

Department of the Treasury

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Transfer Message, other documentation, or evidence submitted in support thereof.

§ 1511.8 Notice of attachment.

The interest of a debtor in a Security Entitlement may be reached by a creditor only by legal process upon the Securities Intermediary with whom the debtor's securities account is main-

tained, except where a Security Entitlement is maintained in the name of a secured party, in which case the debtor's interest may be reached by legal process upon the secured party. The regulations in this part do not purport to establish whether a Federal Reserve Bank is required to honor an order or other notice of attachment in any particular case or class of cases.

CHAPTER XVII—OFFICE OF FEDERAL HOUSING ENTERPRISE OVERSIGHT, DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

SUBCHAPTER A—OFHEO ORGANIZATION AND FUNCTIONS

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SUBCHAPTER A—OFHEO ORGANIZATION AND FUNCTIONS

PART 1700—ORGANIZATION AND FUNCTIONS

Sec.

1700.1 Office of Federal Housing Enterprise Oversight.

1700.2 Organization of the Office of Federal Housing Enterprise Oversight.

1700.3 Official logo and seal.

AUTHORITY: 5 U.S.C. 552; 12 U.S.C. 4513, 4526.

SOURCE: 59 FR 62304, Dec. 5, 1994, unless otherwise noted.

§ 1700.1 Office of Federal Housing Enterprise Oversight.

(a) *Scope and authority.* The Office of Federal Housing Enterprise Oversight (referred to as OFHEO) is an independent office within the Department of Housing and Urban Development. OFHEO was created by the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (Act), Title XIII of the Housing and Community Development Act of 1992 (Pub. L. 102-550, October 28, 1992; 106 Stat. 3943; 12 U.S.C. 4501, *et seq.*). OFHEO is responsible for the examination and financial regulation of the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac) (collectively, the Enterprises). OFHEO is charged with ensuring that the Enterprises are adequately capitalized and operating in a safe and sound manner. OFHEO's costs and expenses are funded by annual assessments paid by the Enterprises. OFHEO is headed by a Director, who is appointed by the President and confirmed by the Senate for a five-year term.

(b) *Location.* OFHEO is located at 1700 G Street NW., 4th Floor, Washington, DC 20552. OFHEO's hours of business are 8:30 a.m.–5:00 p.m. (eastern standard time), Monday through Friday, excluding Federal holidays.

§ 1700.2 Organization of the Office of Federal Housing Enterprise Oversight.

(a) *Director.* The Director has exclusive authority under the Act with respect to the management of OFHEO, and is responsible for directing the de-

velopment, implementation, and review of all OFHEO programs and functions. The Director appoints such personnel as may be necessary to carry out the functions of OFHEO. The Director may delegate to OFHEO officers and employees any of the functions, powers, and duties of the Director, as the Director considers appropriate. The Director may establish and fix the responsibilities of the offices within OFHEO as the Director deems necessary for the efficient functioning of OFHEO.

(b) *Deputy Director.* The Deputy Director of OFHEO is appointed by the Director in accordance with the Act. In the event of the absence, sickness, death or resignation of the Director, the Deputy Director serves as acting Director until the Director's return or the confirmation of a successor. The Deputy Director performs such functions, powers and duties as the Director determines are necessary with respect to OFHEO's management and the development and implementation of OFHEO's programs and functions.

(c) *Executive Director and Chief of Staff.* The Executive Director and Chief of Staff of OFHEO heads the Office of Executive Director. The Executive Director and Chief of Staff reports to the Director and the Deputy Director. The Executive Director and Chief of Staff is the chief administrative officer of OFHEO, serves as a legal advisor on administrative matters, and coordinates communication and cooperation on administrative issues with the Office of General Counsel.

(d) *Offices and functions.* (1) Office of Executive Director. The Office of Executive Director consists of the Office of Budget and Financial Management, the Office of Human Resources Management, the Office of Technology and Information Management, and the Office of Strategic Planning and Management. The Office of Executive Director is responsible for OFHEO-wide management and oversight of all administrative matters.

(2) *Office of Examination.* The Office of Examination plans and conducts examinations of the Enterprises, as required by the Act, prepares and issues reports of examination summarizing the financial condition and management practices of each Enterprise, and seeks preventative and corrective actions as appropriate. The Office complements its on-site examination activities with off-site financial safety and soundness monitoring.

(3) *Office of Capital Supervision.* The Office of Capital Supervision ensures the comprehensive evaluation and classification of the capital adequacy of the Enterprises, the assessment of risks that impact capital and the development of tools to measure such risks. The Office ensures the integrity of capital classifications by effectively producing results under the minimum and risk based capital models and systems and by implementing appropriate enhancements to those measures. The Office assesses new GSE activities under the capital regime and addresses changes in accounting standards. The Office supports its responsibilities as well as other OFHEO offices through research on alternative models and measurements of risk and capital adequacy.

(4) *Office of General Counsel.* The Office of General Counsel advises the Director and OFHEO staff on all legal matters concerning the functions, activities, and operations of OFHEO and of the Enterprises under the Act. The Office is responsible for interpreting the Act and other applicable law, including financial institutions regulatory issues, securities and corporate law principles, and administrative and general legal matters. This Office also coordinates the preparation of legislation and agency regulations and works with other counsels in the government.

(5) *Office of External Relations.* The Office of External Relations is responsible for coordinating and communicating on behalf of OFHEO with the Congress, for monitoring relevant legislative developments, and for analyzing and assisting the Director in developing legislative proposals. The Office also is responsible for directing and coordinating communication with the news media and the public as well

as participating in planning programs for OFHEO.

(6) *Office of Policy Analysis and Research.* The Office of Policy Analysis and Research conducts policy analysis and research to assess the short- and long-term impact on the regulatory and supervisory functions of OFHEO of trends and developments in Enterprise activities, housing finance and financial regulation. The Office also prepares data series, reports and research papers; works with other OFHEO offices to develop policy options; and, makes recommendations to the Director on a broad range of policy issues.

(7) *Office of Compliance.* The Office of Compliance assists the Director in ensuring that the Enterprises operate in compliance with applicable laws, regulations and safety and soundness standards. The Office conducts special review and examinations on focused issues that may arise at the enterprises or that are of concern to OFHEO, often in coordination with other OFHEO offices, to assess compliance and obtain information. The Office also assists in providing information for enforcement actions and other activities as requested by the Director.

(8) *Office of Chief Accountant.* The Office of Chief Accountant advises the Director and OFHEO staff on all accounting matters related to the Enterprises. The Office develops policies regarding accounting and financial reporting and monitors accounting standards that affect the Enterprises, working with the Enterprises at a policy level on emerging issues. The Office supports and coordinates accounting resources within the agency to assure the best and most efficient use of those resources. The Office supports other offices in providing consistent accounting policy interpretation across OFHEO and works with external constituencies on accounting issues.

(e) *Additional information.* Current information on the organization of OFHEO may be obtained by mail from the Office of External Affairs, 1700 G Street NW, 4th Floor, Washington, DC 20552. Such information, as well as other OFHEO information, also may be obtained electronically by accessing

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OFHEO's website located at *www.OFHEO.gov*.

[59 FR 62304, Dec. 5, 1994, as amended at 65 FR 39787, June 28, 2000; 69 FR 18809, Apr. 9, 2004; 70 FR 59629, Oct. 13, 2005]

§ 1700.3 Official logo and seal.

The section describes and displays the logo adopted by the Director as the official symbol representing the Office of Federal Housing Enterprise Oversight. It is displayed on correspondence, selected documents, and signage. The logo serves as the official seal to authenticate official documents of the Agency.

(a) *Description.* The logo is a disc consisting of two concentric circles enclosing the words "Office of Federal Housing Enterprise Oversight" and the inaugural year, 1993. In the center of the disc is a stylized image of a structure consisting of a solid two-tiered pedestal base topped by a solid triangular shape, which represents the roof of the structure. Placed between the base and the top are the letters "OFHEO." These letters spell out the acronym of the Office of Federal Housing Enterprise Oversight and act as a visual link between the top and bottom of the structure.

(b) *Display.* The Office of Federal Housing Enterprise Oversight's official logo and seal appears below:



[68 FR 32629, June 2, 2003]

PART 1701—ASSESSMENTS

Sec.
1701.1 Purpose.
1701.2 Definitions.
1701.3 Annual assessment.

1701.4 Increase in semiannual payment.
1701.5 Notice and review.
1701.6 Delinquent payment.
1701.7 Enforcement of payment.
1701.8 Deposit in fund.

AUTHORITY: 12 U.S.C. 4513(b)(1) and 12 U.S.C. 4516.

SOURCE: 66 FR 18039, Apr. 5, 2001, unless otherwise noted.

§ 1701.1 Purpose.

This part sets forth the policy and procedures of OFHEO with respect to the establishment and collection of the annual assessments of the Enterprises under section 1316 of the Act (12 U.S.C. 4516).

§ 1701.2 Definitions.

For purposes of this part, the term—

(a) *Act* means the Federal Housing Enterprises Financial Safety and Soundness Act of 1992, Title XIII of the Housing and Community Development Act of 1992, Pub. L. 102-550, section 1301, Oct. 28, 1992, 106 Stat. 3672, 3941-4012 (1993) (12 U.S.C. 4501 *et seq.*).

(b) *Adequately capitalized* means the adequately capitalized capital classification under section 1364 of the Act (12 U.S.C. 4614).

(c) *Director* means the Director of the Office of Federal Housing Enterprise Oversight or his or her designee.

(d) *Enterprise* means the Federal National Mortgage Association or the Federal Home Loan Mortgage Corporation; and the term "Enterprises" means, collectively, the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation.

(e) *Surplus funds* means funds that are not obligated as of September 30 of each fiscal year that were collected from any Enterprise pursuant to § 1701.3 or § 1701.4.

(f) *Total assets* means the sum, as of the most recent June quarterly minimum capital report of the Enterprise, of the amounts of the following assets that are used to calculate the quarterly minimum capital requirement of the Enterprise under 12 CFR part 1750:

- (1) On-balance sheet assets;
- (2) Off-balance sheet mortgage-backed securities; and
- (3) Other off-balance sheet obligations.

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(g) *OFHEO* means the Office of Federal Housing Enterprise Oversight.

§ 1701.3 Annual assessment.

(a) *Establishment of assessment.* The Director may, to the extent provided in appropriation acts, establish and collect from the Enterprises an annual assessment for each fiscal year, as allocated under paragraph (b) of this section. The amount of the annual assessment shall not exceed the estimated amount to be sufficient to provide for the necessary administrative and non-administrative expenses to carry out the responsibilities of the Director relating to the Enterprises and to carry out the purposes of the Act.

(b) *Allocation and proportional share.* The annual assessment established under paragraph (a) of this section shall be allocated between the Enterprises. Each Enterprise shall pay a proportional share of the annual assessment that bears the same ratio to the total annual assessment as the total assets of each Enterprise bears to the total assets of both Enterprises.

(c) *Timing and amount of semiannual payment.* (1) Each Enterprise shall pay on or before October 1 and April 1 of each fiscal year an amount of one-half of its proportional share of the annual assessment, except:

(i) As provided in paragraph (c)(2) of this section;

(ii) To the extent surplus funds are credited under paragraph (d) of this section; and

(iii) To the extent a semiannual payment is increased under §1701.4.

(2) If OFHEO is operating under a continuing appropriation as of October 1 of any year, each Enterprise shall pay, on such date as determined by the Director, an amount calculated by applying the annual assessment proportion calculated under paragraph (b) of this section to the amount authorized for expenditure. When OFHEO receives a regular appropriation, the amount of the allocation share of the annual assessment collected from each Enterprise shall be reduced by any partial payments made by each Enterprise in connection with any continuing appropriations.

(d) *Surplus funds.* Surplus funds shall be credited to the annual assessment

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by reducing the amount collected by the amount of the surplus funds. Surplus funds shall be allocated in the same proportion in which they were collected, except as determined by the Director.

§ 1701.4 Increase in semiannual payment.

The Director, in his or her discretion, may increase any semiannual payment to be collected under §1701.3 from an Enterprise that is not classified as adequately capitalized as necessary to pay additional estimated costs of regulation of the Enterprise.

§ 1701.5 Notice and review.

(a) *Written notice.* The Director shall provide each Enterprise with written notice of the annual assessment, the semiannual payments and any partial payments to be collected under this part. In addition, the Director shall provide each Enterprise with written notice of any changes in the assessment procedures that the Director, in his or her sole discretion, deems necessary under the circumstances.

(b) *Request for review.* At the written request of an Enterprise, the Director, in his or her discretion, may review the calculation of the proportional share of the annual assessment, the semiannual payments, and any partial payments to be collected under this part. The determination of the Director is final. Except as provided by the Director, review by the Director does not suspend the requirement that the Enterprise make the semiannual payment or partial payment on or before the date it is due.

§ 1701.6 Delinquent payment.

(a) *Interest and penalties.* The Director may assess interest and penalties on any delinquent semiannual payment or partial payment collected under this part in accordance with 31 U.S.C. 3717 (interest and penalty on claims) and 12 CFR part 1704 (debt collection). The Director may waive interest and penalties in his or her discretion.

(b) *Transfer to general fund.* Any interest and penalties collected under this section shall be transferred to the general fund of the Treasury of the United States.

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§ 1701.7 Enforcement of payment.

Notwithstanding § 1701.6, the Director may enforce the payment of any assessment under this part pursuant to the authorities of sections 1371 (12 U.S.C. 4631) (cease-and-desist proceedings), 1372 (12 U.S.C. 4632) (temporary cease-and-desist orders), and 1376 (12 U.S.C. 4636) (civil money penalties) of the Act.

§ 1701.8 Deposit in fund.

OFHEO shall deposit any annual assessment collected under this part in the Federal Housing Enterprise Oversight Fund established in the Treasury of the United States.

PART 1702—IMPLEMENTATION OF THE PRIVACY ACT OF 1974

Sec.

- 1702.1 Scope.
- 1702.2 Definitions.
- 1702.3 Requests for access to individual records.
- 1702.4 Decision to grant or deny requests for access to individual records.
- 1702.5 Special procedures for medical records.
- 1702.6 Requirements for verification of identity.
- 1702.7 Requests for amendment of individual records.
- 1702.8 Decision to grant or deny requests for amendment of individual records.
- 1702.9 Appeals of the initial decision to deny access to or amendment of individual records.
- 1702.10 Decision to grant or deny appeals.
- 1702.11 Disclosure of individual records to other persons or agencies.
- 1702.12 Accounting of disclosures.
- 1702.13 Requests for accounting of disclosures.
- 1702.14 Fees.
- 1702.15 Preservation of records.
- 1702.16 Rights of parents and legal guardians.
- 1702.17 Penalties.

AUTHORITY: 5 U.S.C. 552a, 12 U.S.C. 4513(b).

SOURCE: 63 FR 8844, Feb. 23, 1998, unless otherwise noted. Redesignated at 65 FR 81327, Dec. 26, 2000.

§ 1702.1 Scope.

(a) This part 1702 sets forth the procedures by which an individual may request access to records about him/her that are maintained by the Office of Federal Housing Enterprise Oversight

(OFHEO) in a designated system of records, amendment of such records, or an accounting of disclosures of such records. This part 1702 implements the provisions of the Privacy Act of 1974, as amended (Privacy Act) (5 U.S.C. 552a).

(b) A request from an individual for a record about that individual that is not contained in an OFHEO designated system of records will be considered to be a Freedom of Information Act (FOIA) (5 U.S.C. 552) request and will be processed under the FOIA.

[63 FR 8844, Feb. 23, 1998. Redesignated and amended at 65 FR 81327, Dec. 26, 2000]

§ 1702.2 Definitions.

For the purposes of this part 1702—

Amendment means any correction of, addition to, or deletion from a record.

Designated system of records means a system of records that OFHEO has listed and summarized in the FEDERAL REGISTER pursuant to the requirements of 5 U.S.C. 552a(e).

Individual means a natural person who is either a citizen of the United States of America or an alien lawfully admitted for permanent residence.

Maintain includes collect, use, disseminate, or control.

Privacy Act Appeals Officer means the OFHEO employee who has been delegated the authority to determine Privacy Act appeals.

Privacy Act Officer means the OFHEO employee who has been delegated the authority to determine Privacy Act requests.

Record means any item, collection, or grouping of information about an individual that is maintained by OFHEO and that contains his/her name, or the identifying number, symbol, or other identifying particular assigned to the individual.

Routine use, with respect to disclosure of a record, means the use of such record for a purpose that is compatible with the purpose for which it was created.

Statistical Record means a record in a system of records maintained only for statistical research or reporting purposes and not used, in whole or in part, in making any determination about an identifiable individual, except as provided by 13 U.S.C. 8.

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System of records means a group of records under the control of OFHEO from which information is retrieved by the name of the individual or some identifying number, symbol, or other identifying particular assigned to the individual.

[63 FR 8844, Feb. 23, 1998. Redesignated and amended at 65 FR 81327, Dec. 26, 2000]

§ 1702.3 Requests for access to individual records.

(a) Any individual may request records about him/her that are maintained by OFHEO.

(b) The procedures for submitting requests are as follows:

(1) If the records are contained in a governmentwide system of records of the U.S. Office of Personnel Management (OPM), the request must be submitted as prescribed by the regulations of OPM (5 CFR part 297).

(2) If the records are contained in a record in a system of records of another Federal agency, the request must be submitted as prescribed in the FEDERAL REGISTER Privacy Act notice for the specific governmentwide system.

(3) If the records are contained in a system of records of OFHEO, the request must be submitted in writing to the Privacy Act Officer, Office of Federal Housing Enterprise Oversight, 1700 G Street, NW., Fourth Floor, Washington, DC 20552. The written request should describe the records sought and identify the designated systems of records in which such records may be contained. (A copy of the designated systems of records published by OFHEO in the FEDERAL REGISTER is available upon request from the Privacy Act Officer.) No individual shall be required to state a reason or otherwise justify a request for access to records about him/her.

§ 1702.4 Decision to grant or deny requests for access to individual records.

(a) *Basis for the decision.* The Privacy Act Officer shall grant access to records upon receipt of a request submitted under § 1702.3(b)(3), unless the records—

(1) Were compiled in reasonable anticipation of a civil action or proceeding; or

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(2) Require special procedures for medical records provided for in § 1702.5.

(b) *Notification procedures.* (1) Within 20 business days of receipt of a request submitted under § 1702.3(b)(3), the Privacy Act Officer shall send a written acknowledgment of receipt to the requesting individual.

(2) As soon as reasonably possible, normally within 20 business days following receipt of the request, the Privacy Act Officer shall send a written notification that informs the individual whether the requested records exist and, if the requested records exist, whether access is granted or denied, in whole or in part.

(c) *Access procedures.* If access is granted, in whole or in part, the Privacy Act Officer shall provide the individual with a reasonable period of time to inspect the records at OFHEO during normal business hours or shall mail a copy of the requested records to the individual.

(d) *Denial procedures.* If access is denied, in whole or in part, the Privacy Act Officer shall inform the individual of the reasons for the denial and of the right to appeal the denial, as set forth in § 1702.9.

[63 FR 8844, Feb. 23, 1998. Redesignated and amended at 65 FR 81327, Dec. 26, 2000]

§ 1702.5 Special procedures for medical records.

The Privacy Act Officer shall grant access to medical records to the requesting individual to whom the medical records pertain. However, if, in the judgment of OFHEO, such direct access may have an adverse effect on that individual, the Privacy Act Officer shall transmit the medical records to a licensed medical doctor named by the individual.

§ 1702.6 Requirements for verification of identity.

(a) *Written requests submitted in person.* Any individual who submits in person a written request under this part, may be required to present two forms of identification, such as an employment identification card, driver's license, passport, or other document

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typically used for identification purposes. One of the two forms of identification must contain the individual's photograph and signature.

(b) *Other written requests.* Any individual who submits, other than in person, a written request under this part may be required to provide either one or both of the following:

(1) Minimal identifying information, such as full name, date and place of birth, or other personal information.

(2) At the election of the individual, either a certification of a duly commissioned notary public of any State or territory or the District of Columbia attesting to the requesting individual's identity or an unsworn declaration subscribed to as true under penalty of perjury under the laws of the United States of America.

§ 1702.7 Requests for amendment of individual records.

(a) *Procedures for requesting amendment of a record.* Any individual may request amendment of any record about him/her that the individual believes is not accurate, relevant, timely, or complete. To request amendment, the individual must submit a written request to the Privacy Act Officer, Office of Federal Housing Enterprise Oversight, 1700 G Street, NW., Fourth Floor, Washington, DC 20552. The request should include—

(1) The reason for requesting the amendment;

(2) A description of the record, or portion thereof, including the name of the appropriate designated system of records, sufficient to enable the Privacy Act Officer to identify the particular record or portion thereof; and

(3) If available, a copy of the record, or portion thereof, on which the specific portion requested to be amended is noted.

(b) *Requirement for identifying information.* The Privacy Act Officer may require the individual making the request for amendment to provide the identifying information specified in § 1702.6.

[63 FR 8844, Feb. 23, 1998. Redesignated and amended at 65 FR 81327, Dec. 26, 2000]

§ 1702.8 Decision to grant or deny requests for amendment of individual records.

