

# Proposed Rules

Federal Register

Vol. 68, No. 126

Tuesday, July 1, 2003

This section of the FEDERAL REGISTER contains notices to the public of the proposed issuance of rules and regulations. The purpose of these notices is to give interested persons an opportunity to participate in the rule making prior to the adoption of the final rules.

## FEDERAL HOUSING FINANCE BOARD

### 12 CFR Parts 900, 932, 955

[No. 2003–10]

RIN 3069–AB18

#### Federal Home Loan Bank Acquired Member Assets

**AGENCY:** Federal Housing Finance Board.

**ACTION:** Proposed rule.

**SUMMARY:** The Federal Housing Finance Board (Finance Board) is proposing to amend its Acquired Member Assets (AMA) regulation, which authorizes the Federal Home Loan Banks (Banks) to acquire certain whole loans from their members. The changes proposed would place greater responsibility with each Bank to design and manage its AMA program, subject to ongoing supervisory review by the Finance Board. The proposed regulation would maintain the core provisions relating to safety and soundness, but would be less prescriptive and simpler than the current rule. The proposed rule also would codify the authority of a Bank to acquire as AMA assets instruments that are created by Bank members or housing associates in cooperation with a Bank and that represent an interest in loans that individually could qualify as AMA.

**DATES:** Comments on this proposed rule must be received in writing on or before September 2, 2003.

**ADDRESSES:** Send comments by electronic mail to [comments@fhfb.gov](mailto:comments@fhfb.gov), by facsimile to (202) 408–2580, or by regular mail to the Federal Housing Finance Board, 1777 F Street, NW., Washington, DC 20006, Attn: Public Comments. Comments will be available for public inspection at this address.

**FOR FURTHER INFORMATION CONTACT:** Scott Smith, Associate Director, [smiths@fhfb.gov](mailto:smiths@fhfb.gov) or (202) 408–2991; Christina Muradian, Senior Financial Analyst, [muradianc@fhfb.gov](mailto:muradianc@fhfb.gov) or (202) 408–2584, Office of Supervision; Sharon Like, Senior Attorney Advisor,

[likes@fhfb.gov](mailto:likes@fhfb.gov) or (202) 408–2930; Thomas Hearn, Senior Attorney Advisor, [hearnt@fhfb.gov](mailto:hearnt@fhfb.gov) or (202) 408–2976; or Thomas Joseph, Senior Attorney Advisor, [josephth@fhfb.gov](mailto:josephth@fhfb.gov) or (202) 408–2512, Office of General Counsel, Federal Housing Finance Board, 1777 F Street, NW., Washington, DC 20006.

#### SUPPLEMENTARY INFORMATION:

##### I. Background

This proposed rule is an important first step in the Finance Board's effort to shift the focus of its regulations from a prescriptive approach to an approach that places greater responsibility on the Banks and relies more on supervisory review. The Finance Board believes that an increased focus on the process of supervisory review will enhance the safety and soundness of the Bank System.

On May 3, 2000, the Finance Board published a proposed rule to authorize the Banks to acquire certain whole loans. See proposed rule, Federal Home Loan Bank Acquired Member Assets, Core Mission Activities, Investments and Advances, 65 FR 25676 (May 3, 2000) (hereinafter the "Proposed AMA Rule"). The Finance Board subsequently adopted a final AMA regulation, which became effective on July 17, 2000. See final rule, Federal Home Loan Bank Acquired Member Assets, Core Mission Activities, Investment and Advances, 65 FR 43969 (July 17, 2000) (hereinafter the "current rule" or "final AMA rule"). The current rule authorizes the Banks to acquire certain loans (principally conforming residential mortgage loans) from their members and housing associates as a means of advancing their housing finance mission, and prescribes in some detail the manner in which the Banks may do so.

Since implementation of the current rule, the Finance Board has recognized that an alternative approach, one that places greater responsibility on the Banks, would likely prove to be more effective and efficient in regulating the Banks' mortgage purchase programs. In addition, the Finance Board, now with several years experience in overseeing these programs, has identified a number of opportunities to clarify and simplify the current rule.

Specifically, the current rule includes prescriptive provisions concerning the risk-sharing structure that may not be

necessary for safety and soundness purposes. Such provisions include the requirement that the rating methodology be verified in writing by a Nationally Recognized Statistical Rating Organization (NRSRO), even though the methodology remains subject to Finance Board approval, and that there must be certain restrictions on the credit enhancement structure, even though the member must bear the economic cost regardless of structure. Also, the current rule includes terms that have proven to be unclear and difficult to define, such as "expected losses" and "valid business purpose." Further, the current rule does not specifically incorporate language to authorize the Banks to acquire as AMA certain instruments that are created by Bank members or housing associates in cooperation with a Bank and that represent an interest in AMA-eligible loans. See final AMA rule, 65 FR at 43974–78. Finally, the practice of collecting AMA data has evolved from the reporting requirements set forth in the current rule, such that some data elements have been found to be either unnecessary or readily available from other sources, while others must be collected going forward to comply with revised modeling requirements and regulatory standards.

Although some opportunities to improve the current rule exist, the current rule does contain a number of appropriate and necessary safety and soundness provisions. These provisions would be maintained or strengthened in the proposed rule, and include the requirements that all AMA must be at least investment grade when acquired, and that only highly rated insurers may provide some portion of the credit enhancement.

The Finance Board invites anyone with an interest in this proposed rule to submit written comments to the Finance Board during the comment period.

##### II. Analysis of Proposed Rule

The proposed rule would revise the current rule as described in the following sections.

###### A. Definitions—Section 955.1

The proposed rule would add four new defined terms, and would delete two of the existing definitions. Changes to individual definitions in the proposed rule are discussed in later sections of this **SUPPLEMENTARY**

**INFORMATION** section in the context of specific regulatory requirements.

*B. Authorization To Invest in AMA—Section 955.2*

Section 955.2 of the current rule authorizes a Bank to invest in AMA, and establishes a three-part test for AMA-eligible investments. See 12 CFR 955.2. The current rule prescribes the types of assets that may qualify as AMA, the required nexus between the Bank and its member or housing associate, and the details of the credit risk-sharing provisions. Under the proposed rule, this section would simply authorize a Bank to invest in AMA, subject to the provisions of part 955 and 12 CFR part 980 (relating to new business activities). The existing provisions relating to asset type, member nexus, and credit risk sharing would be relocated to separate sections.

The proposed rule also would add a definition of “AMA” to § 955.1, and would make conforming changes to the existing definition of “AMA” in 12 CFR 900.2. Under those definitions, the term “AMA” would mean any assets acquired in accordance with, and satisfying the applicable requirements of, proposed §§ 955.3, 955.4 and 955.5, which address the asset type, member nexus, and credit enhancement requirements, respectively.

*C. Three-Part Test—Proposed §§ 955.3, 955.4 and 955.5*

The proposed rule would relocate and revise each element of the three-part test, which currently is set forth in §§ 955.2(a), 955.2(b) and 955.2(c).

**1. Asset Requirement—Proposed § 955.3**

Proposed § 955.3, which would specify the types of assets that are AMA-eligible, would eliminate one item that currently qualifies as AMA and add another item that the Finance Board has included as AMA by interpretation. The proposed rule would retain the provisions of the current rule relating to the acquisition of whole loans that are eligible to secure Bank advances, or that are secured by manufactured housing. See 12 CFR 955.2(a)(1), (a)(2). The proposed rule would eliminate the current provision that allows certain state or local housing finance agency (HFA) bonds to qualify as AMA. 12 CFR 955.2(a)(3). The Banks are authorized to invest in certain highly rated HFA bonds under other provisions of the regulations, and the Finance Board believes that eliminating the separate investment authority under the AMA regulation would not affect the ability of a Bank to invest in HFA bonds rated AA or higher. See 12 CFR 956.2(f),

956.3(a)(4)(iii). Because the proposed rule would remove HFA bonds as AMA, the proposed rule also would eliminate provisions that establish a process for acquiring HFA bonds as AMA from a member or housing associate of another Bank. 12 CFR 955.2(b)(2)(ii).

*AMA-qualified interests in whole loans.* Section 955.3(c) of the proposed rule would expressly authorize as AMA investments certain instruments that represent an interest in qualifying whole loans. The Banks currently are authorized to make such AMA investments, based on Finance Board guidance provided in the preamble to the current rule. See final AMA rule, 65 FR at 43974–78. The proposed rule would codify the existing guidance. The several provisions of the proposed rule that relate to these interests are discussed together below, under the section captioned *AMA-Qualified Interests in Whole Loans*.

**2. Member or Housing Associate Nexus Requirement Proposed § 955.4**

Section 955.4 of the proposed rule would retain a nexus requirement by providing that a Bank may acquire AMA-eligible loans only from its members and housing associates, from members and housing associates of another Bank, or from another Bank. The nexus requirement is intended to ensure that AMA assets have an appropriate connection to the Bank’s member or housing associate. That connection advances the cooperative nature of the Bank System, and effectively precludes the extension of membership benefits to nonmembers. The proposed rule, however, would simplify this member or housing associate nexus requirement. The specific revisions are described below.

