and the  
11 leveraging is clearly 20 to one, and you get a lot  
12 of bang for the buck.

13 The same thing with respect to, you  
14 know, credit enhancing pools. If we make -- if we  
15 use the set aside and give someone a down payment  
16 grant, first time home buyer down payment grant,  
17 you put out \$5,000 or \$10,000 to a household, you  
18 enable one household to buy a house.

19 If, on the other hand, the AHP funds were  
20 used to credit enhance a pool of loans where there  
21 was, for example, no down payment, 100 percent  
22 loan to value, some of those folks would be able

1 to make their loan payments and would be able to  
2 stay current and there would be no credit losses.

3 Some of those borrowers might have  
4 difficulty staying current and there might be some  
5 loss associated with those loans.

6 And if, in fact, you were to pool all  
7 those loans together, and the funds that  
8 previously had been used, dollar for dollar, can  
9 make a down payment assistance, we use, in fact,  
10 to credit enhance a pool of loans for folks who  
11 would not have been eligible for, for example,  
12 prime loans or loans without down payments, it may  
13 be a way of getting much greater, in effect,  
14 financial jujitsu out of the use of the funds, and  
15 you could help more households purchase homes than  
16 would be the case otherwise. And so I hope as we  
17 go forward and think about ways to revise this in  
18 the next cycle, that attention will be given to  
19 this issue using AHP funds to enhance loan pools,  
20 credit enhanced loan pools. Thank you.

21 CHAIRMAN ROSENFELD: Okay. If there's  
22 nothing else, I would accept a motion to approve

1 the regulation to allow staff to make technical  
2 and conforming changes to the rule. Motion,  
3 Director Castaneda?

4 DIRECTOR CASTANEDA: I do.

5 CHAIRMAN ROSENFELD: Is there a second?

6 DIRECTOR BACINO: Second.

7 CHAIRMAN ROSENFELD: Director Bacino.

8 Would the Secretary please call the roll?

9 MS. WILLIS: On the item before the  
10 board, Director Bacino, how do you vote?

11 DIRECTOR BACINO: Yes.

12 MS. WILLIS: Director Castaneda?

13 DIRECTOR CASTANEDA: Yes.

14 MS. WILLIS: Director Mendelowitz?

15 DIRECTOR MENDELOWITZ: Yes.

16 MS. WILLIS: Director Patenaude?

17 DIRECTOR PATENAUDE: Yes.

18 MS. WILLIS: Chairman Rosenfeld?

19 CHAIRMAN ROSENFELD: Yes. The motion is

20 adopted. Before we adjourn for the closed  
21 session, the members of the Finance Board would  
22 like to offer our appreciation to our former

1 colleague, Franz Leichter. In a moment I'm going  
2 to ask the Secretary to read a resolution. But I  
3 think that I certainly, along with my colleagues  
4 on the Board, might inject a little more personal  
5 comment.

6 Franz, you know, in Washington, there's  
7 a saying that success has many fathers. I think  
8 that while frequently true, is really quite  
9 inappropriate in terms of the success of the AHP  
10 new rules. I think in this case it has one  
11 father, and I think the father was you, and from  
12 my perspective, I think you've provided it,  
13 although in many ways, but in particular, you've  
14 provided a great deal of care and insight and  
15 value to this Board's deliberations.

16 And while we're talking about AHP at the  
17 moment, I would also make note of your  
18 contribution in so many other ways, and both your  
19 sensitivity and your intellect in terms of looking  
20 at the issues that we've faced and continue to  
21 face.

22 Again, although you're not currently on

1 the Board, your participation in the development  
2 of the capital rule has been very significant, and  
3 I'm sure, regardless of how it turns out, it will  
4 have your fingerprints on making it a better rule  
5 for the -- better structure for the governance of  
6 the Home Loan Banks. So personally, you have my  
7 deepest appreciation, and we're delighted you're  
8 here. Let me ask the Secretary to read the  
9 resolution, and then I would ask my colleagues,  
10 who I know want to, I'm sure, say something.

11 MS. WILLIS: Resolution 2006-14, on the  
12 occasion of the departure of Franz S. Leichter  
13 from the Board of Directors of the Federal Housing  
14 Finance Board, whereas, Franz S. Leichter served  
15 with distinction and honor between August 14, 2000  
16 and July 25, 2006, as a member of the Board of  
17 Directors of the Federal Housing Finance Board,  
18 and was, by virtue of his substantial prior  
19 service and representing consumer and community  
20 interest, its consumer representative.

