

proposed regulation's impact on access to capital markets, cost of funds, and other costs to the Bank System. The Finance Board will take all comments into consideration before issuing a final regulation. For copies of public comments, contact Karen Rogers, Executive Secretary, by e-mail at rogersk@fhfb.gov, by facsimile at 202/408-2530, or by telephone at 202/408-2910.

II. Statutory and Regulatory Background

A. The Banks

The 12 Banks are privately owned "government-sponsored enterprises" (GSEs) organized under the authority of the Federal Home Loan Bank Act (Bank Act)¹ to support the financing of housing and community lending by their members.² The Bank Act requires the Banks to adopt a cooperative structure. Eligible financial institutions (principally, depository institutions) may become members of a Bank if they satisfy certain statutory and regulatory criteria and purchase a specified amount of a Bank's capital stock.³ Only Bank members may own Bank capital stock and share in Bank profits. Only Bank members, and certain eligible housing associates (such as State housing finance agencies), may borrow from or use other Bank products and services.⁴

B. The Finance Board

The Banks' regulator is the Finance Board, an independent agency in the executive branch of the U.S. government. The Finance Board's primary duty is to ensure that the Banks operate in a financially safe and sound manner. To the extent consistent with that duty, the Finance Board also must supervise the Banks, ensure that the Banks carry out their housing finance mission, and ensure that the Banks remain adequately capitalized and able to raise funds in the capital markets.⁵

C. Gramm-Leach-Bliley Act

The Gramm-Leach-Bliley Act⁶ (GLB Act) required the Banks to adopt new risk-based capital structures. On January 30, 2001, the Finance Board published a final regulation implementing new capital structure requirements for the Banks.⁷ As of July 18, 2002, the Finance Board had approved a new capital plan

for each of the Banks. To date, six Banks have implemented their capital plans and are operating under new capital structures. Until a Bank implements its capital plan, its capital structure is governed by the Finance Board's pre-GLB Act regulations.

D. Bank System Securities

Consolidated Obligations. The Bank Act authorizes the individual Banks to issue debt securities, subject to Finance Board regulation.⁸ While the Finance Board has not adopted regulations permitting the issuance of debt securities by individual Banks and no Bank has ever individually issued debt securities, the Finance Board has adopted regulations authorizing the Office of Finance (OF), a joint office of the Banks, as agent for the Banks, to offer, issue and service consolidated obligations on which the Banks are jointly and severally liable.⁹ The Banks, together with the OF, comprise the Bank System. The Banks' GSE status enables the OF to issue consolidated obligations at favorable rates. The Banks pass along their funding advantage to their members—and ultimately to consumers—by providing advances (secured loans) and other financial services to their members at lower rates than the members generally could obtain elsewhere. At June 30, 2003, the Bank System had \$507 billion of consolidated obligation bonds (maturity of one year or more) and \$134 billion of consolidated obligation discount notes (maturity of less than one year) outstanding.

Equity Securities. Banks that have implemented new capital plans may issue Class A stock or Class B stock (and each class may have subclasses). Shares of both Class A stock and Class B stock are issued at a par value of \$100 per share. Shares of Class A stock are redeemable in cash on six-months written notice to a Bank. Shares of Class B stock are redeemable in cash on five-years written notice to a Bank. The redemption price for shares of both Class A stock and Class B stock is \$100 per share.¹⁰ Banks that have not implemented new capital plans issue only one class of capital stock redeemable by the Bank on six-months notice. This capital stock is also purchased by the member and redeemed

by the Bank at a par value of \$100 per share. Each Bank may also repurchase outstanding shares of any type of Bank capital stock at a price of \$100 per share in certain circumstances.

E. 1933 Act and 1934 Act Exemptions Applicable to Bank Securities

1933 Act Exemption for Bank Equity and Debt Securities. Equity securities issued by individual Banks to their members and debt securities issued by the OF as agent for the Banks to public investors are exempt from the registration requirements of the Securities Act of 1933 (1933 Act)¹¹ because the Banks are persons "controlled or supervised by and acting as an instrumentality of the Government of the United States pursuant to authority granted by the Congress of the United States."¹²

1934 Act Exemption for Bank Debt Securities. Debt securities issued by the OF as agent for the Banks are exempt from the registration requirements of the Securities Exchange Act of 1934 (1934 Act).¹³ Sections 3(a)(12)(A) and 3(a)(42)(B) of the 1934 Act designate as exempt securities, "government securities," including "securities which are issued or guaranteed by corporations in which the United States has a direct or indirect interest and which are designated by the Secretary of the Treasury for exemption as necessary or appropriate in the public interest or for the protection of investors."¹⁴ In Release 34-1168 dated April 28, 1937, the SEC announced the Secretary of the Treasury's designation for exemption of those securities issued by the Federal Home Loan Bank Board (the predecessor agency to the Finance Board) or by the Banks under the authority of Section 11 of the Bank Act. The consolidated obligations issued by the OF as agent for the Banks are issued under the authority of Section 11(a) of the Bank Act.

Bank Equity Securities under the 1934 Act. The Secretary of the Treasury has not designated Bank equity securities for exemption under the 1934 Act.

Basis for 1933 Act and 1934 Act Exemptions. The Banks' 1933 Act and 1934 Act exemptions rest on a presumption, and the Finance Board's supervisory and examination authority over the Banks includes a responsibility to ensure, that the securities activities of government instrumentalities are conducted in the public interest and for the protection of investors. This obligation was reinforced when

¹ 12 U.S.C. 1421 *et seq.*

² 12 U.S.C. 1422a(a)(3)(B)(ii), 1430(i), (j).

³ 12 U.S.C. 1424, 1426.

⁴ 12 U.S.C. 1426, 1430, 1430b.

⁵ 12 U.S.C. 1422a(a)(3)(A), (B).

⁶ Pub. L. 106-102 (1999).

⁷ 66 FR 8262 (January 30, 2001).

⁸ 12 U.S.C. 1431(a).

⁹ 12 CFR 985.3(a). Prior to 2001, the OF performed the same functions for the Finance Board, which had issued consolidated obligations on behalf of the Banks pursuant to Section 11(c) of the Bank Act. The Finance Board no longer issues consolidated obligations on behalf of the Banks under Section 11(c).

¹⁰ 12 CFR 931.1.

¹¹ 15 U.S.C. 77a *et seq.*

¹² 15 U.S.C. 77c(a)(2).

¹³ 15 U.S.C. 78a *et seq.*

¹⁴ 15 U.S.C. 78c(a)(42)(B).