(a) *Notification procedures.* Within 10 business days following receipt of a request for amendment of records, the Privacy Act Officer shall send a written acknowledgment of receipt to the requesting individual. As soon as reasonably possible, normally within 30 business days from the receipt of the request for amendment, the Privacy Act Officer shall send a written notification to the individual that informs him/her of the decision to grant or deny, in whole or in part, the request for amendment.

(b) *Amendment procedures.* If the request is granted, in whole or in part, the requested amendment shall be made to the subject record. A copy of the amended record shall be provided to all prior recipients of the subject record in accordance with § 1702.12(b).

(c) *Denial procedures.* If the request is denied, in whole or in part, the Privacy Act Officer shall include in the written notification the reasons for the denial and an explanation of the right to appeal the denial, as set forth in § 1702.9.

[63 FR 8844, Feb. 23, 1998. Redesignated and amended at 65 FR 81327, Dec. 26, 2000]

§ 1702.9 Appeals of the initial decision to deny access to or amendment of individual records.

Any individual may appeal the initial denial, in whole or in part, of a request for access to or amendment of his/her record. To appeal, the individual must submit a written appeal, within 30 business days following receipt of written notification of denial, to the Privacy Act Appeals Officer, Office of Federal Housing Enterprise Oversight, 1700 G Street, NW., Fourth Floor, Washington, DC 20552. Both the envelope and the appeal request should be marked "Privacy Act Appeal." The appeal should include—

(a) The information specified for requests for access in § 1702.3(b)(3) or for requests for amendment in § 1702.7, as appropriate;

(b) A copy of the initial denial notice; and

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(c) Any other relevant information for consideration by the Privacy Act Appeals Officer.

[63 FR 8844, Feb. 23, 1998. Redesignated and amended at 65 FR 81327, Dec. 26, 2000]

§ 1702.10 Decision to grant or deny appeals.

(a) *Notification of decision.* Within 30 business days following receipt of the appeal, the Privacy Act Appeals Officer shall send a written notification of the decision to grant or deny to the individual making the appeal. The Privacy Act Appeals Officer may extend the 30-day notification period for good cause. If the time period is extended, the Privacy Act Appeals Officer shall inform in writing the individual making the appeal of the reason for the extension and the expected date of the final decision.

(b) *Appeal granted.* If the appeal for access is granted, in whole or in part, the Privacy Act Appeals Officer shall provide the individual with reasonable time to inspect the requested records at OFHEO during normal business hours or mail a copy of the requested records to the individual. If the appeal for amendment is granted, in whole or in part, the requested amendment shall be made. A copy of the amended record shall be provided to all prior recipients of the subject record in accordance with § 1702.12(b).

(c) *Appeal denied.* If the Privacy Act Appeals Officer denies, in whole or in part, the appeal for access or amendment, he/she shall include in the written notification of the reasons for the denial an explanation of the right to seek judicial review of the final decision, and, with respect to an appeal for amendment, the right to submit a statement of disagreement under paragraph (d) of this section.

(d) *Statements of disagreement and explanation.* (1) Upon receipt of a decision to deny, in whole or in part, the appeal for amendment of records, the individual may file a statement with the Privacy Act Appeals Officer that sets forth his/her reasons for disagreeing with the decision. The Privacy Act Appeals Officer shall attach the statement of disagreement to the record that is the subject of the request for amendment. In response to the state-

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ment of disagreement, the Privacy Act Appeals Officer has the discretion to prepare a statement that explains why the requested amendment was not made. If prepared, the statement of explanation shall be attached to the subject record and a copy of the statement provided to the individual who filed the statement of disagreement.

(2) The Privacy Act Appeals Officer shall provide a copy of any statement of disagreement, and may provide any statement of explanation, to prior recipients of the subject record in accordance with § 1702.12(b).

(e) *Right to judicial review.* If OFHEO does not comply with the notification procedures under paragraph (a) of this § 1720.10 with respect to an appeal for amendment of records, the appealing individual may bring a civil action against OFHEO in the appropriate district court of the United States, as provided for under 5 U.S.C. 552a(g)(1)(A) and 552a(g)(5) before receiving the written notification of the decision.

[63 FR 8844, Feb. 23, 1998. Redesignated and amended at 65 FR 81327, Dec. 26, 2000]

§ 1702.11 Disclosure of individual records to other persons or agencies.

(a) OFHEO may disclose a record to a person or agency other than the individual about whom the record pertains only under one or more of the following circumstances:

(1) If requested and authorized in writing by the individual.

(2) With the prior written consent of the individual.

(3) If such disclosure is required under the Freedom of Information Act.

(4) For a routine use, as defined in § 1702.2, with respect to a designated system of records as described by OFHEO in its notice of systems of records published in the FEDERAL REGISTER.

(5) Pursuant to the order of a court of competent jurisdiction.

(6) To the following persons or agencies—

(i) Officers and employees of OFHEO who have a need for the record in the performance of their duties;

(ii) The Bureau of the Census for purposes of planning or carrying out a census or survey or related activity pursuant to the provisions of title 13 of the United States Code;

(iii) A recipient who has provided OFHEO with advance, adequate written assurance that the record will be used solely as a statistical research or reporting record, and the record is to be transferred in a form that is not individually identifiable;

(iv) The National Archives and Records Administration as a record which has sufficient historical or other value to warrant its continued preservation by the U.S. Government, or for evaluation by the Archivist of the United States to determine whether the record has such value;

(v) An agency or an instrumentality of any governmental jurisdiction within or under the control of the United States for a civil or criminal law enforcement activity if the activity is authorized by law, and if the head of the agency or instrumentality has made a written request to OFHEO specifying the particular portion of the record desired and the law enforcement activity for which the record is sought;

(vi) A person pursuant to a showing of compelling circumstances affecting the health or safety of an individual if, concurrently with such disclosure, notification is transmitted to the last known address of the individual to whom the record pertains;

(vii) Either House of Congress, or, to the extent of matter within its jurisdiction, any committee or subcommittee thereof, any joint committee of Congress, or subcommittee of any such joint committee;

(viii) The Comptroller General, or any of his/her authorized representatives, in the course of the performance of the duties of the General Accounting Office; or

(ix) A consumer reporting agency in accordance with 31 U.S.C. 3711(e).

(b) Before a record is disclosed to other persons or agencies under paragraph (a) (1) or (2) of this section, the identifying information specified in § 1702.6 may be required.

[63 FR 8844, Feb. 23, 1998. Redesignated and amended at 65 FR 81327, Dec. 26, 2000]

§ 1702.12 Accounting of disclosures.

(a) OFHEO shall keep an accurate accounting of the date, nature, and purpose of each disclosure of a record, and the name and address of each person or agency to whom a disclosure was made under § 1702.11, except for disclosures made under § 1702.11(a)(3) or (a)(6)(i). OFHEO shall retain such accounting for at least 5 years or the life of the record, whichever is longer, after the disclosure for which the accounting was made.

(b) When a record has been amended, in whole or in part, or when a statement of disagreement has been filed, a copy of the amended record and any statement of disagreement must be provided, and any statement of explanation may be provided, to all prior and subsequent recipients of the affected record whose identities can be determined pursuant to the disclosure accountings required under paragraph (a) of this section.

[63 FR 8844, Feb. 23, 1998. Redesignated and amended at 65 FR 81327, Dec. 26, 2000]

§ 1702.13 Requests for accounting of disclosures.

(a) Any individual may request an accounting of disclosures of records about him/her for which an accounting is required to be maintained under § 1702.12(a) by submitting a written request to the Privacy Act Officer, Office of Federal Housing Enterprise Oversight, 1700 G Street, NW., Fourth Floor, Washington, DC 20552. Before processing the request, the Privacy Act Officer may require that the individual provide the identifying information specified under § 1702.6.

(b) The Privacy Act Officer shall make available the accounting of disclosures required to be maintained under § 1702.12, except for an accounting made under § 1702.11(a)(6)(v).

[63 FR 8844, Feb. 23, 1998. Redesignated and amended at 65 FR 81327, Dec. 26, 2000]

§ 1702.14 Fees.

OFHEO shall not charge any fees for providing a copy of any records, pursuant to a request for access under this part.

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§ 1702.15 Preservation of records.

OFHEO shall preserve all correspondence relating to the written requests it receives and all records processed pursuant to such requests under this part, in accordance with the records retention provisions of General Records Schedule 14, Informational Services Records. OFHEO shall not destroy records that are subject to a pending request for access, amendment, appeal, or lawsuit pursuant to the Privacy Act.

§ 1702.16 Rights of parents and legal guardians.

For purposes of this part, a parent of any minor or the legal guardian of any individual who has been declared to be incompetent due to physical or mental incapacity or age by a court of competent jurisdiction may act on behalf of the individual.

§ 1702.17 Penalties.

The Privacy Act (5 U.S.C. 552a(i)(3)) makes it a misdemeanor, subject to a maximum fine of \$5,000, to knowingly and willfully request or obtain any record concerning an individual from OFHEO under false pretenses.

PART 1703—RELEASE OF INFORMATION

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AUTHORITY: 5 U.S.C. 301, 552; 12 U.S.C. 4513, 4522, 4526, 4639; E.O. 12600, 3 CFR, 1987 Comp., p. 235.

SOURCE: 63 FR 71005, Dec. 23, 1998, unless otherwise noted. Redesignated at 65 FR 81327, Dec. 26, 2000.

Subpart A—General Definitions

§ 1703.1 Scope.

Definitions in §1703.2 relate to the meaning of terms used throughout part 1703.

[63 FR 71005, Dec. 23, 1998. Redesignated and amended at 65 FR 81327, Dec. 26, 2000]

§ 1703.2 General definitions.

For the purpose of this part:

(a) *Appeals Officer* means the person designated by the Director to process appeals of denials of requests for OFHEO records under the FOIA.

(b) *Director* means the Director of OFHEO or his or her designee.

(c) *Document* means any record or paper, including but not limited to a report, credit review, audit, examination, letter, telegram, memorandum, study, calendar and diary entry, log,

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graph, pamphlet, note, chart, tabulation, analysis, statistical or information accumulation, any record of meetings and conversations, film impression, magnetic tape, or any electronic media, disk, film, or mechanical reproduction that is generated, obtained, or adopted by OFHEO in connection with the conduct of its official business.

(d) *Employee* means any officer, former officer, employee, or former employee of OFHEO; any conservator appointed by OFHEO; or any agent or independent contractor acting on behalf of OFHEO, even though the appointment or contract has terminated.

(e) *FOIA* means the Freedom of Information Act.

(f) *FOIA Officer* means the person designated to process requests for OFHEO records under the FOIA.

(g) *Official* means concerning the authorized business of OFHEO.

(h) *OFHEO* means the Office of Federal Housing Enterprise Oversight.

(i) *Person* means any individual, or any agency, corporation, partnership, trust, association, joint venture, pool, syndicate, sole proprietorship, unincorporated organization, or any other form of entity not specifically listed herein, but does not include OFHEO or any employee.

(j) *Record* means any document, regardless of form or format, which is created or obtained by OFHEO and which is under OFHEO control at the time of an FOIA request.

(k) *Requester* means any person seeking access to OFHEO records under the FOIA.

[63 FR 71005, Dec. 23, 1998, as amended at 65 FR 55171, Sept. 13, 2000]

Subpart B—Documents and Information Generally

§ 1703.6 General rule.

Except as authorized by this part or as otherwise necessary in performing official duties, no employee shall in any manner disclose or permit disclosure of any document or information in the possession of OFHEO that is confidential or otherwise of a nonpublic nature, including that regarding OFHEO or the Federal National Mortgage Association (Fannie Mae) or the

Federal Home Loan Mortgage Corporation (Freddie Mac) (collectively, the Enterprises).

§ 1703.7 Applicability.

(a) *General*. The FOIA and the regulations in this part apply to all OFHEO documents and information. However, if another law sets specific procedure for disclosure, OFHEO will process a request in accordance with the procedures that apply to those specific documents. If a request is received for disclosure of a document to the public which is not required to be released under those provisions, OFHEO will consider the request under the FOIA and the regulations in this part.

(b) *The relationship between the FOIA and the Privacy Act of 1974*. The Privacy Act of 1974 (Privacy Act), 5 U.S.C. 552a, applies to records that are about individuals, but only if the records are in a system of records as defined in the Privacy Act. Requests from individuals for records about themselves which are contained in an OFHEO system of records will be processed under the provisions of the Privacy Act as well as the FOIA. OFHEO will not deny access by a first party to a record under the FOIA or the Privacy Act unless the record is not available to that individual under both the Privacy Act and the FOIA.

(c) *Records available through routine distribution procedures*. When the record requested includes material published and offered for sale, *e.g.*, by the Superintendent of Documents or the Government Printing Office, or which is available to the public through an established distribution system (such as that of the National Technical Information Service of the Department of Commerce), or material offered on OFHEO's web site (<http://www.ofheo.gov>), OFHEO will first refer the requester to those sources. Nevertheless, if the requester is not satisfied with the alternative sources, OFHEO will process the request under the FOIA.

[63 FR 71005, Dec. 23, 1998, as amended at 65 FR 55171, Sept. 13, 2000]

§ 1703.8 OFHEO examination reports.

(a) *General*. Reports of examinations prepared by OFHEO may be disclosed

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only in accordance with this part or with the prior written consent of the Director. No person, agency, or authority, or director, officer, employee, or agent thereof, shall disclose any such report or information contained therein in any manner except as authorized in accordance with this subpart. The report of examination is the property of OFHEO and any unauthorized use or disclosure of such report may be subject to the penalties provided in 18 U.S.C. 641.

(b) *Enterprises.* The Director makes available to each Enterprise a copy of OFHEO's report of examination of such Enterprise. The report of examination is the property of OFHEO and is provided to the Enterprise for its confidential use only. Under no circumstance shall the Enterprise or any director, officer, employee, or agent thereof, make public or disclose in any manner the report of examination or any portion of the contents thereof to any person or organization not officially connected with the Enterprise as director, officer, employee, attorney, auditor, or independent auditor. Any other disclosure or use of this report except as expressly permitted by the Director may be subject to the penalties of 18 U.S.C. 641.

(c) *Government agencies.* The Director may make available reports of examination for the confidential use of Federal agencies responsible for investigating or enforcing applicable Federal laws.

§ 1703.9 Orders and agreements available to the public.

(a) *General.* OFHEO shall make the following documents available to the public:

(1) Any written agreement or other written statement for which a violation may be redressed by the Director or any modification to or termination thereof, unless the Director, in the Director's discretion, determines that public disclosure would be contrary to the public interest.

(2) Any order that is issued with respect to any administrative enforcement proceeding initiated by the Director under 12 U.S.C. 4631 through 4641 that has become final in accordance with 12 U.S.C. 4633 and 12 U.S.C. 4634.

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(3) Any modification to or termination of any final order made public pursuant to this section.

(b) *Delay of public disclosure under exceptional circumstances.* If the Director makes a determination in writing that the public disclosure of any final order pursuant to paragraph (a) of this section would seriously threaten the financial health or security of the Enterprise, the Director may delay the public disclosure of such order for a reasonable time.

(c) *Documents filed under seal in public enforcement hearings.* The Director may file any document or part thereof under seal in any hearing commenced by the Director if the Director determines in writing that disclosure thereof would be contrary to the public interest.

(d) *Retention of documents.* The Director shall keep and maintain a record, for not less than 6 years, of all documents described in paragraph (a) of this section and all enforcement agreements and other supervisory actions and supporting documents issued with respect to or in connection with any enforcement proceedings initiated by the Director under 12 U.S.C. 4631 through 4641.

(e) *Disclosure to Congress.* This section may not be construed to authorize the withholding of any information from, or to prohibit the disclosure of any information to, the Congress or any committee or subcommittee thereof.

Subpart C—Availability of Records of OFHEO

§ 1703.11 Official records of OFHEO.

(a) OFHEO shall, upon a written request for records that reasonably describes the information or records and is made in accordance with the provisions of this subpart, make the records available as promptly as practicable to any person for inspection and/or copying, except as provided in paragraph (b) of this section. OFHEO may charge a fee determined in accordance with subpart D of this part. OFHEO will make the record available in the form or format requested if the record is readily reproducible in that form or format

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with reasonable effort. “Readily reproducible” means, with respect to electronic format, that the requested record or records can be downloaded or transferred intact to a computer disk, tape, or other electronic medium using equipment currently in use by OFHEO.

(b) *Records not available.* Except as otherwise provided in this part, or as may be specifically authorized by the Director, the following information and records, or portions thereof, are not available to requesters:

(1) Any record, or portion thereof, that is—

(i) Specifically authorized under criteria established by an Executive order to be kept secret in the interest of national defense or foreign policy, and

(ii) Is in fact properly classified pursuant to such Executive order.

(2) Any record, or portion thereof, related solely to the internal personnel rules and practices of OFHEO.

(3) Any record, or portion thereof that is specifically exempted from disclosure by statute (other than 5 U.S.C. 552b), provided that such statute—

(i) Requires that the matters be withheld from the public in such a manner as to leave no discretion on the issue, or

(ii) Establishes particular criteria for withholding or refers to particular types of matters to be withheld.

(4) Any matter that is a trade secret or that constitutes commercial or financial information obtained from a person and that is privileged or confidential.

(5) Any matter contained in inter-agency or intra-agency memoranda or letters that would not be available by law to a private party in litigation with OFHEO.

(6) Any information contained in personnel and medical files and similar files (including financial files) the disclosure of which would constitute a clearly unwarranted invasion of personal privacy.

(7) Any records or information compiled for law enforcement purposes, but only to the extent that the production of such law enforcement records or information—

(i) Could reasonably be expected to interfere with enforcement proceedings;

(ii) Would deprive a person of a right to fair trial or an impartial adjudication;

(iii) Could reasonably be expected to constitute an unwarranted invasion of personal privacy;

(iv) Could reasonably be expected to disclose the identity of a confidential source, including a State, local, or foreign agency or authority or any private institution or an Enterprise regulated and examined by OFHEO that furnished information on a confidential basis, and, in the case of a record of information compiled by a criminal law enforcement authority in the course of a criminal investigation or by an agency conducting a lawful national security intelligence investigation, information furnished by a confidential source;

(v) Would disclose techniques and procedures for law enforcement investigations or prosecutions, or would disclose guidelines for law enforcement investigations or prosecutions if such disclosure could reasonably be expected to risk circumvention of the law; or

(vi) Could reasonably be expected to endanger the life or physical safety of any individual.

(8) Any matter that is contained in or related to examination, operating, or condition reports that are prepared by, on behalf of, or for the use of OFHEO.

(9) Any geological and geophysical information and data, including maps, concerning wells.

(c) Even if an exemption described in paragraph (b) of this section may be reasonably applicable to a requested record, or portion thereof, OFHEO may elect under the circumstances of any particular request not to apply the exemption to such requested record, or portion thereof. The fact that the exemption is not applied by OFHEO to any requested record, or portion thereof, has no precedential significance as to the application or nonapplication of the exemption to any other requested record, or portion thereof, no matter when the request is received.

(d) Any reasonably segregable portion of a record shall be provided to any person properly requesting such record after deletion of the portions

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which are exempt under this subpart. The amount of the information deleted shall be indicated on the released portion of the record, unless including that indication would harm an interest protected by the exemption in paragraph (b) of this section pursuant to which the deletion is made. If technically feasible, the amount of the information deleted shall be indicated at the place in the record where the deletion is made.

(e) This section does not authorize withholding of information or limit the availability of records to the public, except as specifically stated in this section. This section is not authority to withhold information from Congress.

[65 FR 55171, Sept. 13, 2000]

§ 1703.12 Publicly available records.

(a) The records described in this paragraph are available for public inspection and copying, for a fee determined in accordance with subpart D of this part, at OFHEO's offices located at 1700 G Street, NW., Fourth Floor, Washington, DC 20552. Records created on or after November 1, 1996, and current indexes to all records described in paragraphs (a)(1), (a)(2), (a)(3), and (a)(4) of this section, including those created before November 1, 1996, are available electronically at <http://www.ofheo.gov/docs/>. The publicly available records include—

(1) Any final opinions issued by OFHEO, as well as orders made in adjudication of cases as set forth in §1703.9 of subpart B of this part;

(2) Any statements of policy and interpretation that have been adopted by OFHEO and have not been published in the FEDERAL REGISTER;

(3) Any OFHEO administrative staff manuals and instructions to staff that affect a member of the public, and that are not exempt from disclosure under the Freedom of Information Act;

(4) Copies of all records released pursuant to this subpart that OFHEO determines have become or are likely to become the subject of subsequent requests for substantially the same records; and

(5) Current indexes to the records described in this paragraph.

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(b) To the extent necessary to prevent an invasion of personal privacy, the Director may delete identifying details from a record described in paragraph (a) of this section. In each case of such deletion, the justification will be clearly explained in writing and the extent of such deletion indicated (at the place in the record where the deletion is made if technically feasible), unless including that indication would harm an interest protected by the exemption in §1703.11(b) pursuant to which the deletion is made.

[65 FR 55172, Sept. 13, 2000. Redesignated and amended at 65 FR 81327, Dec. 26, 2000]

§ 1703.13 Requests for records.