*“Valid business purpose” requirement.* The proposed rule would eliminate the “valid business purpose” requirement from § 955.2(b)(1)(ii) of the current rule. 12 CFR 955.2(b)(1)(ii). This provision of the current rule recognizes that members often acquire mortgage loans both by originating them, as well as by purchasing them from other parties and allows the Banks to acquire loans originated by third parties, provided that the members have acquired them for a valid business purpose. It is intended to discourage the use of members as conduits for the sole purpose of passing mortgage loans from a nonmember to the Bank. The current rule, however, does not define what constitutes a “valid business purpose,” and this provision has been difficult to enforce as written. The proposed elimination of this requirement is intended only to simplify the rule, and

does not alter the underlying policy that AMA-eligible whole loans may be acquired only from members and housing associates.

*Origination or issuance requirement.* The proposed rule would eliminate the requirement that AMA must be originated or issued by or through a member, housing associate, or affiliate thereof. 12 CFR 955.2(b)(1)(i). Eliminating this requirement is consistent with the elimination of the “valid business purpose” requirement, noted above. To eliminate only the “valid business purpose” requirement would render ineligible for purchase by Banks AMA-qualifying loans owned by, but not originated by, members. This limitation would put a large segment of the mortgage market out of reach of the AMA programs.

If the “valid business purpose” and “origination or issuance” provisions are eliminated, as proposed, the AMA rule would no longer use the term “affiliate.” Thus, the Finance Board is also proposing to delete the definition of “affiliate” from § 955.1.

*Acquisition of assets from affiliates of a member.* As noted previously, the proposed rule would retain the requirement that a Bank may acquire AMA only from a member, a housing associate, or another Bank. 12 CFR 955.2(b)(2). Accordingly, a Bank could not purchase mortgage assets directly from an affiliate of a member, and any such assets would have to be acquired by the member before a Bank could acquire them as AMA. A number of Banks have suggested that the Finance Board permit the Banks to acquire assets directly from affiliates of a member. As noted above, the nexus requirement ensures that AMA assets have a connection to the members that reflects the cooperative nature of the Bank System. Allowing a Bank to purchase AMA directly from an affiliate would raise concerns about the extension of membership benefits to a nonmember, even if the nonmember were under common control with a member. Such an arrangement might also present practical and operational concerns relating to AMA collateral and credit enhancement because a Bank would have more extensive means of requiring a member to meet its obligations than would be the case for a nonmember institution. The Finance Board, however, is willing to consider this issue further and requests comment on whether, and under what conditions, a Bank may be permitted to acquire AMA-qualifying assets from an affiliate of a member. Among the issues on which the Finance Board seeks comments are whether the rule should treat a wholly-

owned subsidiary of a member differently from other affiliates that are not controlled by the member, and whether the rule should allow an affiliate to sell loans to a Bank, so long as the related member provides the required credit enhancement.

### 3. Credit Risk-Sharing Requirements—Proposed § 955.5

The proposed rule would revise certain aspects of the credit risk-sharing requirements and would reorganize the credit risk-sharing requirements to achieve greater clarity. As noted below, the proposed rule would retain the requirements that the member must enhance the AMA to at least investment grade and that supplemental insurance providers must be rated at least the second highest investment grade. The Finance Board believes that these provisions are important for safety and soundness reasons.

#### a. Required Credit Risk-Sharing Structure—Proposed § 955.5(a)

*AMA product requirement.* Proposed § 955.5(a)(1) would retain the current requirement that the Bank implement a credit risk-sharing structure for each AMA Product,<sup>1</sup> under which a member or housing associate provides the credit enhancement necessary to enhance an asset or pool of assets acquired by the Bank to the equivalent of investment grade. 12 CFR 955.3(b). The proposed rule also would add a definition of “investment grade” to § 955.1, which would define the term to mean a credit quality rating in one of the four highest credit rating categories provided by an NRSRO.

*Asset requirement.* Proposed § 955.5(a)(2) would require a Bank to specify the level within investment grade to which the credit quality of the particular AMA asset or pool of assets must be equivalent. In substance, this revision is the same as the current provision, which authorizes a Bank to require a member or housing associate to provide sufficient credit enhancement to raise the credit quality of the AMA assets above the minimum level of investment grade, e.g., BBB. See 12 CFR 955.3(b).

*Satisfaction of credit enhancement requirement.* Proposed § 955.5(a)(3) would require, for each AMA Product, that the Bank have in place a process and methodology that determines the credit enhancement required, and that demonstrates that the economic value of the credit enhancement provided by the

member or housing associate is sufficient to meet the credit enhancement required. The Bank must have the process and methodology in place prior to the acquisition of any AMA assets, and must maintain the process and methodology for however long the assets remain on its books. The Bank would be required to satisfy the Finance Board as to the adequacy of the process and methodology.

While the proposed rule would maintain the requirement that a Bank must demonstrate the sufficiency of the methodology and economic value of the credit enhancement, to the satisfaction of the Finance Board, the proposed rule would eliminate the requirement that such demonstration may be provided only by written verification from an NRSRO. 12 CFR 955.3(a), (b)(4). Although a Bank could continue to use written NRSRO verification to demonstrate this sufficiency, the proposed rule is intended to allow the Banks the opportunity to determine other means by which to satisfy the requirement. Moreover, although the Finance Board is proposing to eliminate the specific requirement that a Bank obtain written verification from an NRSRO, the Finance Board would continue to use NRSRO standards and practices as the benchmark against which it judges the sufficiency of a Bank’s methodology and the economic value of the credit enhancement. Thus, as under the current rule, to the extent an NRSRO were to decline to rate a structured finance transaction because the underlying asset pool included particular types or categories of assets, then the presence of such assets within an AMA pool would effectively preclude a Bank from calculating a putative credit rating for that pool and from complying with the proposed credit enhancement requirements with regard to that particular pool.<sup>2</sup>

The proposed requirement that a Bank must have in place its process and methodology “prior to the acquisition of any asset or pool of assets and throughout the life of the asset or pool of assets on the Bank’s books,” would replace the current requirement that the Bank must determine the required credit enhancement at the earlier of 270 days from the date of the Bank’s acquisition of the first loan in a pool, or the date at which the amount of a pool’s assets

reaches \$100 million. 12 CFR 955.3(a). As a result of this provision, a Bank would be responsible for ensuring that none of its actions, such as the approval of the sale of mortgage servicing rights by a member or housing associate that is responsible for the required credit enhancement, would affect the estimated credit rating of an asset.

*Elimination of outdated provisions.* The proposed rule would eliminate § 955.3(c) of the current rule, which established a 90-day period within which AMA programs in existence at the time of the effective date of the current rule had to obtain new NRSRO opinion letters. 12 CFR 955.3(c). This provision no longer has any effect, as the 90-day period has since passed.

*Decline in estimated credit rating.* Section 955.5(a)(4) of the proposed rule would clarify the responsibilities of a Bank in the event that the estimated credit rating of an AMA asset or pool of assets were to decline to below the initially required credit rating. In those circumstances, the Bank must either require the member or housing associate to provide sufficient additional credit enhancement to restore the rating, or must recalculate and comply with the risk-based capital requirement for that asset to reflect the reduced estimated credit rating. The substance of this provision is much the same as § 955.6(b) of the current rule. See 12 CFR 955.6(b).

#### b. Credit Enhancement Requirements—Proposed § 955.5(b)

*Member or housing associate responsibility.* Proposed § 955.5(b)(1) would retain the requirement in § 955.3(b) of the current rule that the credit enhancement must be provided by a member or housing associate of the Bank or, with the approval of both Banks, by a member or housing associate of another Bank. 12 CFR 955.3(b). The proposed rule would eliminate, however, many of the prescriptive structural requirements with regard to the credit enhancement that are now contained in § 955.3(b). Instead, the proposed rule would allow a Bank greater freedom to design specific AMA Products. The Finance Board intends to rely on its examination and review process to verify that a Bank’s AMA Products comply with the proposed credit enhancement requirements. Because the proposed credit enhancement requirements would not refer to “expected losses,” as does the current rule, the Finance Board is also proposing to delete the definition of this term from § 955.1.

*Economic cost; third party credit enhancement.* Section 955.5(b)(2) of the proposed rule would broadly state that

<sup>1</sup> The Finance Board is proposing to add a new definition to § 955.1 that “AMA Product” means an AMA structure defined by a specific set of terms and conditions.

<sup>2</sup> For example, if Standard & Poor’s continues to decline to rate mortgage pools that contain loans subject to the Georgia Fair Lending Act, as in effect from October 1, 2002, until March 7, 2003, the Banks would not be in a position to demonstrate that they could rate such loans. Thus, the Banks could not buy such mortgage loans as AMA and still comply with proposed § 955.5(a)(3).

the member or housing associate that initially provides the credit enhancement must bear all of the direct economic consequences of the credit enhancement responsibility. This means that no part of the credit enhancement costs can be paid by a Bank, either directly or indirectly. The proposed rule also would eliminate the criteria in § 955.3(b)(1) of the current rule that apply if a member or housing associate provides a portion of its required credit enhancement through a third party, *i.e.*, by contracting with an insurance affiliate, by purchasing loan-level or pool-level insurance, or by contracting with another member or housing associate. Instead, the authority to provide the required credit enhancement through a third party would be implied from the more general requirement in proposed § 955.5(b)(2) that the member or housing associate must bear all of the economic consequences of the credit enhancement responsibility. This broader language would allow a member or housing associate to purchase insurance (which could include United States government guarantees or insurance) for a portion or all of the credit enhancement obligation, or to sell a portion or all of the obligation to another qualified party, so long as the member or housing associate bears all of the economic consequences of the credit enhancement obligation. See proposed § 955.5(b)(1). The current requirement that a third party may cover only those losses that remain after the member or housing associate has borne expected losses, would be eliminated. See 12 CFR 955.3(b)(1)(i), (b)(1)(ii)(B), (b)(1)(iii)(B), (b)(2). Additional requirements applicable where the third party is an insurer are discussed in the *Use of mortgage insurance* section below.