21 Whereas, Franz S. Leichter has earned  
22 the respect and admiration of his colleagues on

1 the Board of Directors of the Finance Board, the  
2 agency staff and others within the Federal Home  
3 Loan Bank system, for his unwavering dedication to  
4 the housing finance mission and cooperative  
5 structure of the system, and to the maintenance of  
6 its strength, vibrancy, and membership diversity.

7           Whereas, Franz S. Leichter was the Board  
8 of Director's liaison with housing and community  
9 advocacy groups, its lead in the oversight of the  
10 affordable housing and community investment and  
11 development activities of the Federal Home Loan  
12 banks and the Finance Board's process for amending  
13 and improving its affordable housing program  
14 regulation, and a committed advocate for the  
15 maintenance of robust affordable housing finance  
16 and community investment and development programs  
17 within the system.

18           Whereas, Franz S. Leichter was the Board  
19 of Directors' lead in the Finance Board's efforts  
20 to emphasize the incompatibility of predatory  
21 lending practices, with the responsibility of the  
22 Federal Home Loan Banks to carry out their housing

1 finance mission and to ensure that the banks do  
2 not facilitate such practices through the purchase  
3 or acceptance of predatory loans.

4           Whereas, Franz S. Leichter was an  
5 advocate for Main Street and community bank system  
6 members and the communities they serve and was  
7 central to efforts by the Finance Board and the  
8 Federal Home Loan Banks to expand access to system  
9 funds for a greater number of small businesses and  
10 communities.

11           Whereas, Franz S. Leichter was a  
12 principled and outstanding colleague who  
13 demonstrated strength of character, and who, while  
14 a strong and committed advocate for his beliefs,  
15 nevertheless, unfailingly treated his colleagues  
16 and associates with respect and stability and  
17 demonstrated class, even under the most difficult  
18 circumstances.

19           And whereas, Franz S. Leichter is a kind  
20 and thoughtful individual who cares for the  
21 personal and professional well being of those  
22 around him and for the quality of life of people

1 residing in his community.

2 Now, therefore, it is resolved that the  
3 Board of Directors of the Finance Board, and the  
4 agency's employees express their gratitude,  
5 respect, and deep appreciation to Franz S.  
6 Leichter for his dedicated service to the Finance  
7 Board and the nation, and extend best wishes for  
8 his health, happiness, and success in the future.

9 It is further resolved that in  
10 recognition of his outstanding service to the  
11 Finance Board, this resolution and its preamble be  
12 recorded in the minutes of the action taken by the  
13 Board of Directors of the Finance Board, and that  
14 an appropriate copy of this resolution be  
15 presented to Franz S. Leichter as a token of the  
16 esteem and high regard of the Board of Directors  
17 and his colleagues and associates. Signed by  
18 Chairman Rosenfeld, Secretary Jackson, and  
19 Directors Bacino, Castaneda, and Mendelowitz.

20 CHAIRMAN ROSENFELD: Thank you. I may  
21 call upon my colleagues to say anything if they  
22 wish.

1                   DIRECTOR MENDELOWITZ: Thank you,  
2 Mr. Chairman. In the six years that Franz and I  
3 served together on this Board, Franz was, without  
4 doubt, the finest colleague anyone could ask for,  
5 a man of great intellect and energy, a man of  
6 wonderful values, a man who was a true gentleman  
7 in every sense of the word, and a man with an  
8 unwavering commitment to public service and the  
9 public good.

10                   Together, we went through some very  
11 difficult times, and I will not dredge them up,  
12 other than to say that I have often felt that I  
13 don't think I could have survived those dark days  
14 if I didn't have Franz as my colleague. And Franz  
15 is someone from whom I could always derive the  
16 very best advice, the finest leadership, and the  
17 greatest sense of enduring in difficult times.  
18 And so it is with, on the one hand, great sadness  
19 that I observed your retirement from the Board,  
20 and it is with great joy that I could affix my  
21 name to the Board resolution recognizing you for  
22 all the wonderful things that you've brought to

1 the Board. Franz, thank you.

2 DIRECTOR CASTANEDA: I don't think Allan  
3 left too many things for me to say. I just wanted  
4 to add that we very much appreciate your long  
5 service on the Finance Board. And I personally,  
6 Franz, I wish you the best.

7 CHAIRMAN ROSENFELD: Thank you. Is  
8 there any further comments?

9 DIRECTOR PATENAUDE: Mr. Chairman, I'd  
10 just like to thank Franz on behalf of Secretary  
11 Alphonso Jackson for your dedicated service to the  
12 Board. Thank you.

13 CHAIRMAN ROSENFELD: This ends the open  
14 session of the meeting. We will reconvene in  
15 closed session in three minutes.

16 (Whereupon, at 11:15 a.m., the OPEN  
17 SESSION was adjourned.)

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