(a) *Addressing requests.* Requests for records in the possession of OFHEO shall be made in writing but may be submitted by regular mail, electronic mail, or facsimile. If the request is sent by regular mail, the request shall be addressed to FOIA Officer, Office of Federal Housing Enterprise Oversight, 1700 G Street NW., Fourth Floor, Washington, DC 20552, with both the envelope and the letter marked “FOIA Request.” Electronic mail requests shall be addressed to foia_office@ofheo.gov, with “FOIA Request” in the subject line. Requests submitted by fax shall be sent to FOIA Officer at (202) 414-8917 and shall be clearly marked “FOIA Request.” All requests shall include the requester's name, address, and telephone number. An improperly addressed request will be deemed not to have been received for purposes of the 20-day time period set forth in §1703.17(a) of this subpart until it is received, or would have been received with the exercise of due diligence, by the FOIA Officer. Records requested in conformance with this subpart that are not exempt records may be obtained in person, by regular mail, or by electronic mail, as specified in the request, provided the records are readily reproducible in the requested form or format with reasonable effort. Records to be obtained in person will be available for inspection or copying during business hours on a regular business day in the office of OFHEO.

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(b) *Description of records.* Each request must reasonably describe the desired records in sufficient detail to enable OFHEO personnel to locate the records with a reasonable amount of effort. A request for a specific category of records will be regarded as fulfilling this requirement if it enables responsive records to be identified by a technique or process that is not unreasonably burdensome or disruptive of OFHEO operations.

(1) Whenever possible, a request should include specific information about each record sought, such as the date, title or name, author, recipient, and subject matter of the record.

(2) If the FOIA Officer determines that a request does not reasonably describe the records sought, he or she will either advise the requester what additional information is needed to locate the record or otherwise state why the request is insufficient. The FOIA Officer will also extend to the requester an opportunity to confer with OFHEO personnel with the objective of reformulating the request in a manner which will meet the requirements of this section.

[63 FR 71005, Dec. 23, 1998, as amended at 65 FR 55172, Sept. 13, 2000. Redesignated and amended at 65 FR 81327, Dec. 26, 2000]

§ 1703.14 Responses to requests.

(a) *Response to initial request.* The FOIA Officer of OFHEO is authorized to grant or deny any request for a record and to determine appropriate fees.

(b) *Referral to another agency.* When a requester seeks records that originated in another Federal Government agency, OFHEO will refer the request to the other agency for response. If OFHEO refers the request to another agency, it will notify the requester of the referral. A request for any records classified by some other agency will be referred to that agency for response.

(c) *Creating records.* If a person seeks information from OFHEO in a format that does not currently exist, OFHEO will make reasonable efforts to provide the information in the format requested. OFHEO is not required to create a new record of information to satisfy a request.

(d) *No responsive record.* If no records are responsive to the request, the FOIA Officer will so notify the requester in writing.

[63 FR 71005, Dec. 23, 1998, as amended at 65 FR 55173, Sept. 13, 2000]

§ 1703.15 Form and content of responses.

(a) *Form of notice granting a request.* After the FOIA Officer has granted a request in whole or in part, the requester will be notified in writing. The notice shall describe the manner in which the record will be disclosed, whether by providing a copy of the record with the response or at a later date, or by making a copy of the record available to the requester for inspection at a reasonable time and place. The procedure for such an inspection may not unreasonably disrupt the operation of OFHEO. The response letter will also inform the requester of any fees to be charged in accordance with the provisions of subpart D of this part.

(b) *Form of notice denying a request.* When the FOIA Officer denies a request in whole or in part, he or she will so notify the requester in writing. The response will be signed by the FOIA Officer and will include—

(1) The name and title or position of the person making the denial;

(2) An estimate of the volume of any requested matter that is withheld, unless providing the estimate would harm an interest protected by the exemption in § 1703.11(b) pursuant to which the denial was made;

(3) A brief statement of the reason or reasons for the denial, including the FOIA exemption or exemptions which the FOIA Officer has relied upon in denying the request; and

(4) A statement that the denial may be appealed under § 1703.16 of this subpart and a description of the requirements of that section.

[63 FR 71005, Dec. 23, 1998, as amended at 65 FR 55173, Sept. 13, 2000. Redesignated and amended at 65 FR 81327, Dec. 26, 2000]

§ 1703.16 Appeals of denials.

(a) *Right of appeal.* If a request, including a request for expedited processing, has been denied in whole or in part, the requester may appeal the denial to: FOIA Appeals Officer, Office of

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Federal Housing Enterprise Oversight, 1700 G Street, NW, Fourth Floor, Washington DC 20552. Electronic appeals shall be submitted to foia_appeals_office@ofheo.gov with “FOIA Appeal” in the subject line.

(b) *Letter of appeal.* The appeal must be in writing and submitted within 30 days of receipt of the denial letter. The appeal shall be submitted in the manner described in § 1703.13, except that it shall be clearly marked “FOIA Appeal” instead of “FOIA Request.” An appeal shall include a copy of the initial request, a copy of the letter denying the request in whole or in part, and a statement of the circumstances, reasons, or arguments advanced in support of disclosure of the requested record. An improperly addressed appeal shall be deemed not to have been received for the purposes of the 20-day time period set forth in § 1703.17(b) until it is received, or would have been received with the exercise of due diligence, by the Appeals Officer.

(c) *Action on appeal.* The disposition of an appeal will be in writing and will constitute the final action of OFHEO on a request. A decision affirming in whole or in part the denial of a request will include a brief statement of the reason or reasons for affirmance, including each FOIA exemption relied on. If the denial of a request is reversed in whole or in part on appeal, the request will be processed promptly in accordance with the decision on appeal.

(d) *Judicial review.* If the denial of the request for records is upheld in whole or in part, or, if a determination on the appeal has not been mailed at the end of the 20-day period or the last extension thereof, the requester is deemed to have exhausted his or her administrative remedies, giving rise to a right of judicial review under 5 U.S.C. 552(a)(4). However, a requester’s refusal of OFHEO’s offer of an opportunity to limit the scope of the request or arrange an alternate time frame for processing the request shall be considered as a factor in determining whether “exceptional circumstances” exist, which permits a court in which a requester has sought judicial review, to

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grant a stay to allow OFHEO to complete its review of the records.

[63 FR 71005, Dec. 23, 1998, as amended at 65 FR 55173, Sept. 13, 2000. Redesignated and amended at 65 FR 81327, Dec. 26, 2000]

§ 1703.17 Time limits.

(a) *Initial request.* Following receipt of a request for records, the FOIA Officer will determine whether to comply with the request and will notify the requester in writing of his or her determination within 20 days (excluding Saturdays, Sundays, and legal holidays) after receipt of the request.

(b) *Appeal.* A written determination on an appeal submitted in accordance with § 1703.16 of this subpart will be issued within 20 days (excluding Saturdays, Sundays, and legal holidays) after receipt of the appeal. However, determination of an appeal of a denial of expedited processing will be issued as expeditiously as practicable. When a determination cannot be mailed within the applicable time limit, the appeal will nevertheless be processed. In such case, upon the expiration of the time limit, the requester will be informed of the reason for the delay, of the date on which a determination may be expected to be mailed, and of that person’s right to seek judicial review. The requester may be asked to forego judicial review until determination of the appeal.

(c) *Extension of time limits.* The time limits specified in either paragraph (a) or (b) of this section may be extended in unusual circumstances after written notice to the requester setting forth the reasons for the extension and the date on which a determination is expected to be made. If the date specified for the extension is more than 10 days after the initial time allowed for response, OFHEO will provide the requester an opportunity to limit the scope of the request or arrange for an alternate time frame for processing the request. As used in this paragraph, *unusual circumstances* means that there is a need to—

(1) Search for and collect the requested records from facilities that are separate from the office processing the request;

(2) Search for, collect, and appropriately examine a voluminous amount

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of separate and distinct records which are demanded in a single request; or

(3) Consult with another agency having a substantial interest in the determination of the request, or consult with various offices within OFHEO that have a substantial interest in the records requested.

(d) *Related requests.* OFHEO may aggregate multiple requests involving clearly related matters made by a single requester, or a group of requesters acting in concert, if OFHEO reasonably believes that such requests actually constitute a single request that would qualify as an “unusual circumstance.”

(e) *Expedited processing.* (1) Upon a demonstration of compelling need by the requester, OFHEO will grant a request for expedited processing of a FOIA request. If a request for expedited processing is granted, OFHEO will give the request priority and process it as soon as practicable.

(2) To show a compelling need for expedited processing, the requester shall provide a statement demonstrating that:

(i) The failure to obtain the requested records could reasonably be expected to pose an imminent threat to the life or physical safety of an individual; or

(ii) The requester’s main professional occupation or activity is information dissemination and there is a particular urgency to inform the public of government activity involved in the request beyond the public’s right to know about government activity generally.

(3) The requester’s statement of compelling need must be certified to be true and correct to the best of his or her knowledge and belief and must explain in detail the basis for requesting expedited processing. The formality of the certification required to obtain expedited treatment may be waived by OFHEO in its discretion.

(4) A requester seeking expedited processing will be notified within ten (10) working days of the receipt of the request whether expedited processing has been granted. If the request for expedited processing is denied, OFHEO will act on any appeal expeditiously.

[65 FR 55173, Sept. 13, 2000. Redesignated and amended at 65 FR 81327, Dec. 26, 2000]

§ 1703.18 Special procedures for business information.

(a) *In general.* Business information provided to OFHEO by a business submitter shall not be disclosed pursuant to an FOIA request except in accordance with this section.

(b) *Definitions.* For the purpose of this section, the following definitions shall apply:

(1) *Business information* means trade secrets or other commercial or financial information, provided to OFHEO by a submitter, which arguably is protected from disclosure under §1703.11(b)(4), because disclosure could reasonably be expected to cause substantial competitive harm.

(2) *Business submitter* means any person or entity which provides business information, directly or indirectly, to OFHEO and who has a proprietary interest in the information.

(c) *Designation of business information.* Submitters of business information should use good-faith efforts to designate, by appropriate markings, either at the time of submission or at a reasonable time thereafter, those portions of their submissions which they deem to be protected under §1703.11(b)(4). Any such designation will expire 10 years after the records were submitted to the Government, unless the submitter requests, and provides reasonable justification for, a designation period of longer duration.

(d) *Predisclosure notification.* (1) Except as is provided for in paragraph (i) of this section, the FOIA Officer shall, to the extent permitted by law, provide a submitter with prompt written notice of an FOIA request or administrative appeal encompassing its business information whenever required under paragraph (e) of this section. Such notice shall either describe the exact nature of the business information requested or provide copies of the records or portions thereof containing the business information.

(2) Whenever the FOIA Officer provides a business submitter with the notice set forth in paragraph (e)(1) of this section, the FOIA Officer shall notify the requester that the request includes information that may arguably be exempt from disclosure under

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§ 1703.11(b)(4) and that the person or entity who submitted the information to OFHEO has been given the opportunity to comment on the proposed disclosure of information.

(e) *When notice is required.* OFHEO shall provide a business submitter with notice of a request whenever—

(1) The business submitter has in good faith designated the information as business information deemed protected from disclosure under § 1703.11(b)(4); or

(2) OFHEO has reason to believe that the request seeks business information the disclosure of which may result in substantial commercial or financial injury to the business submitter.

(f) *Opportunity to object to disclosure.* Through the notice described in paragraph (d) of this section, OFHEO shall, to the extent permitted by law, afford a business submitter at least 10 days (excluding Saturdays, Sundays, and legal holidays) within which it can provide OFHEO with a detailed written statement of any objection to disclosure. Such statement shall demonstrate why the information is contended to be a trade secret or commercial or financial information that is privileged or confidential and why disclosure would cause competitive harm. Whenever possible, the business submitter's claim of confidentiality should be supported by a statement or certification by an officer or authorized representative of the business submitter. Information provided by a submitter pursuant to this paragraph may itself be subject to disclosure under the FOIA.

(g) *Notice of intent to disclose.* (1) The FOIA Officer shall consider carefully a business submitter's objections and specific grounds for nondisclosure prior to determining whether to disclose business information. Whenever the FOIA Officer decides to disclose business information over the objection of a business submitter, the FOIA Officer shall forward to the business submitter a written notice at least 10 days (excluding Saturdays, Sundays, and legal holidays) before the date of disclosure containing—

(i) A statement of the reasons for which the business submitter's disclosure objections were not sustained,

(ii) A description of the business information to be disclosed, and

(iii) A specified disclosure date.

(2) Such notice of intent to disclose likewise shall be forwarded to the requester at least 10 days (excluding Saturdays, Sundays, and legal holidays) prior to the specified disclosure date.

(h) *Notice of FOIA lawsuit.* Whenever a requester brings suit seeking to compel disclosure of business information, the FOIA Officer shall promptly notify the business submitter of such action.

(i) *Exceptions to predisclosure notification.* The requirements of this section shall not apply if—

(1) The FOIA Officer determines that the information should not be disclosed;

(2) The information lawfully has been published or has been officially made available to the public;

(3) Disclosure of the information is required by law (other than the Freedom of Information Act); or

(4) The designation made by the submitter in accordance with paragraph (c) of this section appears obviously frivolous; except that, in such a case, the FOIA Officer will provide the submitter with written notice of any final decision to disclose business information within a reasonable number of days prior to a specified disclosure date.

[63 FR 71005, Dec. 23, 1998, as amended at 65 FR 55173, Sept. 13, 2000. Redesignated and amended at 65 FR 81327, Dec. 26, 2000]

Subpart D—Fees for Provision of Information

§ 1703.21 Definitions.

For the purpose of this subpart, the following definitions shall apply:

(a) *Commercial use request* means a request for information that is from, or on behalf of, a requester seeking information for a use or purpose that furthers the commercial, trade, or profit interests of the requester or the person on whose behalf the request is being made. To determine whether a request is properly classified as a commercial use request, OFHEO shall determine the purpose for which the requested records shall be used. If OFHEO has reasonable cause to doubt the purpose

specified in the request for which a requester will use the records sought, or where the purpose is not clear from the request itself, OFHEO shall seek additional clarification before assigning the request to a specified category.

(b) *Direct costs* means the expenditures actually incurred by OFHEO in searching for and reproducing records to respond to a request for information. In the case of a commercial use request, the term also means those expenditures OFHEO actually incurs in reviewing records to respond to the request. The direct costs shall include the cost of the time of the employee performing the work, determined in accordance with § 1703.22(b)(1)(i), the cost of any computer searches, determined in accordance with § 1703.22(b)(1)(ii), and the cost of operating duplication equipment. Not included in direct costs are overhead expenses such as costs of space, and heating or lighting the facility in which the records are stored. Direct costs also include the costs incurred by OFHEO for any contract services that may be needed to respond to a request.

(c) *Educational institution* means a preschool, a public or private elementary or secondary school, an institution of undergraduate higher education, an institution of graduate higher education, an institution of professional education, and an institution of vocational education, which operates a program or programs of scholarly research.

(d) *Noncommercial scientific institution* refers to an institution that is not operated on a commercial, trade, or profit basis and which is operated solely for the purpose of conducting scientific research, the results of which are not intended to promote any particular product or industry.

(e) *Representative of the news media* means any person actively gathering news for an entity that is organized and operated to publish or broadcast news to the public. The term “news” means information that is about current events or that would be of current interest to the public. Examples of news media entities include television or radio stations broadcasting to the public at large and publishers of periodicals (but only in those instances in

which the periodicals can qualify as disseminators of “news”) who make their products available for purchase or subscription by the general public. These examples are not intended to be all-inclusive. As traditional methods of news delivery evolve, *e.g.*, electronic dissemination of newspapers through telecommunication services, such alternative media, would be included in this category. “Freelance” journalists may be regarded as working for a news organization if they can demonstrate a solid basis for expecting publication through that organization even though they are not actually employed by the organization. A publication contract would be the clearest proof that a journalist is working for a news organization, but OFHEO may look to the requester’s past publication record to determine whether a journalist is working for a news organization.

(f) *Reproduce and reproduction* means the process of making a copy of a record necessary to respond to a request for information. Such copies take the form of paper copy, microfilm, audio-visual materials, or machine-readable documentation, *e.g.*, magnetic tape or disk. The copy provided shall be in the form or format requested, provided the record is readily reproducible in that form or format with reasonable effort, and shall be in a form reasonably usable by the requesters.

(g) *Review* means the process of examining records located in response to a request for information to determine whether any portion of any record located is permitted to be withheld. It also includes processing any records for disclosure, *e.g.*, doing all that is necessary to prepare the records for release. The term “review” does not include the time spent resolving general legal or policy issues regarding the application of exemptions. OFHEO shall only charge fees for reviewing records in response to a commercial use request.

(h) The term *search* includes all time spent looking for material that is responsive to a request for information, including page-by-page or line-by-line identification of material within records. The term “search” includes the extraction of information from a computer using existing programming.

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Searching for materials shall be done in the most efficient and least expensive manner so as to minimize the costs of OFHEO and the requester. For example, a line-by-line search for responsive material should not be performed when merely reproducing an entire document would be less expensive and the faster method of complying with the request for information. A “search” for material that is responsive to a request should be distinguished from a “review” of material to determine whether the material is exempt from disclosure.

[63 FR 71005, Dec. 23, 1998, as amended at 65 FR 55174, Sept. 13, 2000. Redesignated and amended at 65 FR 81327, Dec. 26, 2000]

§ 1703.22 Fees to be charged—general.

(a) Generally, the fees charged for requests for records pursuant to the Freedom of Information Act will cover the full allowable direct costs of searching for, reproducing, and reviewing records that are responsive to a request for information. Fees will be assessed according to the schedule contained in paragraph (b) of this section and the category of requesters described in §1703.23 of this subpart for services rendered by OFHEO staff in responding to, and processing requests for, records under this part. Fees assessed shall be paid by check or money order payable to the Office of Federal Housing Enterprise Oversight.

(b) *Types of charges.* The types of charges that may be assessed in connection with the production of records in response to a FOIA request are as follows:

(1) *Searches.* (i) *Manual searches for records.* OFHEO will charge for actual search time, billed in 15-minute segments, at a rate determined by whether the employee performing the work is classified as clerical, professional, or executive. The hourly fee for each classification is based on the average of the actual compensation (salary and benefits) of employees in the classification and is adjusted periodically to reflect significant changes in the average compensation of the class. The “executive” classification includes the senior management of OFHEO, *i.e.* Director, Deputy Director, Associate Directors and Deputy Associate Directors. The

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“clerical” classification includes employees performing primarily secretarial, clerical, or ministerial tasks. The “professional” classification includes all positions not classified as “executive” or “clerical.” A current fee schedule is available on electronically at <http://www.ofheo.gov/docs/> or by regular mail.

(ii) *Computer searches for records.* Requesters will be charged at the actual direct costs of conducting a search using existing programming. These direct costs will include the cost of operating the computer equipment for that portion of operating time that is directly attributable to searching for records and the cost of the time of the employee performing the work, determined as described in paragraph (b)(1)(i) of this section. A charge will also be made for any substantial amounts of special supplies or materials used to contain, present, or make available the output of computers, based upon the prevailing levels of costs to OFHEO for the type and amount of such supplies of materials that are used. Nothing in this paragraph shall be construed to entitle any person or entity, as of right, to any services in connection with computerized records, other than services to which such person or entity may be entitled under the provisions of this subpart.

(iii) *Unproductive searches.* OFHEO may charge search fees even if no records are found that are responsive to the request or if the records found are exempt from disclosure.

(2) *Reproduction.* Records will be photocopied at a rate of \$.15 per page. For copies prepared by computer, such as tapes or printouts, the requester will be charged the actual cost, including operator time, of production of the tape or printout. For other methods of reproduction, the actual direct costs of reproducing the record(s) will be charged.

(3) *Review.* Only requesters who are seeking records for commercial use may be charged for time spent reviewing records to determine whether they are exempt from mandatory disclosure. Charges may be assessed only for initial review, *i.e.*, the review undertaken

the first time OFHEO analyzes the applicability of a specific exemption to a particular record or portion of a record. Records or portions of records withheld in full under an exemption that is subsequently determined not to apply may be reviewed again to determine the applicability of other exemptions not previously considered. The costs for such a review are properly assessable.

(4) *Other services and materials.* Where OFHEO elects, as a matter of administrative discretion, to comply with a request for a special service or materials, such as certifying that records are true copies or sending records by special methods, the actual direct costs of providing the service or materials will be charged.

[65 FR 55174, Sept. 13, 2000. Redesignated and amended at 65 FR 81327, Dec. 26, 2000]

§ 1703.23 Fees to be charged—categories of requesters.

(a) *Fees for various requester categories.* Paragraphs (b) through (e) of this section state, for each category of requester, the types of fees generally charged by OFHEO. However, for each of these categories, the fees may be limited, waived or reduced in accordance with the provisions set forth in paragraph (c) of § 1703.24. If OFHEO has reasonable cause to doubt the purpose specified in the request for which a requester will use the records sought, or where the purpose is not clear from the request itself, OFHEO will seek clarification before assigning the request a specific category.

(b) *Commercial use requester.* OFHEO shall charge fees for records requested by persons or entities making a commercial use request in an amount that equals the full direct costs for searching for, reviewing for release, and reproducing the records sought. Commercial use requesters are not entitled to 2 hours of free search time nor 100 free pages of reproduction of records. In accordance with § 1703.22, commercial use requesters may be charged the costs of searching for and reviewing records even if there is ultimately no disclosure of records.