Although the proposed rule would retain the current requirement that members or housing associates are responsible for providing the necessary credit enhancement to raise the credit quality to investment grade, it is less prescriptive than the current rule. This approach is not intended to alter the economics of the current risk-sharing requirement. Instead, it is intended that with fewer restrictions on the form of the credit enhancement, and on the type and degree of supplemental mortgage insurance (SMI), the Banks may develop alternative credit enhancement structures, such as through greater use of pool insurance.

*Direct obligations of members.* Section 955.5(b)(3) of the proposed rule would clarify provisions in the current rule by stating that any portion of a credit enhancement that is a direct

obligation of a member or housing associate and that is not covered by third party insurance generally must be fully secured by that member or housing associate with collateral that is eligible to secure an advance. The current rule had prompted questions about the need for collateral for obligations that are covered by insurance, and the proposed rule would make clear that collateral is required only to support a direct obligation of the member or housing associate itself, not the obligations of an insurer. The proposed rule also would clarify the effect of a transfer of the credit enhancement responsibility to another member or housing associate, by providing expressly that the successor shall continue to comply with any collateral requirements that applied to the initial member or housing associate. Under the proposed rule, a Bank would have an option of holding permanent capital against such direct obligations, in an amount equal to 100 percent of the nominal value of the obligation, in lieu of obtaining collateral from the member or housing associate.

The Finance Board has been asked previously to permit a member or housing associate to secure its credit enhancement obligation with collateral that is not eligible under the Bank Act to secure advances. The Finance Board has not included such a provision in the proposed rule, but requests comment on whether it would be appropriate to allow a member or housing associate to use such non-Bank Act-eligible collateral to secure its credit enhancement obligations.

*Use of mortgage insurance.* Section 955.5(b)(4) of the proposed rule would authorize a member or housing associate to provide all or a portion of its required credit enhancement through mortgage insurance, provided that the insurer is rated not lower than the second highest credit rating. If the rating of the insurer were to fall below the second highest credit rating, the member or housing associate would have 60 days to replace the insurance with an insurer that has the required credit rating. This provision would modify the current rule, which requires that such insurance be maintained at all times, and is intended to recognize that a member or housing associate may not be able to immediately obtain replacement insurance. 12 CFR 955.3(b)(1)(ii)(A). The proposed rule also would clarify the current rule by making clear that the minimum credit rating requirement is applicable to both loan-level and pool-level insurers.

The proposed rule also would eliminate the current restrictions on the type of insurance, particularly pool

insurance, that may be used to cover any portion of the credit enhancement. Under the current rule, a member may use pool-level insurance only to cover that portion of the credit enhancement obligation that is attributable to geographic concentration and pool size. See 12 CFR 955.3(b)(1)(iii). Allowing broader use of pool insurance may enhance the safety and soundness of the Banks' AMA programs. Although the proposed rule would place fewer limitations on the use of mortgage insurance, the Finance Board expects the Banks to continue to monitor closely their exposures to individual mortgage insurers and to manage these exposures prudently. A Bank should perform an independent credit analysis of the SMI companies with which it does business to gain a more detailed understanding of their financial condition and operating performance considering the potential credit concentrations and exposure levels involved. A Bank should evaluate its potential exposure in determining the depth of credit analysis appropriate for individual SMI providers.

#### c. Grandfathered Transactions

The proposed rule would retain the existing AMA grandfather provision, with minor technical revisions, and would relocate it to proposed § 955.5(c). 12 CFR 955.2(c)(2). Under the proposed provision, any AMA-type assets acquired by a Bank in accordance with prior resolutions of the Finance Board would not be subject to the credit enhancement requirements in proposed § 955.5 of the AMA rule, provided that they remain within any total dollar cap imposed by the Finance Board.

#### D. AMA-Qualified Interests in Whole Loans

The Finance Board is proposing to incorporate into the AMA rule previous guidance addressing the acquisition of instruments that represent an interest in AMA-eligible loans. The Finance Board had previously provided this guidance as part of the **SUPPLEMENTARY INFORMATION** section of the final AMA rule. See final AMA rule, 65 FR at 43974–78. Codifying this guidance is intended to make more transparent the existing authority for the Banks to acquire such instruments as AMA. In adopting the Final AMA Rule, the Finance Board stated that a Bank may acquire certificates representing interests in whole loans as AMA only if:

- (1) The certificates are rated by an NRSRO to meet the credit enhancement requirement of § 955.3;
- (2) The certificates are issued following the execution of, and for the purpose of implementing an agreement between and

initiated by the Bank and a Bank System member or housing associate to share risks in compliance with the requirements of § 955.3(b); and

(3) The initiating Bank or Banks acquire substantially all of the certificates. It is the Finance Board's view that, in such a case, the use of a third party to securitize the whole loans would merely represent a vehicle to invest in certain types of AMA under more favorable terms and should therefore be permitted under the rule. However, if the certificates have been created as a security initially available to investors generally, they will not be considered to qualify as "whole loans" under § 955.2(a)(1).

*Id.* at 43974. The Finance Board further explained that mortgage financing instruments structured into senior and subordinated tranches also could be included in the general definition of AMA as long as the transaction was "implemented through a Bank's AMA program using assets that conform with the AMA requirements" and the member involved in the transaction "bore the risk of holding or selling the credit support tranches." *Id.* at 43977. The proposed rule would incorporate the above criteria, albeit in a less prescriptive form, into the three-part AMA test in §§ 955.3(c), 955.4(b) and 955.5.<sup>3</sup>

Section 955.3(c) of the proposed rule, first, would require any instrument that represents an interest in whole loans to be backed only by loans that would be eligible for a Bank to acquire as AMA. In order to qualify as AMA, any such interests also must be created by a member or housing associate, in cooperation with a Bank. To help assure that the Bank's purchase of such instruments is not a mere capital

markets transaction that would not advance the housing finance mission of the Bank System, the Bank cooperating in the creation of the instruments would be required initially to acquire substantially all of the assets issued under this arrangement.

Proposed § 955.3(c) also would make clear that interest only strips (IOs), principal only strips (POs), as well as other interests in the underlying loans that have risk characteristics similar to IOs or POs, would not qualify as AMA.<sup>4</sup> At this time, the Finance Board does not believe that these classes of assets would be consistent with the underlying purpose of the AMA rule, which is to allow a Bank to acquire a high-quality asset from or through its members and housing associates by transactions that support its statutory housing finance mission. See proposed AMA rule, 65 FR at 25681.

Second, § 955.4(b)(1) of the proposed rule would require that the whole loans underlying an AMA-qualified instrument may be acquired only from the same sources from which a Bank may acquire AMA-qualified whole loans. Thus, if a member were to use a trust or other special purpose entity to issue the AMA-qualified interests, the underlying loans must be purchased from: A member or housing associate of the Bank; a member of another Bank, pursuant to an arrangement with that Bank; or a Bank, if approved by the Finance Board. Section 955.6 of the proposed rule would prohibit the use of existing AMA assets to create an AMA-qualified instrument, without the prior approval of the Finance Board. To preserve the nexus between any such AMA-qualified interests in whole loans and the Bank System, the proposed rule also would allow a Bank to sell AMA-qualified interests in whole loans only to other Banks or to members of any Bank.

Finally, to qualify as AMA, an instrument representing an interest in whole loans would have to meet the same credit risk-sharing requirements as are applicable to other AMA-qualified assets. Thus, the instrument would need to be credit-enhanced to a credit quality

equivalent to one of the four categories of investment grade, as determined by the Bank. The proposed rule would differ from the prior guidance provided in the Final AMA Rule, in that it would not require an AMA-qualified interest in whole loans to receive a public rating from an NRSRO. If an NRSRO were to provide a public investment grade rating of the level required by the Bank, that rating would generally satisfy the requirements of proposed § 955.5(a). Further, under proposed §§ 955.5(b)(1) and (b)(2), the member that arranged the creation of the AMA-qualified interest would need to provide the required credit enhancement, and bear all of the economic consequences of the credit enhancement responsibility, as is the case with respect to whole loan AMA assets. The required credit enhancement could be provided through subordinated or credit support tranches. A member generally could meet its obligations under the proposed rule if it were to acquire these support tranches, even if the member later sold these interests.<sup>5</sup> The proposed rule also would allow forms of credit enhancement other than a credit support or subordinated tranche, subject to the Bank satisfying the Finance Board that the credit enhancement obligations of the member or housing associate would meet the requirements of proposed § 955.5(b).

<sup>5</sup> By acquiring the subordinated credit support tranches, the member would be bearing the direct economic consequences of losses from the underlying loans. Clearly, this will be true if the member holds the support tranches for the entire life of the pool of loans underlying the assets, because it will absorb all actual losses up to the required credit enhancement level. The member also will bear the economic consequence of these losses, however, if it sells some or all of the subordinated credit support interests, because of the price risk inherent in the sale of these instruments. Markets will reward low credit losses in the underlying pool of loans with higher prices, and penalize high losses with lower prices. Because of this, the member maintains a strong incentive to assure the credit quality of the loans that will back the senior, AMA-qualified tranches purchased by the Bank, even if the member intends to sell the credit support tranches.

