

FEDERAL HOUSING FINANCE BOARD MEETING

OPEN SESSION

Wednesday, September 13, 2006

ANDERSON COURT REPORTING
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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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