(c) *Educational and noncommercial scientific institutions.* OFHEO shall charge fees for records requested by, or on be-

half of, educational institutions and noncommercial scientific institutions in an amount which equals the cost of reproducing the records responsive to the request, excluding the cost of reproducing the first 100 pages. No search fee shall be charged with respect to requests by educational and noncommercial scientific institutions. For a request to be included in this category, requesters must show that the request being made is authorized by and under the auspices of a qualifying institution, and that the records are not sought for commercial use but are sought in furtherance of scholarly research (if the request is from an educational institution) or scientific research (if the request is from a noncommercial scientific institution).

(d) *News media.* OFHEO shall charge fees for records requested by representatives of the news media in an amount which equals the cost of reproducing the records responsive to the request, excluding the costs of reproducing the first 100 pages. No search fee shall be charged with respect to requests by representatives of the news media. For a request to be included in this category, the requester must qualify as a representative of the news media and the request must not be made for a commercial use. A request for records supporting the news dissemination function of the requester shall not be considered to be a request that is for commercial use.

(e) *All other requesters.* OFHEO shall charge fees for records requested by persons or entities that are not classified in any of the categories listed in paragraphs (b), (c), or (d) of this section in an amount that equals the full reasonable direct cost of searching for and reproducing records that are responsive to the request, excluding the first 2 hours of search time and the cost of reproducing the first 100 pages of records. In accordance with § 1703.22, requesters in this category may be charged the cost of searching for records even if there is ultimately no disclosure of records, excluding the first 2 hours of search time.

(f) For purposes of the exceptions contained in this section on assessment of fees, the word “pages” refers to paper copies of 8½ × 11 or 11 × 14. Thus,

requesters are not entitled to 100 microfiche or 100 computer disks, for example. A microfiche containing the equivalent of 100 pages or a computer disk containing the equivalent of 100 pages of computer printout meets the terms of the exception.

(g) For purposes of paragraph (e) of this section, the term “search time” has as its basis, manual search. To apply this term to searches made by computer, OFHEO will determine the hourly cost of operating the computer equipment and the operator’s time determined as described in paragraph (b)(1)(i) of §1703.22. When the cost of the search (including the operator’s time and the cost of operating the computer equipment to process a request) equals the equivalent dollar amount of two hours of the time of the person performing the work, *i.e.*, the operator, OFHEO will begin assessing charges for the computer.

[63 FR 71005, Dec. 23, 1998, as amended at 65 FR 55174, Sept. 13, 2000. Redesignated and amended at 65 FR 81327, Dec. 26, 2000]

§ 1703.24 Limitations on charging fees.

(a) *In general.* Except for requesters seeking records for a commercial use as described in paragraph (b) of §1703.23, OFHEO will provide, without charge, the first 100 pages of duplication and the first 2 hours of search time, or their cost equivalent.

(b) *No fee charged.* OFHEO will not charge fees to any requester, including commercial use requesters, if the cost of collecting a fee would be equal to or greater than the fee itself. The elements to be considered in determining the “cost of collecting a fee” are the administrative costs of receiving and recording a requester’s remittance and of processing the fee.

(c) *Waiver or reduction of fees.* OFHEO may grant a waiver or reduction of fees if OFHEO determines that the disclosure of the information is in the public interest because it is likely to contribute significantly to public understanding of the operations or activities of the Federal Government, and the disclosure of the information is not primarily in the commercial interest of the requester. Requests for a waiver or reduction of fees will be considered on a case-by-case basis.

(1) The following factors will be considered by OFHEO in determining whether a waiver or reduction of fees is in the public interest:

(i) *The subject of the request: Whether the subject of the requested records concerns “the operations or activities of the Government.”* The subject matter of the requested records, in the context of the request, must specifically concern identifiable operations or activities of the Federal Government with a connection that is direct and clear, not remote or attenuated. Furthermore, the records must be sought for their informative value with respect to those Government operations or activities; a request for access to records for their intrinsic informational content alone will not satisfy this threshold consideration.

(ii) *The informative value of the information to be disclosed: Whether the disclosure is “likely to contribute” to an understanding of Government operations or activities.* The disclosable portions of the requested records must be meaningfully informative on specific Government operations or activities in order to hold potential for contributing to increased public understanding of those operations and activities. The disclosure of information that is already in the public domain, in either a duplicative or substantially identical form, would not be likely to contribute to such understanding, as nothing new would be added to the public record.

(iii) *The contribution to an understanding of the subject by the general public: Whether disclosure of the requested information will contribute to the “public understanding.”* The disclosure must contribute to the understanding of the public at large, as opposed to the individual understanding of the requester or a narrow segment of interested persons. A requester’s identity and qualifications, *e.g.*, expertise in the subject area and ability and intention to convey information to the general public, will be considered.

(iv) *The significance of the contribution in public understanding: Whether the disclosure is likely to “significantly enhance” the public understanding of Government operations or activities.* The public’s understanding of the subject matter in question, as compared to the

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level of public understanding existing prior to the disclosure, must be likely to be enhanced by the disclosure to a significant extent. The FOIA Officer shall not make a separate value judgment as to whether information, even though it in fact would contribute significantly to public understanding of the operations or activities of the Government, is “important” enough to be made public.

(2) In order to determine whether the second fee waiver requirement is met, *i.e.*, that disclosure of the requested information is not primarily in the commercial interest of the requester, OFHEO shall consider the following two factors in sequence:

(i) *The existence and magnitude of a commercial interest: Whether the requester, or any person on whose behalf the requester may be acting, has a commercial interest that would be furthered by the requested disclosure.* In assessing the magnitude of identified commercial interests, consideration will be given to the effect that the information disclosed would have on those commercial interests, as well as to the extent to which FOIA disclosures serve those interests overall. Requesters shall be given a reasonable opportunity in the administrative process to provide information bearing upon this consideration.

(ii) *The primary interest in disclosure: Whether the magnitude of the identified commercial interest of the requester is sufficiently large in comparison with the public interest in disclosure, that disclosure is “primarily in the commercial interest of the requester.”* A fee waiver or reduction is warranted only where, once the “public interest” standard set out in paragraph (c)(1) of this section is satisfied, that public interest can fairly be regarded as greater in magnitude than that of the requester’s commercial interest in disclosure. OFHEO will ordinarily presume that, where a news media requester has satisfied the public interest standard, the public interest will be serviced primarily by disclosure to that requester. Disclosure to requesters who compile and market Federal Government information for direct economic return will not be presumed to primarily serve the “public interest.”

(3) Where only a portion of the requested record satisfies the requirements for a waiver or reduction of fees under this paragraph, a waiver or reduction shall be granted only as to that portion.

(4) A request for a waiver or reduction of fees must accompany the request for disclosure of records and should include—

(i) A clear statement of the requester’s interest in the records;

(ii) The proposed use of the records and whether the requester will derive income or other benefit from such use;

(iii) A statement of how the public will benefit from release of the requested records; and

(iv) If specialized use of the documents is contemplated, a statement of the requester’s qualifications that are relevant to the specialized use.

(5) A requester may appeal the denial of a request for a waiver or reduction of fees in accordance with the provisions of §1703.16.

[63 FR 71005, Dec. 23, 1998. Redesignated and amended at 65 FR 81327, Dec. 26, 2000]

§ 1703.25 Miscellaneous fee provisions.

(a) *Notice of anticipated fees in excess of \$25.00.* Where OFHEO determines or estimates that the fees chargeable will amount to more than \$25.00, OFHEO shall promptly notify the requester of the actual or estimated amount of fees or such portion thereof that can be readily estimated, unless the requester has indicated his or her willingness to pay fees as high as those anticipated. Where a requester has been notified that the actual or estimated fees may exceed \$25.00, the request will be deemed not to have been received until the requester has agreed to pay the anticipated total fee. A notice to the requester pursuant to this paragraph will include the opportunity to confer with OFHEO personnel in order to reformulate the request to meet the requester’s needs at a lower cost.

(b) *Aggregating requests.* A requester may not file multiple requests at the same time, each seeking portions of a record or records, solely in order to avoid the payment of fees. When OFHEO reasonably believes that a requester, or a group of requesters acting

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in concert, is attempting to break a request into a series of requests for the purpose of evading the assessment of fees, OFHEO may aggregate such requests and charge accordingly. One element to be considered in determining whether a belief would be reasonable is the time period over which the requests have occurred. OFHEO will presume that multiple requests of this type made within a 30-day period have been made in order to evade fees. Where requests are separated by a longer period, OFHEO shall aggregate them only where there exists a solid basis for determining that such aggregation is warranted, *e.g.*, where the requests involve clearly related matters. Multiple requests regarding unrelated matters will not be aggregated.

(c) *Advance payment of fees.* (1) OFHEO does not require an advance payment before work is commenced or continued, unless—

(i) OFHEO estimates or determines that the fees are likely to exceed \$250.00. If it appears that the fees will exceed \$250.00, OFHEO will notify the requester of the likely cost and obtain satisfactory assurance of full payment where the requester has a history of prompt payment of FOIA fees. In the case of requesters with no history of payment, OFHEO may require an advance payment of fees in an amount up to the full estimated charge that will be incurred; or

(ii) The requester has previously failed to pay a fee in a timely fashion, *i.e.*, within 30 days of the date of a billing. In such cases, OFHEO may require the requester to pay the full amount owed plus any applicable interest, as provided in paragraph (d) of this section, or demonstrate that the fee owed has been paid, prior to processing any further record request. Under these circumstances, OFHEO may require the requester to make an advance payment of the full amount of the fees anticipated before processing a new request or finishing processing of a pending request from that requester.

(2) A request for an advance deposit shall include an offer to the requester to confer with identified OFHEO personnel to attempt to reformulate the request in a manner which will meet

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the needs of the requester at a lower cost.

(3) When OFHEO requests an advance payment of fees, the administrative time limits described in 5 U.S.C. 552(a)(6) begin only after OFHEO has received the advance payment.

(d) *Interest.* OFHEO may assess interest charges on an unpaid bill starting on the 31st day following the day on which the bill was sent. Once a fee payment has been received by OFHEO, even if not processed, the accrual of interest shall be stayed. Interest charges shall be assessed at the rate prescribed in 31 U.S.C. 3717 and shall accrue from the date of the billing.

Subpart E—Testimony and Production of Documents in Legal Proceedings in Which OFHEO Is Not a Named Party

§ 1703.31 General purposes.

The purposes of this subpart are to maintain the confidentiality of official documents and information of OFHEO, conserve the time of employees for their official duties, maintain the impartial position of OFHEO in litigation in which OFHEO is not a named party, and enable the Director to determine when to authorize testimony and to produce documents in legal proceedings in which OFHEO is not a named party. This subpart sets forth the procedures to be followed with respect to testimony concerning official matters and production of official documents of OFHEO in legal proceedings in which OFHEO is not a named party. This subpart in no way affects the rights and procedures governing public access to official documents pursuant to the FOIA or the Privacy Act.

§ 1703.32 Definitions.

For the purpose of this subpart:

(a) *Court* means any entity conducting a legal proceeding.

(b) *Demand* means any order, subpoena, or other legal process for testimony or documents.

(c) *Legal proceeding* means any administrative, civil, or criminal proceeding, including a discovery proceeding therein, before a court of law, administrative board or commission,

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hearing officer, or other body in which OFHEO is not a named party or in which OFHEO has not instituted the administrative investigation or administrative hearing.

(d) *OFHEO Counsel* means the General Counsel or his or her designee, a Department of Justice attorney, or counsel authorized by OFHEO to act on behalf of OFHEO or an employee.

§ 1703.33 General policy.

It is the policy of OFHEO that in any legal proceeding in which OFHEO is not a named party, no employee shall, in response to a demand, produce any documents contained in the files of OFHEO, or disclose any information relating to, or based upon, documents contained in the files of OFHEO, or disclose or produce any documents acquired as part of the performance of that employee's official duties or because of that employee's official status. Under appropriate circumstances, the Director may grant exceptions in writing to this policy when the Director determines that the testimony of employees or disclosure of official documents would be in the best interest of OFHEO or in the public interest. Prior to any authorized testimony or release of official documents, the requesting party shall obtain a protective order from the court before which the action is pending to preserve the confidentiality of the testimony or documents subsequently produced. The protective order shall be in a form satisfactory to OFHEO.

§ 1703.34 Request for testimony or production of documents.

(a) No employee shall give testimony concerning official matters or produce any official documents in any legal proceeding to which OFHEO is not a named party without the prior written authorization of the Director.

(b) If testimony by an employee concerning official matters or the production of official documents is desired, the requesting party, or his or her attorney, shall submit a letter to the Director setting forth the title of the case, the forum, the requesting party's interest in the case, a summary of the issues in the litigation, the reasons for the request, and a showing that the de-

sired testimony, documents, or information are not reasonably available from any other source. If an appearance or testimony is requested, the letter shall also set forth the intended use of the testimony, a general summary of the scope of the testimony requested, and a showing that no document could be provided and used in lieu of the testimony or other appearance requested.

(c) The General Counsel is authorized to consult with the requesting party or his or her attorney to refine and limit the request so that compliance is less burdensome, or obtain information necessary to make the determination described in § 1703.33 of this subpart. Failure of the requesting party, or his or her attorney, to cooperate in good faith with the General Counsel to enable the Director to make an informed determination under this subpart may serve as the basis for a determination not to comply with the request.

[63 FR 71005, Dec. 23, 1998. Redesignated and amended at 65 FR 81327, Dec. 26, 2000]

§ 1703.35 Scope of permissible testimony.

(a) The scope of permissible testimony by an employee is limited to that set forth in the written authorization granted that employee by the Director.

(b) Employees are not authorized to give opinion testimony, except as authorized by the Director. OFHEO, as the regulatory agency charged with the responsibility of examining, supervising, and regulating the financial safety and soundness and capital adequacy of the Enterprises under the Federal Housing Enterprises Financial Safety and Soundness Act of 1992, 12 U.S.C. 4501 *et seq.*, relies on the ability of its employees to gather full and complete information in order to carry out its statutory responsibilities. The use of employees to give opinion testimony would hamper OFHEO's ability to carry out its statutory responsibilities and would cause a serious administrative burden on OFHEO's staff.

§ 1703.36 Manner in which testimony is given.

(a) Authorized testimony of employees ordinarily will be made available only through depositions or written interrogatories.

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(b) Where, in response to a request, the Director determines that circumstances warrant authorizing testimony by an employee, the requesting party shall cause a subpoena to be served on the employee in accordance with applicable Federal or State rules of procedure, with a copy of the subpoena sent by registered or certified mail to the General Counsel.

(c) Normally, authorized depositions will be taken at OFHEO's office, at a time arranged with the employee that is reasonably fixed to avoid substantial interference with the performance of the employee's duties.

(d) Upon completion of the deposition of an employee, a copy of the transcript of the testimony shall be furnished, at the expense of the party requesting the deposition, to the General Counsel for OFHEO's files.

§ 1703.37 Manner in which documents will be produced.

(a) An employee's authorization to produce official documents is limited to the authority granted that employee by the Director.

(b) Certified or authenticated copies of official OFHEO documents authorized by the Director to be released under this subpart will be provided upon request.

§ 1703.38 Fees.

Unless waived or reduced, the following fees shall be charged for documents produced by OFHEO in connection with requests subject to this subpart:

(a) *Searches for documents.* OFHEO will charge for the actual search time of the employee performing the work, billed in 15-minute segments, as described in §1703.22(b)(1)(i).

(b) *Copying of documents.* The standard copying charge for documents in paper copy is \$.15 per page. When responsive information is provided in a format other than paper copy, such as in the form of computer tapes and disks, OFHEO will assess the direct costs of the tape, disk, or whatever medium is used to produce the information, as well as any related reproduction costs. Normally, only one copy will be provided. Additional copies will

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be provided only upon a showing of demonstrated need.

(c) *Certification or authentication of documents.* OFHEO will charge \$3.00 for each certification or authentication of documents.

(d) *Computer searches.* Services of personnel in the nature of a computer search shall be charged at rates prescribed in paragraph (a) of this section. A charge shall be made for the computer time involved, based upon the prevailing level of costs to OFHEO and upon the particular types of computer and associated equipment and the amount of time that such equipment is utilized. A charge shall also be made for any substantial amount of special supplies or documents used to contain, present, or make available the output of computers, based upon prevailing levels of costs to OFHEO and upon the type and amount of such supplies or documents that are used.

(e) *Other costs.* When other services and documents not specifically identified in this section are requested and provided, their actual cost to OFHEO shall be charged.

(f) *Payments of fees.* A bill will be forwarded to the requesting party upon completion of the production. Payment shall be made by check or money order payable to the Office of Federal Housing Enterprise Oversight.

[63 FR 71005, Dec. 23, 1998, as amended at 65 FR 55175, Sept. 13, 2000. Redesignated and amended at 65 FR 81327, Dec. 26, 2000]

§ 1703.39 Responses to demands served on employees.

(a) *Advice by employee served.* Any employee who is served with a demand in a legal proceeding requiring his or her personal attendance as a witness or requiring the production of documents or information in any proceeding, shall immediately notify the General Counsel of such service, of the testimony and documents described in the demand, and of all relevant facts which may be of assistance to the General Counsel in determining whether the individual in question should be authorized to testify or the documents requested should be made available.

(b) When authorization to testify or to produce documents has not been

granted by the Director, OFHEO Counsel shall provide the party issuing the demand or the court with a copy of the regulations contained in this subpart and shall inform the party issuing the demand or the court that the employee upon whom the demand has been made is prohibited from testifying or producing documents without the prior approval of the Director.

(c) *Appearance by employee served.* Unless OFHEO has authorized disclosure of the information requested, any employee who has OFHEO information that may not be disclosed and who is required to respond to a subpoena or other legal process, shall attend at the time and place required and respectfully decline to disclose or to give any testimony with respect to the information, basing such refusal upon the provisions of this subpart. If the court nevertheless orders the disclosure of the information or the giving of testimony irrespective of instructions from the Director not to produce the documents or disclose the information sought, the employee upon whom the demand has been made shall continue to decline respectfully to disclose the information and shall report promptly the facts to OFHEO for such action as OFHEO may deem appropriate.

(d) A determination under this subpart to comply or not to comply with any demand shall not constitute an assertion or waiver of privilege, lack of relevance, technical deficiencies, or any other ground for noncompliance. OFHEO reserves the right to oppose any demand on any legal ground independent of its determination under this subpart.

§ 1703.40 Responses to demands served on nonemployees.

(a) OFHEO reports of examinations, or any documents related thereto, are the property of OFHEO and are not to be disclosed to any person without the Director's prior written consent.

(b) If any person who has possession of an OFHEO report of examination, or any documents related thereto, is served with a demand in a legal proceeding directing that person to produce such OFHEO documents or to testify with respect thereto, such person shall immediately notify the Gen-

eral Counsel of such service, of the testimony and described documents in the demand, and of all relevant facts. Such person shall also object to the production of such documents or information contained therein on the basis that the documents are the property of OFHEO and cannot be released without OFHEO's consent and that their production must be sought from OFHEO following the procedures set forth in § 1703.33, paragraphs (b) and (c) of § 1703.34, and paragraph (b) of § 1703.37 of this subpart.

[63 FR 71005, Dec. 23, 1998. Redesignated and amended at 65 FR 81328, Dec. 26, 2000]

Subpart F—Rules and Procedures for Service Upon OFHEO

§ 1703.51 Service of process.

(a) Except as otherwise provided by OFHEO regulations, the Federal Rules of Civil Procedure, or order of a court with jurisdiction over OFHEO, any legal process upon OFHEO, including a legal process served on OFHEO demanding access to its records under the FOIA, shall be duly issued and served upon the General Counsel and any OFHEO personnel named in the caption of the documents.

(b) Service of process upon the General Counsel may be effected by personally delivering a copy of the documents to the General Counsel or by sending a copy of the documents to the General Counsel by registered or certified mail, postage prepaid, to the Office of Federal Housing Enterprise Oversight, 1700 G Street, NW., Fourth Floor, Washington, DC 20552.

PART 1704—DEBT COLLECTION

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AUTHORITY: 5 U.S.C. 5514; 26 U.S.C. 6402(d); 31 U.S.C. 3701–3720A.

SOURCE: 64 FR 34969, June 30, 1999, unless otherwise noted. Redesignated at 65 FR 81328, Dec. 26, 2000.

Subpart A—General

§ 1704.1 Authority and scope.

(a) *Authority.* The Office of Federal Housing Enterprise Oversight (OFHEO) issues this part 1704 under the authority of 5 U.S.C. 5514 and 31 U.S.C. 3701–3720A, and in conformity with the FCCS at 4 CFR chapter II; the regulations on salary offset issued by the Office of Personnel Management at 5 CFR

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part 550, subpart K; and the regulations on tax refund offset issued by the Internal Revenue Service at 26 CFR 301.6402–6.

(b) *Scope.* (1) This part 1704 applies to debts that are owed to the Federal Government by Federal employees, other persons, organizations, or entities that are indebted to OFHEO, and by Federal employees of OFHEO who are indebted to other agencies, except for those debts listed in paragraph (b)(2) of this section.