Moreover, given that credit support tranches would be structured to absorb losses up to the initial required amount of the credit enhancement, a Bank that buys the senior investment grade tranches would have no credit exposure to the member that initially acquires the credit support tranches or to any subsequent party that may purchase these support tranches. A credit support tranche, therefore, would not be within the meaning of the phrase "direct obligation of a member or a housing associate" as used in proposed § 955.5(b)(3), and a member or housing associate would not need to provide collateral in connection with this form of credit enhancement. Because the member would not be required to post collateral for the credit support tranches, there also would be no need to restrict the member's sale of those tranches to other Bank members.

<sup>3</sup> The Finance Board's guidance in the final AMA rule was applied in reviewing the Federal Home Loan Bank of Chicago's (Chicago Bank) new business activity notice with regard to the Chicago Bank's Shared Funding™ Program (SFP), an AMA product offered under the Mortgage Partnership Finance Program™ (MPF). See Approval of New Business Activity Notice, 2002-APP-07 (Dec. 4, 2002) (available at [www.fhfb.gov](http://www.fhfb.gov)). Generally, under SFP, a member of the Chicago Bank will purchase AMA-eligible whole loans from other Bank members that have been approved to participate in the program. The Chicago Bank member will transfer these loans to a special purpose entity (SPE) that it establishes. The SPE, in turn, will issue certificates that represent senior investment grade securities and credit support tranches and that are backed by the whole loans. The member will acquire the credit support tranches. The Chicago Bank will acquire the senior investment grade securities, all of which will receive a credit rating from an NRSRO of the second highest investment grade or better. The approval permits the Chicago Bank, or any Bank that subsequently purchases these senior securities, to sell the securities only to other Banks or qualified Bank members. The new business activity approval does not apply to transactions that would involve any loans that a Bank previously purchased as AMA. *Id.* The Chicago Bank announced the completion of its first SFP transaction on March 21, 2003.

<sup>4</sup> The Finance Board recognizes that Banks have expressed interest in buying IOs or POs, specifically as hedging vehicles. This proposed provision would not prevent the Finance Board from removing restrictions that currently prohibit a Bank from acquiring these types of assets for investment or hedging purposes under authority in part 956 of the Finance Board's rules, should the Finance Board decide that such restrictions are no longer warranted. 12 CFR part 956. The proposed provision, instead, would merely clarify that these assets could not be considered AMA and could not be purchased under the authority granted in proposed part 955.

### *E. Restructuring of AMA—Proposed § 955.6*

The Finance Board is proposing to add new § 955.6 to the AMA regulation. This provision would prohibit a Bank from using or selling AMA that it has already purchased and is holding on its books to create alternative asset structures, including those assets described in § 955.3(c) of the proposed rule, without first obtaining Finance Board approval. Actions taken by a Bank with the intent to alter the putative or actual rating of its existing AMA or otherwise change the form of an asset or an asset's existing credit risk-sharing structure, would be covered by this provision. Among the factors the Finance Board would consider in reviewing a request for approval under this proposed section would be: How a Bank intends to unwind an existing credit enhancement structure or incorporate the credit enhancement into the structure of the new asset; whether, after the proposed repackaging is complete, a Bank would be holding an asset that it would not be authorized to purchase under Finance Board rules; and whether the new asset would advance or enhance the housing finance mission embedded in the AMA rule.

### *F. Reporting Requirements for AMA—Proposed § 955.7*

Under the proposed rule, the reporting requirements for AMA, which currently are contained in § 955.4, would be revised and relocated to § 955.7.

The proposed rule would clarify, in new § 955.7(a), that each Bank that has members or housing associates that have provided the initial credit enhancement for AMA, would be responsible for collecting and maintaining the loan-level and pool-level data required by § 955.7 for all residential mortgage loans that constitute or otherwise back such AMA, including assets described in § 955.3(c). The Bank would have this responsibility regardless of whether the AMA is participated in whole or in part to other Banks. Although the Bank would be responsible for collecting and maintaining this data and reporting the data to the Finance Board, the Bank could arrange by contract with another Bank to have this responsibility carried out by the other Bank.

The proposed rule is intended to reduce the overall burden of AMA data collection on the Banks while improving the informational content of the data that are collected. The burden would be lessened by reducing the number of data elements to be collected, by eliminating reporting redundancies,

and by eliminating a requirement that the Banks aggregate data prior to reporting. Informational content would be improved by increasing the frequency of loan-level data reporting, codifying in the proposed rule the current practice of reporting certain data elements added since the implementation of the current rule, and adding a few more data elements needed to satisfy updated credit risk modeling requirements and to comply with revised Office of Management and Budget (OMB) reporting classifications.

*Conforming the requirements to existing practice.* In consultation with the Banks, the Finance Board designed a reporting format for the semi-annual loan-level mortgage reports. In the course of these consultations, non-substantive changes were made to the data requirements of § 955.4, including refining the definitions of some of the reporting elements, and adding new elements to improve database management and enhance monitoring.<sup>6</sup> In addition, while the current rule only requires reporting on loans acquired year-to-date, it was determined that for purposes of safety and soundness monitoring, certain variables should be required to be reported for all outstanding AMA residential mortgage loans, not just for AMA residential mortgage loans acquired during the calendar year. Thus, program-to-date data are currently collected along with data on loans acquired in the calendar year in order to track the performance of each loan and enhance the ability to track delinquencies. The proposed amendments to the data reporting structure and content would reflect the current reporting system in this regard.

*Proposed elimination of data elements.* Since the current rule went into effect, loan-level data have been reported for four semi-annual reports,

<sup>6</sup> The definition of "County" was changed from the county name to the 3-digit Federal Information Processing Standard (FIPS) code for the county. The definition of "PMI Percent" was changed from percent of private mortgage insurance to percent of primary mortgage insurance, including mortgages insured by government agencies. The definition of "Credit Enhancement" was changed from the numeric code indicating the type of credit enhancement to the dollar value of the calculated loan-level credit enhancement. "Prepayment Penalty Terms" was changed to "Prepayment Penalty Date" and defined as the date that the application of the prepayment penalty ends. "Default Status" was changed to "Delinquency Status" and represented the delinquency status of the loan at the end of the reporting period. "Pool Rating" for the letter credit rating of the loan pool was added to the loan-level data reporting requirement. "Interest Rate" was defined as the note rate on the loan at the time of loan origination. New variables added for database management purposes were: "Program Type" and "Pool Number."

and this reporting experience has revealed that some fields required in the current rule are either very sparsely populated or are relatively difficult to collect and provide little information relative to the housing finance mission of the Banks or safety and soundness monitoring. The proposed rule would eliminate these fields.<sup>7</sup>

The current rule also has resulted in reporting duplication. Basic information on loans acquired during the first two quarters of the year is reported twice—first in the second quarter loan-level report and again in the fourth quarter loan-level report. Under proposed § 955.7, loan-level data on the loan, borrower and property characteristics would be required to be reported only once—at the end of the calendar quarter in which the loan is acquired. See proposed Appendices A and B, part I.

*Proposed reduction in reporting burden.* Proposed § 955.7 would reduce the reporting burden on the Banks by eliminating the requirement that the Banks generate aggregate data reports from the loan-level data they collect. Instead, the proposed rule would require that the Banks submit loan-level data in place of the aggregate data. Because the loan-level data are collected and maintained by the Banks in any event, eliminating the aggregate reporting requirement would reduce the Banks' computational burden of aggregating the loan-level data.

In addition, the proposed rule would relieve the Banks from reporting elements that are already collected elsewhere by the Finance Board. Specifically, elements the Banks would no longer report are those that describe the acquiring lender, or member selling the AMA to the Bank, and those containing census level demographic information related to the property.<sup>8</sup> These elements are collected now by the Finance Board through its membership data collection and directly from the Department of Housing and Urban Development (HUD). The proposed rule

<sup>7</sup> Fields that were found to provide little information were the geographic indicator "Place Code," and mortgage identifiers "Cooperative Unit Mortgage," "Mortgage Purchased under the Banks" Community Investment Cash Advances (CICA) Programs" (for single-family AMA), and "Bank Real Estate Owned." "Acquisition Type" would be eliminated due to the addition of the "Program Type" data element.

<sup>8</sup> The eliminated elements include "Acquiring Lender Institution," "Acquiring Lender City," "Acquiring Lender State," "Type of Acquiring Lender Institution," "Census Tract—Percent Minority," "Census Tract—Median Income," "Local Area Median Income," "Tract Income Ratio," "Area Median Family Income," "Borrower Income Ratio," "Unit—Affordable Category," "Unit Type XX—Affordability Level" (for multi-family AMA), and "Geographically Targeted Indicator."

would instead add only a single element to identify such member, the "Federal Housing Finance Board Identification (FHFBID) Number," which will permit linking the AMA data with the Finance Board's membership database.

The proposed rule would also reduce reporting redundancy by removing pool variables from the loan-level data report and requiring a separate pool-level data report. Under the current reporting system, the pool-level credit rating, as well as the participation percentage of each Bank in a loan's pool, is reported at the loan-level. Thus, the same information about the pool is reported numerous times, once for each loan in the pool. Under the proposed rule, a pool identifier would be reported at the loan-level, and pool-level information would be reported only once in the pool-level report. In addition to streamlining the pool-level data reporting, proposed §§ 955.7(c) and (d) would require the Banks to provide a quarterly update on loan pools so that the Finance Board can monitor changes in the credit quality of pools and estimated or actual credit enhancements, which are important safety and soundness considerations. See proposed Appendices A and B, part III. The pool-level report would include: The "Bank District Flag;" the "Pool Number;" 12 variables representing the "Participation Percentages" of each of the 12 Banks in the pool; and four variables representing information on the pool credit enhancement and credit rating—"Pool Rating," "Pool Credit Enhancement," "Recalculated Pool Rating," and "Recalculated Credit Enhancement."

*Proposed addition of new data elements.* The proposed rule would add several new fields to the list of required data elements to comply with OMB Notice of Decision, "Revisions to the Standards for the Classification of Federal Data on Race and Ethnicity," 62 FR 58782 (October 30, 1997) (OMB Notice of Decision). Specifically, "Borrower Ethnicity" and "Co-Borrower Ethnicity," which currently are collected and reported under the "Borrower Race or National Origin" and "Co-Borrower Race or National Origin" fields, would be separately collected

<sup>9</sup>The new data element "Pool Credit Enhancement" would replace the current data element "Credit Enhancement," which itself has been redefined since the current rule was adopted. See n.6, *supra*. The Finance Board has effectively been collecting pool-level credit enhancement values because it aggregates the loan-level credit enhancement values currently collected. Standing alone, however, the loan-level credit enhancement values are not as meaningful as the pool-level values, and the Finance Board, therefore, is proposing to collect the pool-level values directly.

and reported. The race fields would be renamed "Borrower Race" and "Co-Borrower Race," consistent with the OMB Notice of Decision.

The proposed rule also would add the following loan-level data elements to allow for better tracking and modeling of prepayment and default rates of AMA: "Type of Credit Score;" redefinitions of "Borrower Credit Score" and "Co-Borrower Credit Score" to include, in addition to the Fair, Isaacs, Co. (FICO) score, the NextGen FICO credit score; "Adjustment Frequency;" "Negative Amortization;" "Current Unpaid Principal Balance;" "Current Coupon;" and "Loan Amount" (for multi-family AMA).

Each of the two proposed Appendices would be sub-divided into three parts for the three types of data that would be required to be collected and reported: Part I—Loan-level data elements to be reported for all single-family and multi-family AMA acquired during the calendar quarter; part II—Loan-level data elements to be reported for all single-family and multi-family AMA outstanding in the calendar quarter; and part III—Pool-level data elements to be reported for pools of single-family and multi-family AMA. The loan-level data elements contained in part I of both Appendices generally reflect characteristics of the loan or the borrower(s) and should not change over the life of the loan. As indicated above, to simplify the current reporting requirements, loan-level data specified in part I would only be required to be submitted during the calendar quarter in which the loan is acquired by a Bank.

The loan-level data elements contained in part II of the Appendices would include data that the Bank would be required to report for all single-family and multi-family AMA outstanding in a calendar quarter. These data elements are more meaningful when monitored on a continuing basis. This information would be used by the Finance Board to create and maintain a database to be used for safety and soundness monitoring, particularly of the Bank's risk management.

Part III of the Appendices would contain the data that the Bank would be required to report for pools or assets backed by pools. This information also would be used by the Finance Board to monitor the safety and soundness of the Bank's AMA program.

The Finance Board seeks comments on whether the data descriptions in proposed Appendices A and B are clear with regard to whole loans, or pools of such loans, that would back assets described in proposed § 955.3(c).

*Failure to obtain data elements.* The Finance Board recognizes that members or housing associates from whom the Banks acquire AMA may be unable to supply, or may fail to supply, all of the data items specified in Appendices A and B for all assets.

Neither the Bank, nor the member or housing associate from which the Bank acquires an asset, is expected to guarantee that all data items for each asset will be supplied. However, the Finance Board does expect the Banks to: Monitor how completely members or housing associates supply the requested data; identify and report to the Finance Board difficulties, problems or issues with respect to particular data fields or particular members or housing associates; and work with members and housing associates to minimize gaps in the data submissions. This guidance should not be interpreted to mean that the Banks may acquire an asset or a pool of assets if the Banks cannot collect data items necessary for purposes of establishing the equivalent credit rating of such asset or pool of assets under proposed § 955.5(a).

#### *G. Administrative and Investment Transactions Between Banks—Proposed § 955.8*

Under the proposed rule, the provisions governing administrative and investment transactions between Banks, which currently are contained in § 955.5, would be relocated to § 955.8. See 12 CFR 955.5. Section 955.5(c) of the current rule states that a Bank that has delegated its AMA pricing function to another Bank shall retain a right to refuse to acquire AMA at prices it does not consider appropriate. 12 CFR 955.5(c). Under the AMA programs, one Bank can provide the back-office services for other Banks. Section 955.5(c) was included in the current rule to ensure that the other Banks are not obligated to acquire AMA at prices set by the Bank providing the back-office functions. The Banks have now experienced several years of participation in AMA programs, which have grown significantly in volume. The Finance Board seeks comment on whether § 955.5(c) is no longer necessary or appropriate now that the Banks have more experience and options relating to AMA programs.

#### *H. Risk-Based Capital Requirement for AMA—Proposed § 955.9*

The proposed rule would include a risk-based capital provision that specifies the type and amount of capital that a Bank must hold against AMA for which the estimated credit rating is less than the second highest category of

investment grade, *e.g.*, less than AA. Until a Bank implements its capital structure plan and complies with the capital requirements of 12 CFR part 932, it must hold retained earnings against any outstanding AMA with an estimated credit rating of less than the second highest category of investment grade. The amount to be held is to be determined in accordance with Table 1 set forth in the proposed rule, which assigns a factor to particular credit rating categories. This provision simplifies § 955.6(a) of the current rule by eliminating the provision that would allow Banks to also hold general allowance for losses in meeting their risk-based capital requirement. Because the Banks do not hold general allowance for losses, this provision has no practical effect. *See* 12 CFR 955.6(a).

The proposed rule also would make clear that a Bank's risk-based capital requirement for its AMA is governed by § 955.9 only until it has implemented its capital structure plan and has complied with the capital requirements of 12 CFR part 932. After that time, a Bank would be governed solely by part 932 with respect to the risk-based capital requirement for AMA. This provision codifies a position previously stated by the Finance Board. *See* final AMA rule, 65 FR at 43978.

The proposed rule also would make a technical correction to apply the risk-based capital requirement to multi-family AMA, as well as single-family AMA.

The proposed rule would delete current § 955.6(b) regarding the recalculation of the credit enhancement, as provisions for dealing with a decline in the estimated credit rating of an AMA asset or pool of assets would be included under proposed § 955.5(a)(4), discussed above.

#### *I. Acquisition Restrictions on Certain Loans*

The Finance Board seeks comment on whether it should take measures to prevent a Bank from acquiring loans or assets backed by loans, through its AMA program, where the loans have certain features or were made under circumstances that may be considered "predatory" or "abusive." If the Finance Board seeks to limit the Banks' authority to acquire such loans, or assets backed by such loans, what specific measures would need to be incorporated in the rule? Among the issues on which the Finance Board seeks comments are:

(a) Whether the Finance Board should address concerns regarding the acquisition of loans or assets backed by loans where the loans have certain features or were made under

circumstances that may be considered "predatory" or "abusive," by adopting a new regulatory provision that would require each Bank to develop policies to preclude acquiring such loans, or assets backed by such loans;

(b) Whether the Finance Board should address the acquisition of loans or assets backed by loans where the loans have certain features or were made under circumstances that may be considered "predatory" or "abusive," through specific and detailed guidance to each Bank, as other Federal financial institution regulators have done with respect to the institutions they regulate; and

(c) How loans covered by such regulation or guidance should be identified.

#### **III. Paperwork Reduction Act**

The Finance Board's information collection related to AMA assets under the current rule has been reviewed and authorized by the Office of Management and Budget (OMB) under the Paperwork Reduction Act of 1995, as implemented by OMB in regulations at 5 CFR part 1320. The OMB control number is 3069-0058. As described more fully in part F of the **SUPPLEMENTARY INFORMATION** regarding information collection under the proposed section 955.7, the proposed rule makes a series of minor changes to the information presently collected under the current information collection. Because the information collection changes contained in this proposed rule are neither substantive nor material, no additional review or approval is required from OMB. Thus, the Finance Board has not submitted any information to OMB for review.

#### **IV. Regulatory Flexibility Act**

The proposed rule, if adopted as a final rule, will apply only to the Banks, which do not come within the meaning of "small entities," as defined in the Regulatory Flexibility Act (RFA). *See* 5 U.S.C. 601(6). Therefore, in accordance with section 605(b) of the RFA, 5 U.S.C. 605(b), the Finance Board hereby certifies that the proposed rule, if promulgated as a final rule, will not have a significant economic impact on a substantial number of small entities.

#### **List of Subjects**

##### *12 CFR Part 900*

Credit, Federal home loan banks, Reporting and recordkeeping requirements.

##### *12 CFR Part 932*

Capital, Credit, Federal home loan banks, Housing, Investments, Reporting and recordkeeping requirements.

##### *12 CFR Part 955*

Credit, Federal home loan banks, Housing, Reporting and recordkeeping requirements.

Accordingly, the Finance Board hereby proposes to amend parts 900, 932 and 955, chapter IX, title 12, *Code of Federal Regulations*, to read as follows:

#### **PART 900—GENERAL DEFINITIONS APPLYING TO ALL FINANCE BOARD REGULATIONS**

1. The authority citation for part 900 continues to read as follows:

**Authority:** 12 U.S.C. 1422b(a).

2. Revise the definition of "acquired member assets" to read as follows:

##### **§ 900.2 Terms relating to Bank operations, mission and supervision.**

\* \* \* \* \*

*Acquired member assets* or *AMA* means assets acquired in accordance with, and satisfying the applicable requirements of, §§ 955.3, 955.4 and 955.5 of this chapter.