(2) Subparts B and C of this part 1704 do not apply to:

(i) Debts or claims arising under the Internal Revenue Code (26 U.S.C. 1 *et seq.*) or the tariff laws of the United States;

(ii) Any case to which the Contract Disputes Act (41 U.S.C. 601 *et seq.*) applies;

(iii) Any case where collection of a debt is explicitly provided for or provided by another statute, *e.g.* travel advances under 5 U.S.C. 5705 and employee training expenses under 5 U.S.C. 4108, or, as provided for by title 11 of the United States Code, when the claims involve bankruptcy;

(iv) Any debt based in whole or in part on conduct in violation of the antitrust laws or involving fraud, the presentation of a false claim, or misrepresentation on the part of the debtor or any party having an interest in the claim, unless the Department of Justice authorizes OFHEO to handle the collection;

(v) Claims between agencies; or

(vi) A claim that has been outstanding for more than 10 years after the creditor agency's right to collect the debt first accrued, unless facts material to the Federal Government's right to collect were not known and could not reasonably have been known by the officials charged with the responsibility for discovery and collection of such debts.

(3) Nothing in this part 1704 precludes the compromise, suspension, or termination of collection actions, where appropriate under the FCCS, or the use of alternative dispute resolution methods if they are not inconsistent with applicable law and regulations.

(4) Nothing in this part 1704 precludes an employee from requesting waiver of

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an erroneous payment under 5 U.S.C. 5584, 10 U.S.C. 2774, or 32 U.S.C. 716, or from questioning the amount or validity of a debt, in the manner set forth in this part 1704.

[64 FR 34969, June 30, 1999. Redesignated and amended at 65 FR 81328, Dec. 26, 2000]

§ 1704.2 Definitions.

The following definitions apply to the terms used in this part 1704, unless the term is defined elsewhere in this part 1704.

(a) *Administrative offset* means an action, pursuant to 31 U.S.C. 3716, in which the Federal Government withholds funds payable to, or held by the Federal Government for a person, organization, or other entity in order to collect a debt from that person, organization, or other entity. Such funds include funds payable by the Federal Government on behalf of a State Government.

(b) *Agency* means a department, agency, court, court administrative office, or instrumentality in the executive, judicial, or legislative branch of the Federal Government, including government corporations.

(c) *Claim* or *debt* (used interchangeably in this part 1704) means any amount of funds or property that has been determined by an agency official to be due the Federal Government by a person, organization, or entity, except another agency. It also means any amount of money, funds, or property owed by a person to a State, the District of Columbia, American Samoa, Guam, the United States Virgin Islands, the Commonwealth of the Northern Mariana Islands, or the Commonwealth of Puerto Rico. A claim or debt includes:

(1) Funds owed on account of loans made, insured, or guaranteed by the Federal Government, including any deficiency or any difference between the price obtained by the Federal Government in the sale of a property and the amount owed to the Federal Government on a mortgage on the property;

(2) Expenditures of non-appropriated funds;

(3) Overpayments, including payments disallowed by audits performed by the Inspector General of the agency administering the program;

(4) Any amount the Federal Government is authorized by statute to collect for the benefit of any person;

(5) The unpaid share of any non-Federal partner in a program involving a Federal payment, and a matching or cost-sharing payment by the non-Federal partner;

(6) Any fines or penalties assessed by an agency; and

(7) Other amounts of money or property owed to the Federal Government.

(d) *Certification* means a written statement received by a paying agency from a creditor agency that request the paying agency to offset the salary of an employee and specifies that required procedural protections have been afforded the employee.

(e) *Compromise* means the settlement or forgiveness of a debt.

(f) *Creditor agency* means the agency to which the debt is owed, including a debt collection center when acting in behalf of a creditor agency in matters pertaining to the collection of a debt.

(g) *Debt*. See *Claim* or *debt* in paragraph (c) of this section.

(h) *Debt collection center* means the Department of the Treasury or any other agency or division designated by the Secretary of the Treasury with authority to collect debts on behalf of creditor agencies in accordance with 31 U.S.C. 3711(g).

(i) *Debtor* means the person, organization, or entity owing money to the Federal Government.

(j) *Disposable pay* means that part of current basic pay, special pay, incentive pay, retired pay, or retainer pay (or in the case of an employee not entitled to basic pay, other authorized pay) remaining after the deduction of any amount required by law to be withheld (other than deductions to execute garnishment orders in accordance with 5 CFR parts 581 and 582). Among the legally required deductions that OFHEO must apply first to determine disposable pay are levies pursuant to the Internal Revenue Code (title 26, United States Code) and deductions described in 5 CFR 581.105 (b) through (f), as follows:

- (1) Federal employment taxes;
- (2) Amounts withheld for the United States Soldiers' and Airmen's Home;
- (3) Amounts deducted for Medicare;

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(4) Fines and forfeiture ordered by a court-martial or by a commanding officer;

(5) Federal, State, or local income taxes to the extent authorized or required by law, but no greater than would be the case if the employee claimed all dependents to which her or she is entitled and such additional amounts for which the employee presents evidence of a tax obligation supporting the additional withholding;

(6) Health insurance premiums;

(7) Normal retirement contributions, including employee contributions to the Thrift Savings Plan; and

(8) Normal life insurance premiums, *e.g.*, Serviceman's Group Life Insurance and "Basic Life" Federal Employee's Group Life Insurance premiums, not including amounts deducted for supplementary coverage.

(k) *Employee* means a current employee of OFHEO or other agency, including a current member of the Armed Forces or a Reserve of the Armed Forces of the United States.

(l) *FCCS* means the Federal Claims Collection Standards at 4 CFR chapter II.

(m) *Hearing official* means an individual who is responsible for conducting any hearing with respect to the existence or amount of a debt claimed and for rendering a decision on the basis of such hearing. A hearing official may not be under the supervision or control of the Director of OFHEO when OFHEO is the creditor agency but may be an administrative law judge.

(n) *Notice of Intent* means a written notice of a creditor agency to a debtor that states that the debtor owes a debt to the creditor agency and appraises the debtor of the applicable procedural rights.

(o) *Notice of salary offset* means a written notice from the paying agency to an employee after a certification has been issued by a creditor agency that informs the employee that salary offset will begin at the next officially established pay interval.

(p) *Paying agency* means an agency of the Federal Government that employs the individual who owes a debt to an agency of the Federal Government.

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(q) *Salary offset* means an administrative offset to collect a debt under 5 U.S.C. 5514 by deductions at one or more officially established pay intervals from the current pay account of an employee without his or her consent.

(r) *Waiver* means the cancellation, remission, forgiveness, or non-recovery of a debt allegedly owed by an employee to OFHEO or another agency as permitted or required by 5 U.S.C. 5584 or 8346(b), 10 U.S.C. 2774, 32 U.S.C. 716, or any other law.

[64 FR 34969, June 30, 1999. Redesignated and amended at 65 FR 81328, Dec. 26, 2000]

§ 1704.3 Collection of debts and referrals to the Department of the Treasury.

(a) *Collection activity*. The collection of debts directly and by offset shall be pursued in accordance with this part 1704. This part 1704 incorporates all applicable debt collection provisions of the FCCS and supplements the FCCS by the prescription of procedures necessary and appropriate for the operations of OFHEO.

(b) *Referral of delinquent debts*. (1) OFHEO shall transfer to the Secretary of the Department of the Treasury any past due, legally enforceable nontax debt that has been delinquent for a period of 180 days or more so that the Secretary may take appropriate action to collect the debt or terminate collection action in accordance with 31 U.S.C. 3716, 5 U.S.C. 5514, the FCCS, 5 CFR 550.1108, and 31 CFR part 285.

(2) OFHEO may transfer any past due, legally enforceable nontax debt that has been delinquent for less than a period of 180 days to a debt collection center for collection in accordance with 31 U.S.C. 3716, 5 U.S.C. 5514, 5 CFR 550.1108, 31 CFR part 285, and the FCCS.

[64 FR 34969, June 30, 1999. Redesignated and amended at 65 FR 81328, Dec. 26, 2000]

§§ 1704.4-1704.19 [Reserved]

Subpart B—Salary Offset

§ 1704.20 Authority and scope.

(a) *Authority*. OFHEO may collect debts owed by employees to the Federal Government by means of salary offset under the authority of 5 U.S.C.

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5514, 5 CFR part 550, subpart K, and this subpart B.

(b) *Scope.* (1) The procedures set forth in this subpart B apply to situations where OFHEO is attempting to collect a debt by salary offset that is owed to it by an individual employed by OFHEO or by another agency; or where OFHEO employs an individual who owes a debt to another agency.

(2) The procedures set forth in this subpart B do not apply to:

(i) Any routine intra-agency adjustment of pay that is attributable to clerical or administrative error or delay in processing pay documents that have occurred within the four pay periods preceding the adjustment, or any adjustment to collect a debt amounting to \$50 or less. However, at the time of any such adjustment, or as soon thereafter as possible, OFHEO or its designated payroll agent shall provide the employee with a written notice of the nature and the amount of the adjustment and a point of contact for contesting such adjustment.

(ii) Any negative adjustment to pay that arises from an employee's election of coverage or a change in coverage under a Federal benefits program that requires periodic deductions from pay, if the amount to be recovered was accumulated over four pay periods or less. However, at the time the such adjustment is made, OFHEO or its payroll agent shall provide in the employee's earnings statement a clear and concise statement that informs the employee of the previous overpayment.

§ 1704.21 Notice requirements before salary offset where OFHEO is the creditor agency.

(a) *Notice of Intent.* Deductions from an employee's salary may not be made unless OFHEO provides the employee with a Notice of Intent a minimum of 30 calendar days before the salary offset is initiated.

(b) *Contents of Notice of Intent.* The Notice of Intent shall advise the employee of the following:

(1) OFHEO has reviewed the records relating to the claim and has determined that the employee owes the debt;

(2) OFHEO intends to collect the debt by deductions from the employee's current disposable pay account;

(3) The amount of the debt and the facts giving rise to the debt;

(4) The frequency and amount of the intended deduction (stated as a fixed dollar amount or as a percentage of pay not to exceed 15 percent of disposable pay), and the intention to continue the deductions until the debt and all accumulated interest are paid in full or otherwise resolved;

(5) The name, address, and telephone number of the person to whom the employee may propose a written alternative schedule for voluntary repayment, in lieu of salary offset. The employee shall include a justification for the alternative schedule in his or her proposal. If the terms of the alternative schedule are agreed upon by the employee and OFHEO, the alternative written schedule shall be signed by both the employee and OFHEO;

(6) An explanation of OFHEO's policy concerning interest, penalties, and administrative costs, including a statement that such assessments must be made unless excused in accordance with the FCCS;

(7) The employee's right to inspect and copy all records of OFHEO pertaining to his or her debt that are not exempt from disclosure or to receive copies of such records if he or she is unable personally to inspect the records as the result of geographical or other constraints;

(8) The name, address, and telephone number of the OFHEO employee to whom requests for access to records relating to the debt must be sent;

(9) The employee's right to a hearing conducted by an impartial hearing official with respect to the existence and amount of the debt claimed or the repayment schedule *i.e.*, the percentage of disposable pay to be deducted each pay period, so long as a request is filed by the employee as prescribed in § 1704.23; the name and address of the office to which the request for a hearing should be sent; and the name, address, and telephone number of a person whom the employee may contact concerning procedures for requesting a hearing;

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(10) The filing of a request for a hearing on or before the 15th calendar day following receipt of the Notice of Intent will stay the commencement of collection proceedings and a final decision on whether a hearing will be held (if a hearing is requested) will be issued at the earliest practical date;

(11) OFHEO shall initiate certification procedures to implement a salary offset unless the employee files a request for a hearing on or before the 15th calendar day following receipt of the Notice of Intent;

(12) Any knowingly false or frivolous statement, representations, or evidence may subject the employee to:

(i) Disciplinary procedures appropriate under 5 U.S.C. chapter LXXV, 5 CFR part 752, or any other applicable statutes or regulations;

(ii) Penalties under the False Claims Act, 31 U.S.C. 3729-3731, or under any other applicable statutory authority; or

(iii) Criminal penalties under 18 U.S.C. 286, 287, 1001, and 1002, or under any other applicable statutory authority;

(13) Any other rights and remedies available to the employee under statutes or regulations governing the program for which the collection is being made;

(14) Unless there are applicable contractual or statutory provisions to the contrary, amounts paid on or deducted from debts that are later waived or found not to be owed to the Federal Government shall be promptly refunded to the employee; and

(15) Proceedings with respect to the debt are governed by 5 U.S.C. 5514.

[64 FR 34969, June 30, 1999. Redesignated and amended at 65 FR 81328, Dec. 26, 2000]

§ 1704.22 Review of OFHEO records related to the debt.

(a) *Request for review.* An employee who desires to inspect or copy OFHEO records related to a debt owed by the employee to OFHEO must send a letter to the individual designated in the Notice of Intent requesting access to the relevant records. The letter must be received in the office of that individual within 15 calendar days after the employee's receipt of the Notice of Intent.

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(b) *Review location and time.* In response to a timely request submitted by the employee, the employee shall be notified of the location and time when the employee may inspect and copy records related to his or her debt that are not exempt from disclosure. If the employee is unable personally to inspect such records as the result of geographical or other constraints, OFHEO shall arrange to send copies of such records to the employee.

§ 1704.23 Opportunity for a hearing where OFHEO is the creditor agency.

(a) *Request for a hearing—(1) Time-period for submission.* An employee who requests a hearing on the existence or amount of the debt held by OFHEO or on the salary-offset schedule proposed by OFHEO, must send such request to OFHEO. The request for a hearing must be received by OFHEO on or before the 15th calendar day following receipt by the employee of the Notice of Intent.

(2) *Failure to submit timely.* If the employee files a request for a hearing after the expiration of the 15th calendar day, OFHEO may accept the request if the employee can show that the delay was the result of circumstances beyond his or her control or that he or she failed to receive actual notice of the filing deadline.

(3) *Contents of request.* The request for a hearing must be signed by the employee and must fully identify and explain with reasonable specificity all the facts, evidence, and witnesses, if any, that the employee believes support his or her position. The employee must also specify whether he or she requests an oral hearing. If an oral hearing is requested, the employee should explain why a hearing by examination of the documents without an oral hearing would not resolve the matter.

(4) *Failure to request a hearing.* The failure of an employee to request a hearing will be considered an admission by the employee that the debt exists in the amount specified in the Notice of Intent that was provided to the employee under § 1704.21(b).

(b) *Obtaining the services of a hearing official—(1) Debtor is not OFHEO employee.* When the debtor is not an

OFHEO employee and OFHEO cannot provide a prompt and appropriate hearing before an administrative law judge or other hearing official, OFHEO may request a hearing official from an agent of the paying agency, as designated in 5 CFR part 581, appendix A, or as otherwise designated by the paying agency.

(2) *Debtor is OFHEO employee.* When the debtor is an OFHEO employee, OFHEO may contact any agent of another agency, as designated in 5 CFR part 581, appendix A, or as otherwise designated by the agency, to request a hearing official.

(c) *Procedure*—(1) *Notice of hearing.* After the employee requests a hearing, the hearing official shall notify the employee of the form of the hearing to be provided. If the hearing will be oral, the notice shall set forth the date, time, and location of the hearing, which must occur no more than 30 calendar days after the request is received, unless the employee requests that the hearing be delayed. If the hearing will be conducted by an examination of documents, the employee shall be notified within 30 calendar days that he or she should submit evidence and arguments in writing to the hearing official.

(2) *Oral hearing.* (i) An employee who requests an oral hearing shall be provided an oral hearing if the hearing official determines that the matter cannot be resolved by an examination of the documents alone, as for example, when an issue of credibility or veracity is involved. The oral hearing need not be an adversarial adjudication and rules of evidence need not apply. Witnesses who testify in an oral hearing shall do so under oath or affirmation.

(ii) Oral hearings may take the form of, but are not limited to:

(A) Informal conferences with the hearing official in which the employee and agency representative are given full opportunity to present evidence, witnesses, and argument;

(B) Informal meetings in which the hearing examiner interviews the employee; or

(C) Formal written submissions followed by an opportunity for oral presentation.

(3) *Hearing by examination of documents.* If the hearing official determines that an oral hearing is not necessary, he or she shall make the determination based upon an examination of the documents.

(d) *Record.* The hearing official shall maintain a summary record of any hearing conducted under this section.

(e) *Decision.* (1) The hearing official shall issue a written opinion stating his or her decision, based upon all evidence and information developed during the hearing, as soon as practicable after the hearing, but not later than 60 calendar days after the date on which the request was received by OFHEO, unless the hearing was delayed at the request of the employee, in which case the 60-day decision period shall be extended by the number of days by which the hearing was postponed.

(2) The decision of the hearing official shall be final and is considered to be an official certification regarding the existence and the amount of the debt for purposes of executing salary offset under 5 U.S.C. 5514. If the hearing official determines that a debt may not be collected by salary offset, but OFHEO finds that the debt is still valid, OFHEO may seek collection of the debt through other means in accordance with applicable law and regulations.

(f) *Content of decision.* The written decision shall include:

(1) A summary of the facts concerning the origin, nature, and amount of the debt;

(2) The hearing official's findings, analysis, and conclusions; and

(3) The terms of any repayment schedules, if applicable.

(g) *Failure to appear.* If, in the absence of good cause shown, such as illness, the employee or the representative of OFHEO fails to appear, the hearing official shall proceed with the hearing as scheduled, and make his or decision based upon the oral testimony presented and the documentation submitted by both parties. At the request of both parties, the hearing official may schedule a new hearing date. Both parties shall be given reasonable notice

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of the time and place of the new hearing.

[64 FR 34969, June 30, 1999. Redesignated and amended at 65 FR 81328, Dec. 26, 2000]

§ 1704.24 Certification where OFHEO is the creditor agency.

(a) *Issuance.* OFHEO shall issue a certification in all cases where the hearing official determines that a debt exists or the employee admits the existence and amount of the debt, as for example, by failing to request a hearing.

(b) *Contents.* The certification must be in writing and state:

(1) That the employee owes the debt;
(2) The amount and basis of the debt;
(3) The date of the Federal Government's right to collect the debt first accrued;

(4) The date the employee was notified of the debt, the action(s) taken pursuant to OFHEO's regulations, and the dates such actions were taken;

(5) If the collection is to be made by lump-sum payment, the amount and date such payment will be collected;

(6) If the collection is to be made in installments, the amount or percentage of disposable pay to be collected in each installment and, if OFHEO wishes, the desired commencing date of the first installments, if a date other than the next officially established pay period; and

(7) A statement that OFHEO's regulation on salary offset has been approved by the Office of Personnel Management pursuant to 5 CFR part 550, subpart K.

§ 1704.25 Voluntary repayment agreements as alternative to salary offset where OFHEO is the creditor agency.

(a) *Proposed repayment schedule.* In response to a Notice of Intent, an employee may propose to repay the debt voluntarily in lieu of salary offset by submitting a written proposed repayment schedule to OFHEO. Any proposal under this section must be received by OFHEO within 15 calendar days after receipt of the Notice of Intent.

(b) *Notification of decision.* In response to a timely proposal by the employee, OFHEO shall notify the employee whether the employee's proposed repayment schedule is acceptable.

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OFHEO has the discretion to accept, reject, or propose to the employee a modification of the proposed repayment schedule.

(1) If OFHEO decides that the proposed repayment schedule is unacceptable, the employee shall have 15 calendar days from the date he or she received notice of the decision in which to file a request for a hearing.

(2) If OFHEO decides that the proposed repayment schedule is acceptable or the employee agrees to a modification proposed by OFHEO, an agreement shall be put in writing and signed by both the employee and OFHEO.

§ 1704.26 Special review where OFHEO is the creditor agency.

(a) *Request for review.* (1) An employee subject to salary offset or a voluntary repayment agreement may, at any time, request a special review by OFHEO of the amount of the salary offset or voluntary repayment, based on materially changed circumstances, including, but not limited to, catastrophic illness, divorce, death, or disability.

(2) The request for special review must include an alternative proposed offset or payment schedule and a detailed statement, with supporting documents, that shows why the current salary offset or payments result in extreme financial hardship to the employee and his or her spouse and dependents. The detailed statement must indicate:

- (i) Income from all sources;
- (ii) Assets;
- (iii) Liabilities;
- (iv) Number of dependents;
- (v) Expenses for food, housing, clothing, and transportation;
- (vi) Medical expenses; and
- (vii) Exceptional expenses, if any.

(b) *Evaluation of request.* OFHEO shall evaluate the statement and supporting documents and determine whether the original offset or repayment schedule imposes extreme financial hardship on the employee. OFHEO shall notify the employee in writing within 30 calendar days of such determination, including, if appropriate, a revised offset or payment schedule. If the special review results in a revised offset or repayment

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schedule, OFHEO shall provide a new certification to the paying agency.

§ 1704.27 Notice of salary offset where OFHEO is the paying agency.

(a) *Notice.* Upon issuance of a proper certification by OFHEO (for debts owed to OFHEO) or upon receipt of a proper certification from another creditor agency, OFHEO shall send the employee a written notice of salary offset.

(b) *Content of notice.* Such written notice of salary offset shall advise the employee of the:

(1) Certification that has been issued by OFHEO or received from another creditor agency;

(2) Amount of the debt and of the deductions to be made; and

(3) Date and pay period when the salary offset will begin.

(c) If OFHEO is not the creditor agency, OFHEO shall provide a copy of the notice of salary offset to the creditor agency and advise the creditor agency of the dollar amount to be offset and the pay period when the offset will begin.

§ 1704.28 Procedures for salary offset where OFHEO is the paying agency.