\* \* \* \* \*

#### **PART 932—FEDERAL HOME LOAN BANK CAPITAL REQUIREMENTS**

3. The authority citation for part 932 continues to read as follows:

**Authority:** 12 U.S.C. 1422a(a)(3), 1422b(a), 1426, 1440, 1443, 1446.

##### **§ 932.4 [Amended]**

4. Amend the first sentence in § 932.4(e)(2)(ii)(E) by:

- a. Removing the phrase "described in § 955.2 of this chapter"; and
- b. Removing "§ 955.3" and adding, in its place, "§ 955.5".

##### **§ 932.9 [Amended]**

5. Amend the first sentence of § 932.9(a)(3) by removing the phrase "acquired member assets identified in § 955.2(a)(3) of this chapter or are otherwise".

6. Revise part 955 to read as follows:

#### **PART 955—ACQUIRED MEMBER ASSETS**

Sec.

955.1 Definitions.

955.2 Authorization to invest in AMA.

955.3 Asset requirement.

955.4 Member or housing associate nexus requirement.

955.5 Credit risk-sharing requirements.

955.6 Restructuring of AMA.



- 955.7 Reporting requirements.  
 955.8 Administrative and investment transactions between Banks.  
 955.9 Risk-based capital requirement.

Appendix A to Part 955—Reporting Requirements for AMA That Are Single-Family

Residential Mortgage Loans or Single-Family Residential Mortgage Loans Backing AMA

Appendix B to Part 955—Reporting Requirements for AMA That Are Multi-Family

Residential Mortgage Loans or Multi-Family Residential Mortgage Loans Backing AMA

**Authority:** 12 U.S.C. 1422a(a)(3), 1422b(a), 1426, 1430, 1430b, 1431.

**§ 955.1 Definitions.**

As used in this part:

*Acquired member assets* or *AMA* means assets acquired in accordance with, and satisfying the applicable requirements of, §§ 955.3, 955.4 and 955.5.

*AMA Product* means an AMA structure defined by a specific set of terms and conditions.

*Investment grade* means a credit quality rating in one of the four highest credit rating categories provided by an NRSRO.

*Pool* means a group of assets acquired under a given master commitment or similar agreement.

*Residential real property* has the meaning set forth in § 950.1 of this chapter.

**§ 955.2 Authorization to invest in AMA.**

Each Bank is authorized to invest in assets that qualify as AMA, subject to the requirements of this part and part 980 of this chapter.

**§ 955.3 Asset requirement.**

Assets that qualify as AMA shall be limited to the following:

(a) Whole loans that are eligible to secure advances under §§ 950.7(a)(1)(i), (a)(2)(ii), (a)(4), or (b)(1) of this chapter, excluding:

(1) Single-family mortgage loans where the loan amount exceeds the limits established pursuant to 12 U.S.C. 1717(b)(2); and

(2) Loans made to an entity, or secured by property, not located in a state;

(b) Whole loans secured by manufactured housing, regardless of whether such housing qualifies as residential real property under state law; or

(c) Other assets that are created by a member or housing associate in cooperation with a Bank, where the assets are backed by whole loans that meet the requirements of paragraphs (a)

or (b) of this section, provided that the Bank must initially acquire substantially all of such assets and the assets do not constitute interest only strips (IO), principal only strips (PO), or other interests in the underlying loans that have risk characteristics that are similar to IO or PO instruments.

**§ 955.4 Member or housing associate nexus requirement.**

(a) In the case of assets described in §§ 955.3(a) and (b), a Bank shall acquire the assets, by means of either a purchase or a funding transaction, only from:

(1) A member or housing associate of the Bank;

(2) A member of another Bank, pursuant to an arrangement with that other Bank; or

(3) Another Bank.

(b) In the case of assets described in § 955.3(c):

(1) The whole loans underlying the assets shall be acquired only from:

(i) A member or housing associate of the Bank;

(ii) A member of another Bank, pursuant to an arrangement with that other Bank; or

(iii) A Bank, if approved by the Finance Board under § 955.6; and

(2) The assets may be sold by a Bank only to other Banks or to members of any Bank.

**§ 955.5 Credit risk-sharing requirements.**

(a) *Required credit risk-sharing structure.* (1) *Product requirement.* For each AMA Product, the Bank shall implement, and have in place, a credit risk-sharing structure under which a member or housing associate provides the credit enhancement necessary to enhance an asset or pool of assets acquired by the Bank to a credit quality that is equivalent to investment grade.

(2) *Asset requirement.* For each AMA asset or pool of assets to be acquired, a Bank shall specify the particular credit rating within investment grade to which the credit quality of the asset or pool of assets shall be equivalent, after accounting for the credit enhancement provided by the member or housing associate.

(3) *Satisfaction of credit enhancement requirement.* For each AMA Product, prior to the acquisition of any asset or pool of assets and throughout the life of the asset or pool of assets on the Bank's books, the Bank shall have in place a process and methodology that, to the satisfaction of the Finance Board:

(i) Determines the applicable credit enhancement required under paragraphs (a)(1) and (a)(2) of this section; and

(ii) Demonstrates that the economic value of the credit enhancement

provided by the member or housing associate is sufficient to meet the applicable credit enhancement required under paragraphs (a)(1) and (a)(2) of this section.

(4) *Decline in estimated credit rating.* If the estimated credit rating of an asset or pool of assets declines to a credit rating below the credit rating required by the Bank at the time of acquisition of the asset or pool of assets, the Bank, at its discretion, shall either:

(i) Require the member or housing associate to provide additional credit enhancement in an amount sufficient to restore the estimated credit rating for such asset or pool of assets; or

(ii) Recalculate, and comply with, the risk-based capital requirement for the asset or pool of assets in accordance with § 932.4 of this chapter or § 955.9, as applicable, based on the reduced estimated credit rating.

(b) *Credit enhancement requirements.*

(1) *Members and housing associates.*

The credit enhancement required under paragraphs (a)(1) and (a)(2) of this section shall be provided by:

(i) A member or housing associate of the Bank; or

(ii) With the approval of both Banks, a member or housing associate of another Bank.

(2) *Economic cost.* The member or housing associate that initially provides the required credit enhancement shall bear all of the economic consequences of the credit enhancement responsibility.

(3) *Direct obligations.* Any portion of the required credit enhancement that is a direct obligation of a member or housing associate of any Bank and that is not covered by insurance from a third party insurance company, shall be fully secured by collateral eligible to secure advances under part 950 of this chapter, except as otherwise provided in this paragraph. If a member or housing associate transfers such credit enhancement responsibility to another member or housing associate, the successor shall continue to satisfy the collateral requirement. In lieu of obtaining collateral to secure such direct obligations, a Bank may hold permanent capital (or retained earnings, if the Bank has not yet converted its capital structure) against the direct obligation in an amount equal to 100 percent of the nominal value of the direct obligation. This requirement shall apply in addition to the risk-based capital requirements under § 932.4 of this chapter or § 955.9, as applicable.

(4) *Mortgage insurance.* A member or housing associate may provide all or a portion of its required credit enhancement through mortgage

insurance purchased from an insurer that is rated not lower than the second highest credit rating. If the rating of the insurer falls below the second highest credit rating, the member or housing associate shall have 60 days to replace the insurer with another insurer rated not lower than the second highest credit rating.

(c) *Grandfathered transactions.* Assets acquired in transactions otherwise authorized by resolution of the Finance Board and that are within any total dollar cap established by the Finance Board at the time of such authorization, shall not be subject to the requirements of this section.

**§ 955.6 Restructuring of AMA.**

A Bank shall not alter the credit risk-sharing structure of any AMA that it has acquired, nor shall it take any actions with the intent or effect of altering the actual or putative credit rating of any such AMA, without the prior approval of the Finance Board. A Bank also shall not sell or otherwise use any AMA in order to create a new type of asset, including assets described in § 955.3(c), without prior Finance Board approval.

**§ 955.7 Reporting requirements.**

(a) *Bank responsibility for collecting and maintaining data.* Each Bank that has members or housing associates that have provided the initial credit enhancement for AMA, shall be responsible for collecting and maintaining the loan-level and pool-level data required by this section for all residential mortgage loans that constitute or otherwise back such AMA, including assets described in § 955.3(c).

(b) *Loan-level data elements.* The loan-level data collected and maintained by each Bank shall include the data elements specified in Appendix A, Parts I and II, or in Appendix B, Parts I and II.

(c) *Pool-level data elements.* The pool-level data collected and maintained by each Bank shall include the data elements specified in Appendix A, Part III, or in Appendix B, Part III.

(d) *Quarterly Mortgage Reports.* Beginning in calendar year 2004, each Bank that is required to collect and maintain data under this section shall be responsible for submitting such data to the Finance Board within 60 days of the end of each calendar quarter and in a machine-readable format specified by the Finance Board.

(e) *Additional reports.* The Finance Board may at any time require a Bank to submit reports in addition to those required under paragraph (d) of this section.

**§ 955.8 Administrative and investment transactions between Banks.**

(a) *Delegation of administrative duties.* A Bank may delegate the administration of an AMA Product to another Bank whose administrative office has been examined and approved by the Finance Board to process AMA transactions. Prior to entering into any AMA-related agreements with a member or housing associate, a Bank shall disclose the existence of any such delegation, or the possibility that the Bank may later make such a delegation.