(a) *Generally.* OFHEO shall coordinate salary deductions under this section and shall determine the amount of an employee's disposable pay and the amount of the salary offset subject to the requirements in this section. Deductions shall begin the pay period following the issuance of the certification by OFHEO or the receipt by OFHEO of the certification from another agency, or as soon thereafter as possible.

(b) *Types of collection.*—(1) *Lump-sum payment.* If the amount of the debt is equal to or less than 15 percent of the employee's disposable pay, such debt ordinarily will be collected in one lump-sum payment.

(2) *Installment deductions.* Installment deductions will be made over a period not greater than the anticipated period of employment. The size and frequency of installment deductions will bear a reasonable relation to the size of the debt and the employee's ability to pay. However, the amount deducted for any pay period will not exceed 15 percent of the disposable pay from which the deduction is made unless the employee

has agreed in writing to the deduction of a greater amount. The installment payment should normally be sufficient in size and frequency to liquidate the debt in no more than three years. Installment payments of less than \$50 should be accepted only in the most unusual circumstances.

(3) *Lump-sum deductions from final check.* In order to liquidate a debt, a lump-sum deduction exceeding 15 percent of disposable pay may be made pursuant to 31 U.S.C. 3716 from any final salary payment due a former employee, whether the former employee was separated voluntarily or involuntarily.

(4) *Lump-sum deductions from other sources.* Whenever an employee subject to salary offset is separated from OFHEO, and the balance of the debt cannot be liquidated by offset of the final salary check, OFHEO may offset any later payments of any kind to the former employee to collect the balance of the debt pursuant to 31 U.S.C. 3716.

(c) *Multiple debts.* (1) Where two or more creditor agencies are seeking salary offset, or where two or more debts are owed to a single creditor agency, OFHEO may, at his or her discretion, determine whether one or more debts should be offset simultaneously within the 15 percent limitation.

(2) In the event that a debt owed OFHEO is certified while an employee is subject to salary offset to repay another agency, OFHEO may, at its discretion, determine whether the debt to OFHEO should be repaid before the debt to the other agency is repaid, repaid simultaneously with the other debt, or repaid after the debt to the other agency.

(3) A levy pursuant to the Internal Revenue Code of 1986 shall take precedence over other deductions under this section, as provided in 5 U.S.C. 5514(d).

§ 1704.29 Coordinating salary offset with other agencies.

(a) *Responsibility of OFHEO as the creditor agency.* (1) OFHEO shall be responsible for:

(i) Arranging for a hearing upon proper request by a Federal employee;

(ii) Preparing the Notice of Intent consistent with the requirements of § 1704.21;

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(iii) Obtaining hearing officials from other agencies pursuant to § 1704.23(b); and

(iv) Ensuring that each certification of debt is sent to a paying agency pursuant to § 1704.24(b).

(2) Upon completion of the procedures set forth in §§ 1704.24–1704.26, OFHEO shall submit to the employee's paying agency, if applicable, a certified debt claim and an installment agreement or other instruction on the payment schedule.

(i) If the employee is in the process of separating from the Federal Government, OFHEO shall submit its debt claim to the employee's paying agency for collection by lump-sum deduction from the employee's final check. The paying agency shall certify the total amount of its collection and furnish a copy of the certification to OFHEO and to the employee.

(ii) If the employee is already separated and all payments due from his or her former paying agency have been paid, OFHEO may, unless otherwise prohibited, request that money due and payable to the employee from the Federal Government be administratively offset to collect the debt.

(iii) When an employee transfers to another paying agency, OFHEO shall not repeat the procedures described in §§ 1704.24–1704.26. Upon receiving notice of the employee's transfer, OFHEO shall review the debt to ensure that collection is resumed by the new paying agency.

(b) *Responsibility of OFHEO as the paying agency*—(1) *Complete claim*. When OFHEO receives a certified claim from a creditor agency, the employee shall be given written notice of the certification, the date salary offset will begin, and the amount of the periodic deductions. Deductions shall be scheduled to begin at the next officially established pay interval or as otherwise provided for in the certification.

(2) *Incomplete claim*. When OFHEO receives an incomplete certification of debt from a creditor agency, OFHEO shall return the claim with notice that procedures under 5 U.S.C. 5514 and 5 CFR 550.1104 must be followed, and that a properly certified claim must be received before OFHEO will take action

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to collect the debt from the employee's current pay account.

(3) *Review*. OFHEO is not authorized to review the merits of the creditor agency's determination with respect to the amount or validity of the debt certified by the creditor agency.

(4) *Employees who transfer from one paying agency to another agency*. If, after the creditor agency has submitted the debt claim to OFHEO, the employee transfers to another agency before the debt is collected in full, OFHEO must certify the total amount collected on the debt. One copy of the certification shall be furnished to the employee and one copy shall be sent to the creditor agency along with notice of the employee's transfer. If OFHEO is aware that the employee is entitled to payments from the Civil Service Retirement and Disability Fund or other similar payments, it must provide written notification to the agency responsible for making such payments that the debtor owes a debt (including the amount) and that the requirements set forth herein and in 5 CFR part 550, subpart k, have been met.

[64 FR 34969, June 30, 1999. Redesignated and amended at 65 FR 81328, Dec. 26, 2000]

§ 1704.30 Interest, penalties, and administrative costs.

Where OFHEO is the creditor agency, OFHEO shall assess interest, penalties, and administrative costs pursuant to 31 U.S.C. 3717 and the FCCS.

§ 1704.31 Refunds.

(a) Where OFHEO is the creditor agency, OFHEO shall promptly refund any amount deducted under the authority of 5 U.S.C. 5514 when:

(1) OFHEO receives notice that the debt has been compromised or otherwise found not to be owing to the Federal Government; or

(2) An administrative or judicial order directs OFHEO to make a refund.

(b) Unless required by law or contract, refunds under this section shall not bear interest.

§ 1704.32 Request from a creditor agency for the services of a hearing official.

(a) OFHEO may provide qualified personnel to serve as hearing officials

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upon request of a creditor agency when—

(1) The debtor is employed by OFHEO and the creditor agency cannot provide a prompt and appropriate hearing before a hearing official furnished pursuant to another lawful arrangement; or

(2) The debtor is employed by the creditor agency and that agency cannot arrange for a hearing official.

(b) Services provided by OFHEO to creditor agencies under this section shall be provided on a fully reimbursable basis pursuant to 31 U.S.C. 1535.

[64 FR 34969, June 30, 1999. Redesignated and amended at 65 FR 81328, Dec. 26, 2000]

§ 1704.33 Non-waiver of rights by payments.

A debtor's payment, whether voluntary or involuntary, of all or any portion of a debt being collected pursuant to this subpart B shall not be construed as a waiver of any rights that the debtor may have under any statute, regulation, or contract, except as otherwise provided by law or contract.

§§ 1704.34–1704.39 [Reserved]

Subpart C—Administrative Offset

§ 1704.40 Authority and scope.

OFHEO may collect a debt owed to the Federal Government from a person, organization, or other entity by administrative offset, pursuant to 31 U.S.C. 3716, where:

(a) The debt is certain in amount;

(b) Administrative offset is feasible, desirable, and not otherwise prohibited;

(c) The applicable statute of limitations has not expired; and

(d) Administrative offset is in the best interest of the Federal Government.

§ 1704.41 Administrative offset prior to completion of procedures.

Prior to the completion of the procedures described in §1704.42, OFHEO may effect administrative offset if failure to offset would substantially prejudice its ability to collect the debt, and if the time before the payment is to be made does not reasonably permit completion of the procedures described in §1704.42. Such prior administrative off-

set shall be followed promptly by the completion of the procedures described in §1704.42.

[64 FR 34969, June 30, 1999. Redesignated and amended at 65 FR 81328, Dec. 26, 2000]

§ 1704.42 Procedures.

Unless the procedures described in §1704.41 are used, prior to collecting any debt by administrative offset or referring such claim to another agency for collection through administrative offset, OFHEO shall provide the debtor with the following:

(a) Written notification of the nature and amount of the debt, the intention of OFHEO to collect the debt through administrative offset, and a statement of the rights of the debtor under this section;

(b) An opportunity to inspect and copy the records of OFHEO related to the debt that are not exempt from disclosure;

(c) An opportunity for review within OFHEO of the determination of indebtedness. Any request for review by the debtor shall be in writing and shall be submitted to OFHEO within 30 calendar days of the date of the notice of the offset. OFHEO may waive the time limits for requesting review for good cause shown by the debtor. OFHEO shall provide the debtor with a reasonable opportunity for an oral hearing when:

(1) An applicable statute authorizes or requires OFHEO to consider waiver of the indebtedness involved, the debtor requests waiver of the indebtedness, and the waiver determination turns on an issue of credibility or veracity; or

(2) The debtor requests reconsideration of the debt and OFHEO determines that the question of the indebtedness cannot be resolved by review of the documentary evidence, as for example, when the validity of the debt turns on an issue of credibility or veracity. Unless otherwise required by law, an oral hearing under this subpart C is not required to be a formal evidentiary hearing, although OFHEO shall document all significant matters discussed at the hearing. In those cases where an oral hearing is not required by this subpart C, OFHEO shall make its determination on the request for

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waiver or reconsideration based upon a review of the written record; and

(d) An opportunity to enter into a written agreement for the repayment of the amount of the claim at the discretion of OFHEO.

[64 FR 34969, June 30, 1999. Redesignated and amended at 65 FR 81328, Dec. 26, 2000]

§ 1704.43 Interest.

OFHEO shall assess interest, penalties, and administrative costs on debts owed to the Federal Government, in accordance with 31 U.S.C. 3717 and the FCCS. OFHEO may also assess interest and related charges on debts that are not subject to 31 U.S.C. 3717 and the FCCS to the extent authorized under the common law or other applicable statutory authority.

§ 1704.44 Refunds.

OFHEO shall refund promptly those amounts recovered by administrative offset but later found not to be owed to the Federal Government.

§ 1704.45 Requests for administrative offset to other Federal agencies.

(a) OFHEO may request that a debt owed to OFHEO be collected by administrative offset against funds due and payable to a debtor by another agency.

(b) In requesting administrative offset, OFHEO, as creditor, shall certify in writing to the agency holding funds of the debtor:

(1) That the debtor owes the debt;

(2) The amount and basis of the debt; and

(3) That OFHEO has complied with the requirements of its own administrative offset regulations and the applicable provisions of the FCCS with respect to providing the debtor with due process.

§ 1704.46 Requests for administrative offset from other Federal agencies.

(a) Any agency may request that funds due and payable to a debtor by OFHEO be administratively offset in order to collect a debt owed to such agency by the debtor.

(b) OFHEO shall initiate the requested administrative offset only upon:

(1) Receipt of written certification from the creditor agency that:

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(i) The debtor owes the debt, including the amount and basis of the debt;

(ii) The agency has prescribed regulations for the exercise of administrative offset; and

(iii) The agency has complied with its own administrative offset regulations and with the applicable provisions of the FCCS, including providing any required hearing or review.

(2) A determination by OFHEO that collection by administrative offset against funds payable by OFHEO would be in the best interest of the Federal Government as determined by the facts and circumstances of the particular case and that such administrative offset would not otherwise be contrary to law.

§ 1704.47 Administrative offset against amounts payable from Civil Service Retirement and Disability Fund.

(a) *Request for administrative offset.* Unless otherwise prohibited by law, OFHEO may request that monies that are due and payable to a debtor from the Civil Service Retirement and Disability Fund (Fund) be offset administratively in reasonable amounts in order to collect in one full payment or in a minimal number of payments debt owed to OFHEO by the debtor. Such requests shall be made to the appropriate officials of the Office of Personnel Management in accordance with such regulations as may be prescribed by the Director of the Office of Personnel Management.

(b) *Contents of certification.* When making a request for administrative offset under paragraph (a) of this section, OFHEO shall include a written certification that:

(1) The debtor owes OFHEO a debt, including the amount of the debt;

(2) OFHEO has complied with the applicable statutes, regulations, and procedures of the Office of Personnel Management; and

(3) OFHEO has complied with the requirements of the FCCS, including any required hearing or review.

(c) If OFHEO decides to request administrative offset under paragraph (a) of this section, it shall make the request as soon as practicable after completion of the applicable procedures. This will satisfy any requirement that

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administrative offset be initiated prior to the expiration of the applicable statute of limitations. At such time as the debtor makes a claim for payments from the Fund, if at least one year has elapsed since the administrative offset request was originally made, the debtor shall be permitted to offer a satisfactory repayment plan in lieu of administrative offset if he or she establishes that changed financial circumstances would render the administrative offset unjust.

(d) If OFHEO collects part or all of the debt by other means before deductions are made or completed pursuant to paragraph (a) of this section, OFHEO shall act promptly to modify or terminate its request for administrative offset under paragraph (a) of this section.

§§ 1704.48–1704.49 [Reserved]

Subpart D—Tax Refund Offset

§ 1704.50 Authority and scope.

The provisions of 26 U.S.C. 6402(d) and 31 U.S.C. 3720A authorize the Secretary of the Treasury to offset a delinquent debt owed the Federal Government from the tax refund due a taxpayer when other collection efforts have failed to recover the amount due.

§ 1704.51 Definitions.

(a)(1) *Debt* means money owed by an individual, organization, or entity from sources which include loans insured or guaranteed by the Federal Government and all other amounts due the Federal Government from fees, leases, services, overpayments, civil and criminal penalties, damages, interest, fines, administrative costs, and all other similar sources.

(2) A debt becomes eligible for tax refund offset procedures if:

(i) It cannot currently be collected pursuant to the salary offset procedures of 5 U.S.C. 5514(a)(1);

(ii) The debt is ineligible for administrative offset under 31 U.S.C. 3716(a) by reason of 31 U.S.C. 3716(c)(2), or it cannot be collected currently by administrative offset under 31 U.S.C. 3716(a); and

(iii) The requirements of this section are otherwise satisfied.

(3) All judgment debts are past due for purposes of this subpart D. Judgment debts remain past due until paid in full.

(b) *Dispute* means a written statement supported by documentation or other evidence that all or part of an alleged debt is not past due or legally enforceable, that the amount is not the amount currently owed, that the outstanding debt has been satisfied, or in the case of a debt reduced to judgment, that the judgement has been satisfied or stayed.

(c) *Notice* means the information sent to the debtor pursuant to § 1704.53. The date of the notice is that date shown on the notice letter as its date of issuance.

[64 FR 34969, June 30, 1999. Redesignated and amended at 65 FR 81328, Dec. 26, 2000]

§ 1704.52 Procedures.

(a) *Referral to the Department of the Treasury.* (1) OFHEO may refer any past due, legally enforceable nonjudgment debt of an individual, organization, or entity to the Department of the Treasury for tax refund offset if OFHEO's or the referring agency's rights of action accrued more than three months but less than 10 years before the offset is made.

(2) Debts reduced to judgment may be referred at any time.

(3) Debts in amounts lower than \$25 are not subject to referral.

(4) In the event that more than one debt is owed, the tax refund offset procedures shall be applied in the order in which the debts became past due.

(5) OFHEO shall notify the Department of the Treasury of any change in the amount due promptly after receipt of payment or notice of other reductions.

(b) *Notice.* OFHEO shall provide the debtor with written notice of its intent to offset before initiating the offset. Notice shall be mailed to the debtor at the current address of the debtor, as determined from information obtained from the Internal Revenue Service pursuant to 26 U.S.C. 6103(m)(2), (4), (5) or maintained by OFHEO. The notice sent to the debtor shall state the amount of the debt and inform the debtor that:

(1) The debt is past due;

(2) OFHEO intends to refer the debt to the Department of the Treasury for offset from tax refunds that may be due to the taxpayer;

(3) OFHEO intends to provide information concerning the delinquent debt exceeding \$100 to a consumer reporting bureau unless such debt has already been disclosed; and

(4) Before the debt is reported to a consumer reporting agency, if applicable, and referred to the Department of the Treasury for offset from tax refunds, the debtor has 65 calendar days from the date of notice to request a review under paragraph (d).

(c) *Report to consumer reporting agency.* If the debtor neither pays the amount due nor presents evidence that the amount is not past due or is satisfied or stayed, OFHEO will report the debt to a consumer reporting agency at the end of the notice period, if applicable, and refer the debt to the Department of the Treasury for offset from the taxpayer's Federal tax refund. OFHEO shall certify to the Department of the Treasury that reasonable efforts have been made by OFHEO to obtain payment of such debt.

(d) *Request for review.* A debtor may request a review by OFHEO if he or she believes that all or part of the debt is not past due or is not legally enforceable, or in the case of a judgment debt, that the debt has been stayed or the amount satisfied, as follows:

(1) The debtor must send a written request for review to OFHEO at the address provided in the notice.

(2) The request must state the amount disputed and reasons why the debtor believes that the debt is not past due, is not legally enforceable, has been satisfied, or if a judgment debt, has been satisfied or stayed.

(3) The request must include any documents that the debtor wishes to be considered or state that additional information will be submitted within the time permitted.

(4) If the debtor wishes to inspect records establishing the nature and amount of the debt, the debtor must make a written request to OFHEO for an opportunity for such an inspection. The office holding the relevant records not exempt from disclosure shall make them available for inspection during

normal business hours within one week from the date of receipt of the request.

(5) The request for review and any additional information submitted pursuant to the request must be received by OFHEO at the address stated in the notice within 65 calendar days of the date of issuance of the notice.

(6) In reaching its decision, OFHEO shall review the dispute and shall consider its records and any documentation and arguments submitted by the debtor. OFHEO shall send a written notice of its decision to the debtor. There is no administrative appeal of this decision.

(7) If the evidence presented by the debtor is considered by a non-OFHEO agent or other entities or persons acting on behalf of OFHEO, the debtor shall be accorded at least 30 calendar days from the date the agent or other entity or person determines that all or part of the debt is past due and legally enforceable to request review by OFHEO of any unresolved dispute.

(8) Any debt that previously has been reviewed pursuant to this section or any other section of this part, or that has been reduced to a judgment, may not be disputed except on the grounds of payments made or events occurring subsequent to the previous review or judgment.

PART 1705—IMPLEMENTATION OF THE EQUAL ACCESS TO JUSTICE ACT

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- 1705.20 Filing and service of the application for award and related papers.
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- 1705.29 Payment of award.

AUTHORITY: 5 U.S.C. 504(c)(1).

SOURCE: 65 FR 26732, May 9, 2000, unless otherwise noted. Redesignated and amended at 65 FR 81328, Dec. 26, 2000.

Subpart A—General Provisions

§ 1705.1 Purpose and scope.

(a) This part implements the Equal Access to Justice Act, 5 U.S.C. 504, by establishing procedures for the filing and consideration of applications for award of fees and other expenses to eligible individuals and entities who are parties to adversary adjudications before OFHEO.

(b) This part applies to the award of fees and other expenses in connection with adversary adjudications before OFHEO. However, if a court reviews the underlying decision of the adversary adjudication, an award for fees and other expenses may be made only pursuant to 28 U.S.C. 2412(d)(3).

§ 1705.2 Definitions.

(a) *Adjudicative officer* means the official who presided at the underlying adversary adjudication, without regard to whether the official is designated as a hearing examiner, administrative law judge, administrative judge, or otherwise.

(b) *Adversary adjudication* means an administrative proceeding conducted by OFHEO under 5 U.S.C. 554 in which the position of OFHEO or any other agency of the United States is represented by counsel or otherwise, including but not limited to an adjudication conducted under 12 CFR part 1780. Any issue as to whether an administrative proceeding is an adversary adjudication for purposes of this part will

be an issue for resolution in the proceeding on the application for award.

(c) *Affiliate* means an individual, corporation, or other entity that directly or indirectly controls or owns a majority of the voting shares or other interests of the party, or any corporation or other entity of which the party directly or indirectly owns or controls a majority of the voting shares or other interest, unless the adjudicative officer determines that it would be unjust and contrary to the purpose of the Equal Access to Justice Act in light of the actual relationship between the affiliated entities to consider them to be affiliates for purposes of this part.

(d) *Agency counsel* means the attorney or attorneys designated by the General Counsel of OFHEO to represent OFHEO in an adversary adjudication covered by this part.

(e) *Demand of OFHEO* means the express demand of OFHEO that led to the adversary adjudication, but does not include a recitation by OFHEO of the maximum statutory penalty when accompanied by an express demand for a lesser amount.

(f) *Fees and other expenses* include reasonable attorney or agent fees, the reasonable expenses of expert witnesses, and the reasonable cost of any study, analysis, engineering report, test, or project that is found by the agency to be necessary for the preparation of the eligible party's case.

(g) *Final disposition* means the date on which a decision or order disposing of the merits of the adversary adjudication or any other complete resolution of the adversary adjudication, such as a settlement or voluntary dismissal, becomes final and unappealable, both within the agency and to the courts.

(h) *OFHEO* means the Office of Federal Housing Enterprise Oversight.

(i) *Party* means an individual, partnership, corporation, association, or public or private organization that is named or admitted as a party, that is admitted as a party for limited purposes, or that is properly seeking and entitled as of right to be admitted as a party in an adversary adjudication.

(j) *Position of OFHEO* means the position taken by OFHEO in the adversary adjudication, including the action or

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failure to act by OFHEO upon which the adversary adjudication was based.

§ 1705.3 Eligible parties.

(a) To be eligible for an award of fees and other expenses under § 1705.4(a), a party must be a small entity as defined in 5 U.S.C. 601.