(b) *Terminability of agreements.* Any agreement made between two or more Banks in connection with any AMA Product shall be made terminable by either party after a reasonable notice period.

(c) *Delegation of pricing authority.* A Bank that has delegated its AMA pricing function to another Bank shall retain a right to refuse to acquire AMA at prices it does not consider appropriate.

**§ 955.9 Risk-based capital requirement.**

(a) *General.* Until a Bank implements its capital structure plan and complies with part 932 of this chapter, it shall hold retained earnings against any outstanding AMA for which the estimated credit rating is less than the second highest category of investment grade.

(b) *Requirement.* The amount of retained earnings to be held under this section shall be at least equal to the product of the outstanding balance of the AMA and the factor associated with its putative credit rating, as set forth in Table 1 of this section.

TABLE 1

Putative credit rating of AMA	Percentage applicable to on-balance sheet equivalent value of AMA
Third Highest Investment Grade .....	0.90
Fourth Highest Investment Grade .....	1.50
If Downgraded to Below Investment Grade After Acquisition By Bank:	
Highest Below Investment Grade .....	2.25
Second Highest Below Investment Grade .....	2.60
All Other Below Investment Grade .....	100.00

**Appendix A to Part 955—Reporting Requirements for AMA That Are Single-Family Residential Mortgage Loans or Single-Family Residential Mortgage Loans Backing AMA**

**Part I—Fields To Be Reported for All Such Loans Acquired During the Calendar Quarter**

1. *Bank District Flag*—Two-digit code designating the District Bank where the member institution that initially provides the credit enhancement for the AMA is located.

2. *Program Type*—Two-digit code, as designated by the Finance Board, identifying AMA Program type (e.g., MPP-FHA; MPP-100, etc.).

3. *Loan Number*—Bank assigned numeric identifier, unique to each mortgage loan within a Bank's AMA portfolio.

4. *Pool Number*—Bank assigned numeric identifier for the pool in which the mortgage loan is a part; the Pool Number should be unique within a Bank's AMA portfolio.

5. *U.S. Postal State*—Two-digit Federal Information Processing Standard (FIPS) code for the property.

6. *U.S. Postal Zip Code*—Five-digit zip code for the property.

7. *MSA Code*—Five-digit code for the property's Metropolitan Statistical Area (MSA).

8. *County*—Three-digit FIPS code for the property's county, as designated in the most recent decennial census by the Bureau of the Census.

9. *Census Tract/Block Numbering Area (BNA)*—Tract/BNA number for the property as used in the most recent decennial census by the Bureau of the Census.

10. *Borrower(s) Annual Income*—Combined income of all borrowers at the time of mortgage loan origination.

11. *Acquisition Unpaid Principal Balance (UPB)*—UPB in whole dollars of the mortgage loan when the loan was first acquired by a Bank, or of each mortgage loan backing an asset when such asset was first acquired by a Bank.

12. *Loan-to-Value (LTV) Ratio at Origination*—LTV ratio of the mortgage loan at the time of origination.

13. *Date of Mortgage Loan*—Date the mortgage loan was originated.

14. *Date of Acquisition*—Date a Bank first acquires the mortgage loan, or the asset backed by the mortgage loan.

15. *Purpose of Mortgage Loan*—Code indicating the purpose of the mortgage loan (e.g., purchase money mortgage, refinancing, construction mortgage, property rehabilitation).

16. *Product Type*—Code indicating the product type of the mortgage (e.g., fixed rate mortgage, adjustable rate mortgage (ARM), balloon mortgage, graduated payment mortgage (GPM) or growing equity mortgage (GEM), reverse annuity mortgage, or other).

17. *Federal Insurance or Guarantee*—Code that indicates whether any part of the mortgage loan has Federal insurance or a Federal guarantee, and from which agency.

18. *Primary Mortgage Insurance Percent*—Percent of loan balance at origination covered by private and/or government mortgage insurance.

19. *Term of Mortgage at Origination*—Term of the mortgage loan at the time of origination, in months.

20. *Amortization Term*—For amortizing mortgage loans, the amortization term of the mortgage loan, in months.

21. *FHFBID Number*—Federal Housing Finance Board Identification Number of the member institution that initially provides the credit enhancement for the AMA.

22. *Number of Borrowers*—Number of borrowers at the time of origination.

23. *First-Time Home Buyers*—Code indicating whether the mortgagor(s) are first-time homebuyers.

24. *Borrower Race*—Code indicating the race of the borrower (e.g., Asian, Native Hawaiian or Other Pacific Islander). Codes are to be consistent with the race codes used in the latest decennial census.

25. *Borrower Ethnicity*—Code indicating the ethnicity of the borrower (i.e., “Hispanic or Latino” or “Not Hispanic or Latino”), consistent with the latest decennial census ethnicity codes.

26. *Co-Borrower Race*—Code indicating the race of the co-borrower (e.g., Asian, Native Hawaiian or Other Pacific Islander). Codes are to be consistent with the race codes used in the latest decennial census.

27. *Co-Borrower Ethnicity*—Code indicating the ethnicity of the co-borrower (i.e., “Hispanic or Latino” or “Not Hispanic or Latino”), consistent with the latest decennial census ethnicity codes.

28. *Borrower Gender*—Code that indicates whether the borrower is male or female.

29. *Co-Borrower Gender*—Code that indicates whether the co-borrower is male or female.

30. *Age of Borrower*—Age of borrower, in years, at the time of mortgage loan origination.

31. *Age of Co-Borrower*—Age of co-borrower, in years, at the time of mortgage loan origination.

32. *Occupancy Code*—Code that indicates whether the mortgaged property is an owner-occupied principal residence, or a rental investment property.

33. *Number of Units*—Number of units in the mortgaged property (i.e., one to four).

34. *Unit—Number of Bedrooms*—Four separate fields indicating, where the property contains non-owner-occupied dwelling units, the number of bedrooms in each of those units.

35. *Unit—Reported Rent Level*—Four separate fields indicating, where the property contains non-owner-occupied dwelling units, the rent level for each unit in whole dollars.

36. *Unit—Reported Rent Level Plus Utilities*—Four separate fields indicating, where the property contains non-owner-occupied dwelling units, the rent level plus the utility cost for each unit in whole dollars.

37. *Unit—Owner-Occupied*—Four separate fields indicating whether each of the units is owner-occupied.

38. *Original Interest Rate*—Interest rate on the loan at the time of origination.

39. *Loan Amount*—Mortgage loan balance at the time of origination.

40. *Front-end Ratio*—Ratio of principal, interest, taxes, and insurance to Borrower(s) Annual Income at the time of origination.

41. *Back-end Ratio*—Ratio of all debt payments to Borrower(s) Annual Income at the time of origination.

42. *Type of Credit Score*—Code indicating borrower(s) credit score type (i.e., Fair, Isaacs, Co. (FICO) or NextGen FICO).

43. *Borrower Credit Score*—The Fair, Isaacs, Co. (FICO) or NextGen FICO credit score of borrower at the time of mortgage loan origination.

44. *Co-Borrower Credit Score*—The Fair, Isaacs, Co. (FICO) or NextGen FICO credit score of co-borrower at the time of mortgage loan origination.

45. *Self-Employed Indicator*—Code indicating whether the borrower was self-employed at the time of mortgage loan origination.

46. *Property Type*—Code indicating the type of property (e.g., single-family detached, condominium, PUD).

47. *ARM Index*—For ARMs only, index used for the calculation of interest on an ARM.

48. *ARM Margin*—For ARMs only, margin added to the index used for the calculation of the interest on an ARM.

49. *Adjustment Frequency*—For ARMs only, interest rate adjustment frequency in months.

50. *Negative Amortization*—For ARMs only, code indicating if amortization is negative.

51. *Prepayment Penalty Date*—Date that the application of a prepayment penalty ends.

#### **Part II—Fields To Be Reported for All Such Loans That Are Outstanding in the Calendar Quarter**

52. *Bank District Flag*—Two-digit code designating the District Bank where the member institution that initially provides the credit enhancement for the AMA is located.

53. *Loan Number*—Bank assigned numeric identifier, unique to each mortgage loan within a Bank’s AMA portfolio.

54. *Delinquency Status*—Code indicating the delinquency status of the mortgage loan at the end of the calendar quarter.

55. *Termination Date*—For mortgage loans that terminated during the calendar quarter, date on which the mortgage loan terminated.

56. *Termination Type*—For mortgage loans that terminated during the calendar quarter, code indicating the reason for the mortgage loan termination (e.g., prepayment, foreclosure).

57. *Current Unpaid Principal Balance (UPB)*—UPB on the mortgage loan at the end of the calendar quarter.

58. *Current Coupon*—For ARMs only, mortgage interest rate on the mortgage loan at the end of the calendar quarter.

#### **Part III—Fields To Be Reported for Pools of Such Loans**

59. *Bank District Flag*—Two-digit code designating the District Bank where the member institution that initially provides the credit enhancement for the AMA is located.

60. *Pool Number*—Bank assigned numeric identifier for the pool in which the mortgage loan is a part; the Pool Number should be unique within a Bank’s AMA portfolio.

61. *Participation Percentages*—Twelve separate fields indicating each Bank’s

percentage participation in the AMA-eligible pool or asset backed by such a pool, as of the date the Bank acquires any portion of the pool or asset.

62. *Pool Rating*—For pools of mortgage loans or assets backed by such mortgage loans, the putative or actual letter credit rating of the pool as of the date the Bank acquires any portion of the pool or asset backed by such pools.