(b)(1) To be eligible for an award of fees and other expenses for prevailing parties under § 1705.5(b), a party must be one of the following:

(i) An individual who has a net worth of not more than \$2 million;

(ii) The sole owner of an unincorporated business who has a net worth of not more than \$7 million, including both personal and business interest, and not more than 500 employees; however, a party who owns an unincorporated business will be considered to be an “individual” rather than the “sole owner of an unincorporated business” if the issues on which the party prevails are related primarily to personal interests rather than to business interests.

(iii) A charitable or other tax-exempt organization described in section 501(c)(3) of the Internal Revenue Code, 26 U.S.C. 501(c)(3), with not more than 500 employees;

(iv) A cooperative association as defined in section 15(a) of the Agricultural Marketing Act, 12 U.S.C. 1141j(a), with not more than 500 employees; or

(v) Any other partnership, corporation, association, unit of local government, or organization that has a net worth of not more than \$7 million and not more than 500 employees.

(2) For purposes of eligibility under paragraph (b) of this section:

(i) The employees of a party include all persons who regularly perform services for remuneration for the party, under the party’s direction and control. Part-time employees shall be included on a proportional basis.

(ii) The net worth and number of employees of the party and its affiliates shall be aggregated to determine eligibility.

(iii) The net worth and number of employees of a party shall be determined as of the date the underlying adversary adjudication was initiated.

(c) A party that participates in an adversary adjudication primarily on

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behalf of one or more entities that would be ineligible for an award is not itself eligible for an award.

[65 FR 26732, May 9, 2000. Redesignated and amended at 65 FR 81328, Dec. 26, 2000]

§ 1705.4 Standards for awards.

(a) An eligible party that files an application for award of fees and other expenses in accordance with this part shall receive an award of fees and other expenses related to defending against a demand of OFHEO if the demand was in excess of the decision in the underlying adversary adjudication and was unreasonable when compared with the decision under the facts and circumstances of the case, unless the party has committed a willful violation of law or otherwise acted in bad faith, or unless special circumstances make an award unjust. The burden of proof that the demand of OFHEO was substantially in excess of the decision and is unreasonable when compared with the decision is on the eligible party.

(b) An eligible party that submits an application for award in accordance with this part shall receive an award of fees and other expenses incurred in connection with an adversary adjudication in which it prevailed or in a significant and discrete substantive portion of the adversary adjudication in which it prevailed, unless the position of OFHEO in the adversary adjudication was substantially justified or special circumstances make an award unjust. OFHEO has the burden of proof to show that its position was substantially justified and may do so by showing that its position was reasonable in law and in fact.

§ 1705.5 Allowable fees and expenses.

(a) Awards of fees and other expenses shall be based on rates customarily charged by persons engaged in the business of acting as attorneys, agents, and expert witnesses, even if the services were made available without charge or at a reduced rate to the party. However, except as provided in § 1705.6, an award for the fee of an attorney or agent may not exceed \$125 per hour and an award to compensate an expert witness may not exceed the highest rate at which OFHEO pays expert witnesses. However, an award may also include

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the reasonable expenses of the attorney, agent, or expert witness as a separate item if he or she ordinarily charges clients separately for such expenses.

(b) In determining the reasonableness of the fee sought for an attorney, agent, or expert witness, the adjudicative officer shall consider the following:

(1) If the attorney, agent, or expert witness is in private practice, his or her customary fees for similar services; or, if the attorney, agent, or expert witness is an employee of the eligible party, the fully allocated costs of the services;

(2) The prevailing rate for similar services in the community in which the attorney, agent, or expert witness ordinarily performs services;

(3) The time actually spent in the representation of the eligible party;

(4) The time reasonably spent in light of the difficulty or complexity of the issues in the adversary adjudication; and

(5) Such other factors as may bear on the value of the services provided.

(c) In determining the reasonable cost of any study, analysis, engineering report, test, project, or similar matter prepared on behalf of a party, the adjudicative officer shall consider the prevailing rate for similar services in the community in which the services were performed.

(d) Fees and other expenses incurred before the date on which an adversary adjudication was initiated will be awarded only if the eligible party can demonstrate that they were reasonably incurred in preparation for the adversary adjudication.

[65 FR 26732, May 9, 2000. Redesignated and amended at 65 FR 81328, Dec. 26, 2000]

§ 1705.6 Rulemaking on maximum rate for fees.

If warranted by an increase in the cost of living or by special circumstances, OFHEO may adopt regulations providing for an award of attorney or agent fees at a rate higher than \$125 per hour in adversary adjudications covered by this part. Special circumstances include the limited availability of attorneys or agents who are qualified to handle certain types of ad-

versary adjudications. OFHEO will conduct any rulemaking proceedings for this purpose under the informal rulemaking procedures of the Administrative Procedures Act, 5 U.S.C. 553.

§ 1705.7 Awards against other agencies.

If another agency of the United States participates in an adversary adjudication before OFHEO and takes a position that was not substantially justified, the award or appropriate portion of the award to an eligible party that prevailed over that agency shall be made against that agency.

§§ 1705.8–1705.9 [Reserved]

Subpart B—Information Required from Applicants

§ 1705.10 Contents of the application for award.

(a) An application for award of fees and other expenses under either § 1705.4(a) and § 1705.4(b) shall:

(1) Identify the applicant and the adversary adjudication for which an award is sought;

(2) State the amount of fees and other expenses for which an award is sought;

(3) Provide the statements and documentation required by paragraph (b) or (c) of this section and § 1705.12 and any additional information required by the adjudicative officer; and

(4) Be signed by the applicant or an authorized officer or attorney of the applicant and contain or be accompanied by a written verification under oath or under penalty of perjury that the information provided in the application is true and correct.

(b) An application for award under § 1705.4(a) shall show that the demand of OFHEO was substantially in excess of, and was unreasonable when compared to, the decision in the underlying adversary adjudication under the facts and circumstances of the case. It shall also show that the applicant is a small entity as defined in 5 U.S.C. 601.

(c) An application for award under § 1705.4(b) shall:

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(1) Show that the applicant has prevailed in a significant and discrete substantive portion of the underlying adversary adjudication and identify the position of OFHEO in the adversary adjudication that the applicant alleges was not substantially justified;

(2) State the number of employees of the applicant and describe briefly the type and purposes of its organization or business (if the applicant is not an individual);

(3) State that the net worth of the applicant does not exceed \$2 million, if the applicant is an individual; or for all other applicants, state that the net worth of the applicant and its affiliates, if any, does not exceed \$7 million; and

(4) Include one of the following:

(i) A detailed exhibit showing the net worth (net worth exhibit) of the applicant and its affiliates, if any, when the underlying adversary adjudication was initiated. The net worth exhibit may be in any form convenient to the applicant as long as the net worth exhibit provides full disclosure of the assets and liabilities of the applicant and its affiliates, if any, and is sufficient to determine whether the applicant qualifies as an eligible party;

(ii) A copy of a ruling by the Internal Revenue Service that shows that the applicant qualifies as an organization described in section 501(c)(3) of the Internal Revenue Code, 26 U.S.C. 501(c)(3); or in the case of a tax-exempt organization not required to obtain a ruling from the Internal Revenue Service on its exempt status, a statement that describes the basis for the belief that the applicant qualifies under such section; or

(iii) A statement that the applicant is a cooperative association as defined in section 15(a) of the Agricultural Marketing Act, 12 U.S.C. 1141j(a).

[65 FR 26732, May 9, 2000. Redesignated and amended at 65 FR 81328, Dec. 26, 2000]

§ 1705.11 Request for confidentiality of net worth exhibit.

(a) The net worth exhibit described in § 1705.10(c)(4)(i) shall be included in the public record of the proceeding for the award of fees and other expenses, except if confidential treatment is re-

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quested and granted as provided in paragraph (b) of this section.

(b)(1) The applicant may request confidential treatment of the information in the net worth exhibit by filing a motion directly with the adjudicative officer in a sealed envelope labeled “Confidential Financial Information.” If the adjudicative officer finds that the information should be withheld from public disclosure, any request to inspect or copy the information by another party or the public shall be resolved in accordance with the Freedom of Information Act, 5 U.S.C. 552b, and the Releasing Information regulation at 12 CFR part 1710.

(2) The motion shall:

(i) Include a copy of the portion of the net worth exhibit sought to be withheld;

(ii) Describe the information sought to be withheld; and

(iii) Explain why the information is exempt from disclosure under the Freedom of Information Act and why public disclosure of the information would adversely affect the applicant and is not in the public’s interest.

(iv) Be served on agency counsel but need not be served on any other party to the proceeding.

[65 FR 26732, May 9, 2000. Redesignated and amended at 65 FR 81328, Dec. 26, 2000]

§ 1705.12 Documentation of fees and expenses.

(a) The application for award shall be accompanied by full and itemized documentation of the fees and other expenses for which an award is sought. The adjudicative officer may require the applicant to provide vouchers, receipts, logs, or other documentation for any fees or expenses claimed.

(b) A separate itemized statement shall be submitted for each entity or individual whose services are covered by the application. Each itemized statement shall include:

(1) The hours spent by each entity or individual;

(2) A description of the specific services performed and the rates at which each fee has been computed; and

(3) Any expenses for which reimbursement is sought, the total amount claimed, and the total amount paid or

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payable by the applicant or by any other person or entity.

§§ 1705.13–1705.19 [Reserved]

Subpart C—Procedures for Filing and Consideration of the Application for Award

§ 1705.20 Filing and service of the application for award and related papers.

(a) An application for an award of fees and other expenses must be filed no later than 30 days after the final disposition of the underlying adversary adjudication.

(b) An application for award and other papers related to the proceedings on the application for award shall be filed and served on all parties in the same manner as papers are filed and served in the underlying adversary adjudication, except as otherwise provided in this part.

(c) The computation of time for filing and service of the application of award and other papers shall be computed in the same manner as in the underlying adversary adjudication.

§ 1705.21 Answer to the application for award.

(a) Agency counsel shall file an answer within 30 days after service of an application for award of fees and other expenses except as provided in paragraphs (b) and (c) of this section. In the answer, agency counsel shall explain any objections to the award requested and identify the facts relied upon to support the objections. If any of the alleged facts are not already in the record of the underlying adversary adjudication, agency counsel shall include with the answer either supporting affidavits or a request for further proceedings under § 1705.25.

(b) If agency counsel and the applicant believe that the issues in the application for award can be settled, they may jointly file a statement of their intent to negotiate a settlement. The filing of this statement shall extend the time for filing an answer for an additional 30 days. Upon request by agency counsel and the applicant, the adjudicative officer may grant for good cause further time extensions.

(c) Agency counsel may request that the adjudicative officer extend the time period for filing an answer. If agency counsel does not answer or otherwise does not contest or settle the application for award within the 30-day period or the extended time period, the adjudicative officer may make an award of fees and other expenses upon a satisfactory showing of entitlement by the applicant.

[65 FR 26732, May 9, 2000. Redesignated and amended at 65 FR 81328, Dec. 26, 2000]

§ 1705.22 Reply to the answer.

Within 15 days after service of an answer, the applicant may file a reply. If the reply is based on any alleged facts not already in the record of the underlying adversary adjudication, the applicant shall include with the reply either supporting affidavits or a request for further proceedings under § 1705.25.

[65 FR 26732, May 9, 2000. Redesignated and amended at 65 FR 81328, Dec. 26, 2000]

§ 1705.23 Comments by other parties.

Any party to the underlying adversary adjudication other than the applicant and agency counsel may file comments on an application for award within 30 calendar days after it is served, or on an answer within 15 calendar days after it is served. A commenting party may not participate further in proceedings on the application unless the adjudicative officer determines that the public interest requires such participation in order to permit full exploration of matters raised in the comments.

§ 1705.24 Settlement.

The applicant and agency counsel may agree on a proposed settlement of an award before the final decision on the application for award is made, either in connection with a settlement of the underlying adversary adjudication or after the underlying adversary adjudication has been concluded. If the eligible party and agency counsel agree on a proposed settlement of an award before an application for award has been filed, the application shall be filed with the proposed settlement.

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§ 1705.25 Further proceedings on the application for award.

(a) On request of either the applicant or agency counsel, on the adjudicative officer's own initiative, or as requested by the Director of OFHEO under §1705.27, the adjudicative officer may order further proceedings, such as an informal conference, oral argument, additional written submissions, or, as to issues other than substantial justification (such as the applicant's eligibility or substantiation of fees and expenses), pertinent discovery or an evidential hearing. Such further proceedings shall be held only when necessary for full and fair resolution of the issues arising from the application for award and shall be conducted as promptly as possible. The issue as to whether the position of OFHEO in the underlying adversary adjudication was substantially justified shall be determined on the basis of the whole administrative record that was made in the underlying adversary adjudication.

(b) A request that the adjudicative officer order further proceedings under this section shall specifically identify the information sought on the disputed issues and shall explain why the additional proceedings are necessary to resolve the issues.

[65 FR 26732, May 9, 2000. Redesignated and amended at 65 FR 81328, Dec. 26, 2000]

§ 1705.26 Decision of the adjudicative officer.

(a) The adjudicative officer shall make the initial decision on the basis of the written record, except if further proceedings are ordered under §1705.25.

(b) The adjudicative officer shall issue a written initial decision on the application for award within 30 days after completion of proceedings on the application. The initial decision shall become the final decision of OFHEO after 30 days from the day it was issued, unless review is ordered under §1705.27.

(c) In all initial decisions, the adjudicative officer shall include findings and conclusions with respect to the applicant's eligibility and an explanation of the reasons for any difference between the amount requested by the applicant and the amount awarded. If the applicant has sought an award against

more than one agency, the adjudicative officer shall also include findings and conclusions with respect to the allocation of payment of any award made.

(d) In initial decisions on applications filed pursuant to §1705.4(a), the adjudicative officer shall include findings and conclusions as to whether OFHEO made a demand that was substantially in excess of the decision in the underlying adversary adjudication and that was unreasonable when compared with that decision; and, if at issue, whether the applicant has committed a willful violation of the law or otherwise acted in bad faith, or whether special circumstances would make the award unjust.

(e) In decisions on applications filed pursuant to §1705.4(b), the adjudicative officer shall include written findings and conclusions as to whether the applicant is a prevailing party and whether the position of OFHEO was substantially justified; and, if at issue, whether the applicant unduly protracted or delayed the underlying adversary adjudication or whether special circumstance make the award unjust.

[65 FR 26732, May 9, 2000. Redesignated and amended at 65 FR 81328, Dec. 26, 2000]

§ 1705.27 Review by OFHEO.

Within 30 days after the adjudicative officer issues an initial decision under §1705.26, either the applicant or agency counsel may request the Director of OFHEO to review the initial decision of the adjudicative officer. The Director of OFHEO or his or her designee may also decide, on his or her own initiative, to review the initial decision. Whether to review a decision is at the discretion of the Director of OFHEO or his or her designee. If review is ordered, the Director of OFHEO or his or her designee shall issue a final decision on the application for award or remand the application for award to the adjudicative officer for further proceedings under §1705.25.

[65 FR 26732, May 9, 2000. Redesignated and amended at 65 FR 81328, Dec. 26, 2000]

§ 1705.28 Judicial review.

Any party, other than the United States, that is dissatisfied with the final decision on an application for

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award of fees and expenses under this part may seek judicial review as provided in 5 U.S.C. 504(c)(2).

§ 1705.29 Payment of award.

To receive payment of an award of fees and other expenses granted under this part, the applicant shall submit a copy of the final decision that grants the award and a certification that the applicant will not seek review of the

decision in the United States courts to the Director, Office of Federal Housing Enterprise Oversight, 1700 G Street, NW., Washington, DC 20552. OFHEO shall pay the amount awarded to the applicant within 60 days of receipt of the submission of the copy of the final decision and the certification, unless judicial review of the award has been sought by any party to the proceedings.

SUBCHAPTER B [RESERVED]

SUBCHAPTER C—SAFETY AND SOUNDNESS

PART 1710—CORPORATE GOVERNANCE

Subpart A—General

Sec.

- 1710.1 Purpose.
- 1710.2 Definitions.
- 1710.3–1710.9 [Reserved]

Subpart B—Corporate Practices and Procedures

- 1710.10 Law applicable to corporate governance.
- 1710.11 Board of directors.
- 1710.12 Committees of board of directors.
- 1710.13 Compensation of board members, executive officers, and employees.
- 1710.14 Code of conduct and ethics.
- 1710.15 Conduct and responsibilities of board of directors.
- 1710.16 Prohibition of extensions of credit to board members and executive officers.
- 1710.17 Certification of disclosures by chief executive officer and chief financial officer.
- 1710.18 Change of audit partner.
- 1710.19 Compliance and risk management programs; compliance with other laws.

Subpart C—Indemnification

- 1710.20 Indemnification.

Subpart D—Modification of Certain Provisions

- 1710.30 Modification of certain provisions.

AUTHORITY: 12 U.S.C. 4513(a) and 4513(b)(1).

SOURCE: 67 FR 38370, June 4, 2002, unless otherwise noted.

Subpart A—General

§ 1710.1 Purpose.

OFHEO is responsible under the Federal Housing Enterprises Financial Safety and Soundness Act of 1992, 12 U.S.C. 4501 *et seq.*, for ensuring the safety and soundness of the Enterprises. In furtherance of that responsibility, this part sets forth minimum standards with respect to the corporate governance practices and procedures of the Enterprises.

§ 1710.2 Definitions.

For purposes of this part, the term:

(a) *Act* means the Federal Housing Enterprises Financial Safety and Soundness Act of 1992, Title XIII of the Housing and Community Development Act of 1992, Pub. L. 102-550, section 1301, Oct. 28, 1992, 106 Stat. 3672, 3941 through 4012 (1993) (12 U.S.C. 4501 *et seq.*).

(b) *Board member* means a member of the board of directors.

(c) *Board of directors* means the board of directors of an Enterprise.

(d) *Chartering acts* mean the Federal National Mortgage Association Charter Act and the Federal Home Loan Mortgage Corporation Act, which are codified at 12 U.S.C. 1716 through 1723i and 12 U.S.C. 1451 through 1459, respectively.

(e) *Compensation* means any payment of money or the provision of any other thing of current or potential value in connection with employment. The term “compensation” includes all direct and indirect payments of benefits, both cash and non-cash, including, but not limited to, payments and benefits derived from compensation or benefit agreements, fee arrangements, perquisites, stock option plans, post employment benefits, or other compensatory arrangements.

(f) *Director* means the Director of OFHEO or his or her designee.

(g) *Employee* means a salaried individual, other than an executive officer, who works part-time, full-time, or temporarily for an Enterprise.

(h) *Enterprise* means the Federal National Mortgage Association or the Federal Home Loan Mortgage Corporation; and the term “Enterprises” means, collectively, the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation.

(i) *Executive officer* means any senior executive officer and any senior vice president of an Enterprise and any individual with similar responsibilities, without regard to title, who is in charge of a principal business unit, division, or function of an Enterprise, or

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who reports directly to the chairperson, vice chairperson, chief operating officer, or president of an Enterprise.

(j) *NYSE* means the New York Stock Exchange.

(k) *OFHEO* means the Office of Federal Housing Enterprise Oversight.

(l) *Senior executive officer* means the chairperson of the board of directors, chief executive officer, chief financial officer, chief operating officer, president, vice chairperson, any executive vice president of an Enterprise, and any individual, without regard to title, who has similar responsibilities.

§§ 1710.3–1710.9 [Reserved]

Subpart B—Corporate Practices and Procedures

§ 1710.10 Law applicable to corporate governance.

(a) *General*. The corporate governance practices and procedures of each Enterprise shall comply with applicable chartering acts and other Federal law, rules, and regulations, and shall be consistent with the safe and sound operations of the Enterprise.

(b) *Election and designation of body of law*. (1) To the extent not inconsistent with paragraph (a) of this section, each Enterprise shall follow the corporate governance practices and procedures of the law of the jurisdiction in which the principal office of the Enterprise is located, as amended; Delaware General Corporation Law, Del. Code Ann. tit. 8, as amended; or the Revised Model Business Corporation Act, as amended.

(2) Each Enterprise shall designate in its bylaws the body of law elected for its corporate governance practices and procedures pursuant to this paragraph within 90 calendar days from August 5, 2002.

§ 1710.11 Board of directors.

(a) *Membership*—(1) *Limits on service of board members*—(i) *General requirement*. No board member of an Enterprise may serve on the board of directors for more than 10 years or past the age of 72, whichever comes first; provided, however, a board member may serve his or her full term if he or she has served less than 10 years or is 72 years on the

date of his or her election or appointment to the board.

(ii) *Waiver*. Upon written request of an Enterprise, the Director may waive, in his or her sole discretion and for good cause, the limits on the service of a board member under paragraph (a)(1)(i) of this section.

(2) *Independence of board members*. A majority of seated members of the board of directors of an Enterprise shall be independent board members, as defined under rules set forth by the NYSE, as amended from time to time.

(b) *Meetings, quorum and proxies, information, and annual review*—(1) *Frequency of meetings*. The board of directors of an Enterprise shall meet at least eight times a year and no less than once a calendar quarter to carry out its obligations and duties under applicable laws, rules, regulations, and guidelines.

(2) *Non-management board member meetings*. Non-management directors of an Enterprise shall meet at regularly scheduled executive sessions without management participation.