63. *Pool Credit Enhancement*—The dollar amount of the credit enhancement required to bring the pool to the credit rating as specified by the Bank.

64. *Recalculated Pool Rating*—For pools of mortgage loans where the credit enhancement is recalculated during the calendar quarter, the recalculated putative or actual letter credit rating using the initial amount of the Pool Credit Enhancement.

65. *Recalculated Credit Enhancement*—For pools of mortgage loans that have the credit enhancement recalculated during the calendar quarter, the dollar amount of the credit enhancement required to bring the pool to the initial putative or actual letter credit rating.

#### **Appendix B to Part 955—Reporting Requirements for AMA That Are Multi-Family Residential Mortgage Loans or Multi-Family Residential Mortgage Loans Backing AMA**

##### **Part I—Fields To Be Reported for All Such Loans Acquired During the Calendar Quarter**

1. *Bank District Flag*—Two-digit code designating the District Bank where the member institution that initially provides the credit enhancement for the AMA is located.

2. *Program Type*—Two-digit code, as designated by the Finance Board, identifying AMA Program type.

3. *Loan Number*—Bank assigned numeric identifier, unique to each mortgage loan within a Bank’s AMA portfolio.

4. *Pool Number*—Bank assigned numeric identifier, for the pool in which the mortgage loan is a part; the Pool Number should be unique within a Bank’s AMA portfolio.

5. *U.S. Postal State*—Two-digit Federal Information Processing Standard (FIPS) code for the property.

6. *U.S. Postal Zip Code*—Five-digit zip code for the property.

7. *MSA Code*—Five-digit code for the property’s Metropolitan Statistical Area (MSA).

8. *County*—Three-digit FIPS code for the property’s county, as designated in the most recent decennial census by the Bureau of the Census.

9. *Census Tract/Block Numbering Area (BNA)*—Tract/BNA number for the property as used in the most recent decennial census by the Bureau of the Census.

10. *Acquisition Unpaid Principal Balance (UPB)*—UPB in whole dollars of the mortgage loan when the loan was first acquired by a Bank, or of each mortgage loan backing an asset when such asset was first acquired by a Bank.

11. *Original Interest Rate*—Interest rate on the loan at the time of origination.

12. *Loan Amount*—Mortgage loan balance at the time of origination.

13. *Loan-to-Value (LTV) Ratio at Origination*—LTV ratio of the mortgage loan at the time of origination.

14. *Date of Mortgage Loan*—Date the mortgage loan was originated.

15. *Date of Acquisition*—Date a Bank first acquires the mortgage loan or the asset backed by the mortgage loan.

16. *Purpose of Mortgage Loan*—Code indicating the purpose of the mortgage loan (e.g., purchase money mortgage, refinancing, construction mortgage, property rehabilitation).

17. *Cooperative Project Loan*—Code indicating whether the mortgage loan is a project loan on a cooperative housing building.

18. *Mortgagor Type*—Code indicating the type of mortgagor (i.e., an individual, a for-profit entity such as a corporation or partnership, a nonprofit entity such as a corporation or partnership, a public entity, or other type of entity).

19. *Product Type*—Code indicating the product type of the mortgage (e.g., fixed rate mortgage, adjustable rate mortgage (ARM), balloon mortgage, graduated payment mortgage (GPM) or growing equity mortgage (GEM), reverse annuity mortgage, or other).

20. *Construction Loan*—Code indicating whether the mortgage is for a construction loan.

21. *Federal Insurance or Guarantee*—Code that indicates whether any part of the mortgage loan has Federal insurance or a Federal guarantee, and from which agency.

22. *Primary Mortgage Insurance Percent*—Percent of loan balance at origination covered by private and/or government mortgage insurance.

23. *FHA Risk Share Percent*—The percentage of the risk assumed for the mortgage purchased under a risk-sharing arrangement with FHA.

24. *Mortgage Purchased under the Banks' Community Investment Cash Advances (CICA) Programs*—Code indicating whether the mortgage is on a project under an AHP, CIP or other CICA program.

25. *Term of Mortgage at Origination*—Term of the mortgage loan at the time of origination, in months.

26. *Amortization Term*—For amortizing mortgage loans, the amortization term of the mortgage loan, in months.

27. *FHFBID Number*—Federal Housing Finance Board Identification Number of the member institution that initially provides the credit enhancement for the AMA.

28. *Number of Units*—The number of units in the mortgaged property.

29. *Public Subsidy Program*—Code indicating whether the mortgaged property is involved in a public subsidy program and which level(s) of government are involved in the subsidy program (i.e., Federal government only, other only, Federal government, etc.).

30. *Unit Class Level*—The following data apply to unit types in a particular mortgaged property. The unit types are defined by the Banks for each property and are differentiated based on the number of bedrooms in the units and on the average contract rent for the units. A unit type must be included for each bedroom size category in the property:

A. *Unit Type XX-Number of Bedroom(s)*—The number of bedrooms in the unit type;

B. *Unit Type XX-Number of Unit*—The number of units in the property within the unit type;

C. *Unit Type XX-Average Reported Rent Level*—The average rent level for the unit type in whole dollars;

D. *Unit Type XX-Average Reported Rent Plus Utilities*—The average reported rent level plus the utility cost for each unit in whole dollars; and

E. *Unit Type XX-Tenant Income Indicator*—Indicates whether the tenant's income is less than 60 percent of area median income, greater than or equal to 60 percent but less than 80 percent of area median income, greater than or equal to 80 percent but less than 100 percent of area median income, or greater than or equal to 100 percent of area median income.

31. *Debt Service Coverage Ratio*—Ratio of net operating income to debt service.

32. *ARM Index*—For ARMs only, index used for the calculation of interest on an ARM.

33. *ARM Margin*—For ARMs only, margin added to the index used for the calculation of the interest on an ARM.

34. *Adjustment Frequency*—For ARMs only, interest rate adjustment frequency in months.

35. *Negative Amortization*—For ARMs only, code indicating if amortization is negative.

36. *Prepayment Penalty Date*—Date that the application of a prepayment penalty ends.

#### Part II—Fields To Be Reported for All Such Loans That Are Outstanding in the Calendar Quarter

37. *Bank District Flag*—Two-digit code designating the District Bank where the member institution that initially provides the credit enhancement for the AMA is located.

38. *Loan Number*—Bank assigned numeric identifier, unique to each mortgage loan within a Bank's AMA portfolio.

39. *Delinquency Status*—Code indicating the delinquency status of the mortgage loan at the end of the calendar quarter.

40. *Termination Date*—For mortgage loans that terminated during the reporting period, date on which the mortgage loan terminated.

41. *Termination Type*—For mortgage loans that terminated during the calendar quarter, code indicating the reason for the mortgage loan termination (e.g., prepayment, foreclosure).

42. *Current Unpaid Principal Balance (UPB)*—UPB on the mortgage loan at the end of the calendar quarter.

43. *Current Coupon*—For ARMs only, mortgage interest rate on the mortgage loan at the end of the calendar quarter.

#### Part III—Fields To Be Reported for Pools of Such Loans

44. *Bank District Flag*—Two-digit code designating the District Bank where the member institution that initially provides the credit enhancement for the AMA is located.

45. *Pool Number*—Bank assigned numeric identifier for the pool of which the mortgage loan is a part; the Pool Number should be unique within a Bank's AMA portfolio.

46. *Participation Percentages*—Twelve separate fields indicating each Bank's percentage participation in the AMA-eligible pool or asset backed by such a pool, as of the date the Bank acquires any portion of the pool or asset.

47. *Pool Rating*—For pools of mortgage loans or assets backed by such mortgage loans, the putative or actual letter credit rating of the pool as of the date the Bank acquires any portion of the pool or asset backed by such pools.

48. *Pool Credit Enhancement*—The dollar amount of the credit enhancement required to bring the pool to the credit rating as specified by the Bank.

49. *Recalculated Pool Rating*—For pools of mortgage loans where the credit enhancement is recalculated during the calendar quarter, the recalculated putative or actual letter credit rating using the initial amount of the Pool Credit Enhancement.

50. *Recalculated Credit Enhancement*—For pools of mortgage loans that have the credit enhancement recalculated during the calendar quarter, the dollar amount of the credit enhancement required to bring the pool to the initial putative or actual letter credit rating.

Dated: June 19, 2003.

The Board of Directors of the Federal Housing Finance Board.

**John T. Korsmo,**

*Chairman.*

[FR Doc. 03-16477 Filed 6-30-03; 8:45 am]

BILLING CODE 6725-01-P

## DEPARTMENT OF THE INTERIOR

### Bureau of Indian Affairs

#### 25 CFR Chapter I

#### Meetings of the No Child Left Behind Negotiated Rulemaking Committee

**AGENCY:** Bureau of Indian Affairs, Interior.

**ACTION:** Announcement of negotiated rulemaking committee meetings.

**SUMMARY:** The Secretary of the Interior has established an advisory Committee to develop recommendations for proposed rules for Indian education under six sections of The No Child Left Behind Act of 2001. As required by the Federal Advisory Committee Act, we are announcing dates and locations of the next three meetings of the No Child Left Behind Negotiated Rulemaking Committee.

**DATES AND ADDRESSES:** The Committee's next three meeting dates and locations are :

July 14-18, 2003 Minneapolis, MN  
Marriott Airport Hotel, 2020 East 79th Street, Bloomington, MN 55425  
(beginning July 14 at 1:30 p.m. CDT and ending July 18 at 12 noon CDT)