(3) *Quorum of board of directors; proxies not permissible*. For the transaction of business, a quorum of the board of directors of an Enterprise is at least a majority of the seated board of directors and a board member may not vote by proxy.

(4) *Information*. Management of an Enterprise shall provide a board member of the Enterprise with such adequate and appropriate information that a reasonable board member would find important to the fulfillment of his or her fiduciary duties and obligations.

(5) *Annual review*. At least annually, the board of directors of an Enterprise shall review, with appropriate professional assistance, the requirements of laws, rules, regulations, and guidelines that are applicable to its activities and duties.

[70 FR 17310, Apr. 6, 2005]

§ 1710.12 Committees of board of directors.

(a) *General*. The board of directors may rely, in directing the Enterprise, on reports from committees of the board of directors, provided, however, that no committee of the board of directors shall have the authority of the

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board of directors to amend the bylaws and no committee shall operate to relieve the board of directors or any board member of a responsibility imposed by applicable law, rule, or regulation.

(b) *Frequency of meetings.* A committee of the board of directors of an Enterprise shall meet with sufficient frequency to carry out its obligations and duties under applicable laws, rules, regulations, and guidelines.

(c) *Required committees.* An Enterprise shall provide for the establishment of, however styled, the following committees of the board of directors, which committees shall be in compliance with the charter, independence, composition, expertise, duties, responsibilities, and other requirements set forth under section 301 of the Sarbanes-Oxley Act of 2002, Pub. L. 107-204 (Jul. 30, 2002) (SOA), as amended from time to time, with respect to the audit committee, and under rules issued by the NYSE, as amended from time to time—

- (1) Audit committee;
- (2) Compensation committee; and
- (3) Nominating/corporate governance committee.

[67 FR 38370, June 4, 2002. Redesignated and amended at 70 FR 17310, 17311, Apr. 6, 2005]

§ 1710.13 Compensation of board members, executive officers, and employees.

(a) *General.* Compensation of board members, executive officers, and employees of an Enterprise shall not be in excess of that which is reasonable and appropriate, shall be commensurate with the duties and responsibilities of such persons, shall be consistent with the long-term goals of the Enterprise, shall not focus solely on earnings performance, but shall take into account risk management, operational stability and legal and regulatory compliance as well, and shall be undertaken in a manner that complies with applicable laws, rules, and regulations.

(b) *Reimbursement.* If an Enterprise is required to prepare an accounting restatement due to the material non-compliance of the Enterprise, as a result of misconduct, with any financial reporting requirement under the securities laws, the chief executive officer and chief financial officer of the Enter-

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prise shall reimburse the Enterprise as provided under section 304 of the SOA, as amended from time to time. This provision does not otherwise limit the authority of OFHEO to employ remedies available to it under its enforcement authorities.

[67 FR 38370, June 4, 2002. Redesignated and amended at 70 FR 17310, 17311, Apr. 6, 2005]

§ 1710.14 Code of conduct and ethics.

(a) *General.* An Enterprise shall establish and administer a written code of conduct and ethics that is reasonably designed to assure the ability of board members, executive officers, and employees of the Enterprise to discharge their duties and responsibilities, on behalf of the Enterprise, in an objective and impartial manner, and that includes standards required under section 406 of the SOA, as amended from time to time, and other applicable laws, rules, and regulations.

(b) *Review.* Not less than once every three years, an Enterprise shall review the adequacy of its code of conduct and ethics for consistency with practices appropriate to the Enterprise and make any appropriate revisions to such code.

[70 FR 17311, Apr. 6, 2005]

§ 1710.15 Conduct and responsibilities of board of directors.

(a) *Purpose.* The purpose of this section, and of this subpart, is to set forth minimum standards of the conduct and responsibilities of the board of directors in furtherance of the safe and sound operations of each Enterprise. The provisions of this section neither provide shareholders of an Enterprise with additional rights nor impose liability on any board member under State law.

(b) *Conduct and responsibilities.* The board of directors of an Enterprise is responsible for directing the conduct and affairs of the Enterprise in furtherance of the safe and sound operation of the Enterprise and shall remain reasonably informed of the condition, activities, and operations of the Enterprise. The responsibilities of the board of directors include having in place

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adequate policies and procedures to assure its oversight of, among other matters, the following:

(1) Corporate strategy, major plans of action, risk policy, programs for legal and regulatory compliance and corporate performance, including but not limited to prudent plans for growth and allocation of adequate resources to manage operations risk;

(2) Hiring and retention of qualified senior executive officers and succession planning for such senior executive officers;

(3) Compensation programs of the Enterprise;

(4) Integrity of accounting and financial reporting systems of the Enterprise, including independent audits and systems of internal control;

(5) Process and adequacy of reporting, disclosures, and communications to shareholders, investors, and potential investors;

(6) Extensions of credit to board members and executive officers; and

(7) Responsiveness of executive officers in providing accurate and timely reports to Federal regulators and in addressing the supervisory concerns of Federal regulators in a timely and appropriate manner.

(c) *Guidance.* The board of directors should refer to the body of law elected under § 1710.10 and to publications and other pronouncements of OFHEO for additional guidance on conduct and responsibilities of the board of directors.

[67 FR 38370, June 4, 2002, as amended at 70 FR 17311, Apr. 6, 2005]

§ 1710.16 Prohibition of extensions of credit to board members and executive officers.

An Enterprise may not directly or indirectly, including through any subsidiary, extend or maintain credit, arrange for the extension of credit, or renew an extension of credit, in the form of a personal loan to or for any board member or executive officer of the Enterprise as provided by section 402 of the SOA, as amended from time to time.

[70 FR 17311, Apr. 6, 2005]

§ 1710.17 Certification of disclosures by chief executive officer and chief financial officer.

The chief executive officer and the chief financial officer of an Enterprise shall review each quarterly report and annual report issued by the Enterprise and such reports shall include certifications by such officers as required by section 302 of the SOA, as amended from time to time.

[70 FR 17311, Apr. 6, 2005]

§ 1710.18 Change of audit partner.

An Enterprise may not accept audit services from an external auditing firm if the lead or coordinating audit partner who has primary responsibility for the external audit of the Enterprise, or the external audit partner who has responsibility for reviewing the external audit has performed audit services for the Enterprise in each of the five previous fiscal years.

[70 FR 17312, Apr. 6, 2005]

§ 1710.19 Compliance and risk management programs; compliance with other laws.

(a) *Compliance program.* (1) An Enterprise shall establish and maintain a compliance program that is reasonably designed to assure that the Enterprise complies with applicable laws, rules, regulations, and internal controls.

(2) The compliance program shall be headed by a compliance officer, however styled, who reports directly to the chief executive officer of the Enterprise. The compliance officer shall report regularly to the board of directors or an appropriate committee of the board of directors on compliance with and the adequacy of current compliance policies and procedures of the Enterprise, and shall recommend any adjustments to such policies and procedures that he or she considers necessary and appropriate.

(b) *Risk management program.* (1) An Enterprise shall establish and maintain a risk management program that is reasonably designed to manage the risks of the operations of the Enterprise.

(2) The risk management program shall be headed by a risk management

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officer, however styled, who reports directly to the chief executive officer of the Enterprise. The risk management officer shall report regularly to the board of directors or an appropriate committee of the board of directors on compliance with and the adequacy of current risk management policies and procedures of the Enterprise, and shall recommend any adjustments to such policies and procedures that he or she considers necessary and appropriate.

(c) *Compliance with other laws.* (1) If an Enterprise deregisters or has not registered its common stock with the U.S. Securities and Exchange Commission (Commission) under the Securities Exchange Act of 1934, the Enterprise shall comply or continue to comply with sections 301, 302, 304, 402, and 406 of the SOA, as amended from time to time, subject to such requirements as provided by § 1710.30 of this part.

(2) An Enterprise that has its common stock registered with the Commission shall maintain such registered status, unless it provides 60 days prior written notice to the Director stating its intent to deregister and its understanding that it will remain subject to the requirements of sections 301, 302, 304, 402, and 406 of the SOA, as amended from time to time, subject to such requirements as provided by § 1710.30 of this part.

[70 FR 17312, Apr. 6, 2005]

Subpart C—Indemnification

§ 1710.20 Indemnification.

(a) *Safety and soundness authority.* OFHEO has the authority, under the Act, to prohibit or restrict reimbursement or indemnification of any current or former board member or any current or former executive officer by an Enterprise or by any affiliate of an Enterprise in furtherance of the safe and sound operations of the Enterprise.

(b) *Policies and procedures.* Each Enterprise shall have in place policies and procedures consistent with this part for indemnification, including the approval or denial by the board of directors of indemnification of current and former board members and current or former executive officers. Such policies and procedures should address, among

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other matters, standards relating to indemnification, investigation by the board of directors, and review by independent counsel.

Subpart D—Modification of Certain Provisions

§ 1710.30 Modification of certain provisions.

In connection with standards of Federal or state law (including the Revised Model Corporation Act) or NYSE rules that are made applicable to an Enterprise by §§ 1710.10, 1710.11, 1710.12, 1710.17, and 1710.19 of this part, the Director, in his or her sole discretion, may modify the standards contained in this part in accordance with 5 U.S.C. 553 and upon written notice to the Enterprise.

[70 FR 17312, Apr. 6, 2005]

PART 1720—SAFETY AND SOUNDNESS

Sec.

1720.1 Authority.

1720.2 Safety and soundness standards.

APPENDIX A TO PART 1720—POLICY GUIDANCE; MINIMUM SAFETY AND SOUNDNESS REQUIREMENTS

APPENDIX B TO PART 1720—POLICY GUIDANCE; NON-MORTGAGE LIQUIDITY INVESTMENTS

APPENDIX C TO PART 1720—POLICY GUIDANCE; SAFETY AND SOUNDNESS STANDARDS FOR INFORMATION

AUTHORITY: 12 U.S.C. 4513(a), 4513(b)(1), 4513(b)(5), 4517(a), 4521(a)(2) through (3), 4631, 4632, and 4636.

SOURCE: 67 FR 55693, Aug. 30, 2002, unless otherwise noted.

§ 1720.1 Authority.

(a) *Authority.* This part is issued by the Office of Federal Housing Enterprise Oversight (OFHEO) pursuant to sections 1313(a), 1313(b)(1), and 1313(b)(5) of the Federal Housing Enterprise Financial Safety and Soundness Act (Act) (12 U.S.C. 4513(a), 4513(b)(1), and 4513(b)(5)). These provisions of the Act authorize OFHEO to take any action deemed appropriate by the Director of OFHEO to ensure that the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation (the Enterprises) are operated in a safe and sound manner, including by

adopting supervisory policies and standards by regulation, guidance, or other process.

(b) *Preservation of existing authority.* No action by OFHEO undertaken with reference to a policy guidance or this regulation will in any way limit the authority of the Director otherwise to address unsafe or unsound conditions or practices, or other violations of law, rule or regulation. Action with reference to a policy guidance or this regulation may be taken separate from, in conjunction with, or in addition to any other supervisory response, enforcement action, or agency-imposed requirements deemed appropriate by OFHEO. Nothing in this regulation or any guidance issued by OFHEO limits the authority of the Director pursuant to section 1313 of the Act (12 U.S.C. 4513) or any other provision of law, rule or regulation applicable to the Enterprises.

§1720.2 Safety and soundness standards.

Policy guidances as may be adopted from time to time by OFHEO, addressing safety and soundness standards, shall apply to the Enterprises. If OFHEO determines that an Enterprise does not meet a requirement set out in such policy guidance, it may require corrective or remedial actions by the Enterprise, and take such enforcement action as the Director deems to be appropriate.

APPENDIX A TO PART 1720—POLICY GUIDANCE; MINIMUM SAFETY AND SOUNDNESS REQUIREMENTS

A—BACKGROUND AND INTRODUCTION

- I. Background
- II. Introduction

B—OPERATIONAL AND MANAGERIAL REQUIREMENTS

- I. Asset underwriting and credit quality.
- II. Balance sheet growth and management.
- III. Market risk.
- IV. Information technology.
- V. Internal controls.
- VI. Audits.
- VII. Information reporting and documentation.
- VIII. Board and management responsibilities and function.
- IX. Format of policies and procedures.

C—COMPLIANCE PLANS

- I. Notice; submission and review of compliance plan.
- II. Failure to submit acceptable plan or to comply with plan.

A—BACKGROUND AND INTRODUCTION

I. Background. The Federal Housing Enterprises Safety and Soundness Act of 1992, Title XIII of Pub. L. No. 102-550 (the Act) empowers OFHEO to take any such action as the Director determines to be appropriate to ensure that the federally sponsored housing enterprises, Fannie Mae and Freddie Mac, are, among other things, adequately capitalized and operating safely, including by adopting supervisory policies and standards by regulation or other guidance or process.

i. OFHEO herein sets forth the minimum supervisory requirements used by the agency in reviewing the ensuring, the adequacy of policies and procedures of the Enterprises in the areas of: (1) Asset underwriting and credit quality; (2) balance sheet growth; (3) market risks; (4) information technology; (5) internal controls; (6) audits; (7) information reporting and documentation; and (8) board and management responsibilities and functions. If the agency finds that an Enterprise fails to meet any requirement or standard set forth in this pronouncement, the Director may, among other things, require the Enterprise to submit to the agency and implement an adequate plan to achieve timely compliance with the requirement or standard. If the Enterprise fails to submit such an adequate plan within the time specified by the agency or fails in any material respect to implement the plan, the agency may take additional supervisory action. The Director may at any time prescribe such supervisory actions as deemed appropriate to correct conditions resulting from an unsafe or unsound practice or condition or deficiency in complying with regulatory requirements or standards including, but not limited to, issuance of a notice of charges or order, imposition of civil money penalties, or other remedial actions or sanctions as determined by the Director.

ii. The minimum supervisory requirements and standards identify key safety and soundness concerns regarding operation and management of an Enterprise, and ensure that action is taken to avoid the emergence of problems that might entail serious risks to an Enterprise. The minimum supervisory requirements of the Policy Guidance also reflect the need for internal policies and procedures in particular areas that, if not appropriately addressed by the Enterprises, may warrant action by OFHEO in order to reduce risks of loss and possible capital impairment. The proposed minimum requirements set forth herein are intended to effect these

purposes without dictating how the Enterprises must be operated and managed; moreover, the Policy Guidance does not set out detailed operational and managerial procedures that an Enterprise must have in place. The Policy Guidance is intended to identify the ends that proper operational and management policies and procedures are to achieve, while leaving the means to be devised by each Enterprise as it designs and implements its own policies and procedures. Where OFHEO does specify particular requirements, each Enterprise's management is left with substantial flexibility to fashion and implement them.

iii. The Policy Guidance is not intended to effect a change in OFHEO's policies; the announced minimum requirements reflect the basic underlying criteria OFHEO uses to assess the operations and managerial quality of an Enterprise. OFHEO will determine compliance with the requirements and related standards through examinations of the Enterprises, as well as off-site surveillance means and other interchanges with each Enterprise.

iv. OFHEO routinely undertakes to evaluate an Enterprise's overall policies, in order to determine whether such policies are safe and sound in principle and in practice. OFHEO also evaluates whether procedures are in place to ensure that an Enterprise's overall policies as adopted by the Enterprise's board of directors and management are, in fact, applied in the normal course of business. As reflected in the Policy Guidance, the Enterprises are, at a minimum, expected to adopt appropriate policies and internal guidelines, and to put in place procedures to ensure they are followed as a matter of routine.

v. Nothing in the Policy Guidance in any way limits the authority of OFHEO to otherwise address unsafe or unsound conditions or practices, or violations of applicable law, regulation or supervisory order. Action referencing the Policy Guidance may be taken separate from, in conjunction with or in addition to any other enforcement action available to OFHEO. Compliance with the Policy Guidance in general would not preclude a finding by the agency that an Enterprise is otherwise engaged in a specific unsafe or unsound practice or is in an unsafe or unsound condition, or requiring corrective or remedial action with regard to such practice or condition. That is, supervisory action is not precluded against an Enterprise that has not been cited for a deficiency under the Policy Guidance. Conversely, an Enterprise's failure to comply with one of the supervisory requirements set forth in the Policy Guidance may not warrant a formal supervisory response from OFHEO, if the agency determines the matter may be otherwise addressed in a satisfactory manner. For example, OFHEO may require timely submission

of a plan to achieve compliance with the particular requirement or standard without taking any other enforcement action.

II. Introduction. i. *Authority, purpose, and scope.*

a. *Authority.* This Policy Guidance is issued by the Office of Federal Housing Enterprise Oversight (OFHEO) pursuant to sections 1313(a), 1313(b)(1), 1313(b)(5) and 1371 of the Federal Housing Enterprise Safety and Soundness Act (Act) (12 U.S.C. 4513(a), 4513(b)(1), 4513(b)(5) and 4631). These provisions of the Act authorize OFHEO to take any action deemed appropriate by the Director of OFHEO to ensure that the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation (the Enterprises) are operated in a safe and sound manner, including by adopting supervisory policies and standards by regulation, guidance, or other process.

b. *Purpose and scope.* This Policy Guidance sets out certain minimum safety and soundness requirements for the business and operations of the Enterprises, and reiterates agency policies requiring the Enterprises to establish and implement policies and procedures that are sufficient to effectuate compliance with supervisory standards. If OFHEO determines that an Enterprise does not meet the requirements set forth herein, the Director may require the Enterprise to submit and carry out a plan to achieve compliance, or may take other corrective and remedial actions. The requirements enumerated herein are supervisory minimums. In order to satisfy an Enterprise's overarching obligation under the Act to conduct its operations in a safe and sound manner, it may be necessary and appropriate for an Enterprise to take additional measures in these or other areas, as directed by OFHEO through regulation, guidance, order or otherwise as part of the supervisory process.

ii. *Preservation of existing authority.* Neither this Policy Guidance nor any action by OFHEO to enforce compliance of an Enterprise therewith in any way limits the authority of the Director otherwise to address unsafe or unsound conditions or practices, or other violations of law or other regulation. Action under this Policy Guidance may be taken separate from, in conjunction with, or in addition to any other enforcement action deemed appropriate by OFHEO. Nothing in this Policy Guidance or related guidances limits the authority of the Director pursuant to section 1313 of the Act (12 U.S.C. 4513) or any other provision of law, rule or regulation applicable to the Enterprises.

iii. *Definitions.* For purposes of this Policy Guidance, except as modified therein or unless the context otherwise requires, the terms used have the same meaning as set forth in section 1303 of the Act (12 U.S.C. 4502).

B—OPERATIONAL AND MANAGERIAL
REQUIREMENTS

I. Asset underwriting and credit quality. An Enterprise should establish and implement policies and procedures to adequately assess credit risks before they are assumed, and monitor such risks subsequently to ensure that they conform to the Enterprise's credit risk standards on an individual and an aggregate basis. The Enterprise should:

i. For loans purchased and loans collateralizing securities guaranteed by the Enterprise, adopt and implement prudent underwriting standards and procedures commensurate with the type of loan or loans and the markets in which the loan or loans were made that include consideration of the borrower's and any guarantor's financial condition and ability to repay as well as the type and value of any collateral or credit enhancement;

ii. To the extent the Enterprise's assets are serviced or administered by other entities or are covered by mortgage insurance or other credit enhancements or arrangements, the Enterprise's policies and procedures should recognize the consequences and implications of such contractual arrangements for the Enterprise's credit risk;

iii. Establish and implement policies and procedures to address declining credit quality and to require appropriate corrective action; to establish sufficient reserves; and to deal with defaulted assets so as to minimize losses;

iv. Establish and implement policies and procedures to select and price credit risk to ensure that the Enterprise is appropriately compensated commensurate with the credit risk it assumes and its statutory obligations;

v. Establish and implement policies and procedures that address the prudential selection, management and handling of counterparty credit exposure that arises from engaging in hedging activities and the use derivative instruments; and

vi. Establish and implement policies and procedures to identify, monitor and evaluate its credit exposures on an aggregate basis so as to assess the implications and consequences of matters such as concentration exposure (including geographic as well as product concentrations), to identify and evaluate credit risk trends effectively, and to maintain and revise appropriately its systems and procedures for underwriting, servicing, and monitoring of such exposures and changes to those exposures.

II. Balance sheet growth and management. An Enterprise's balance sheet growth should be prudent and consider:

i. The source, volatility, and use of funds that support balance sheet growth;

ii. Any changes in credit risk or interest rate risk resulting from balance sheet growth;

iii. The effect of balance sheet growth on the Enterprise's capital adequacy; and

iv. The appropriate policies and procedures needed to manage changes in risk that may occur as a result of balance sheet growth.

III. Market risk. An Enterprise should establish and implement policies and procedures that allow for the effective identification, measurement, monitoring, and management of market risk. The Enterprise should:

i. Establish and implement policies and procedures sufficient to quantify and monitor the interest rate risk of the Enterprise effectively and to model the effect of differing interest rate scenarios on the Enterprise's financial condition and operations;

ii. Develop risk management strategies that respond appropriately to changes in interest rates;

iii. Establish and implement policies and procedures sufficient to quantify and monitor the Enterprise's liquidity effectively, and to identify and anticipate various market environments and their effects on the Enterprises' liquidity; and

iv. Establish and maintain an effective contingency plan for liquidity under varying scenarios.

IV. Information technology. An Enterprise should establish and implement policies and procedures to ensure that its computing resources, proprietary and nonpublic information and data are:

i. Protected from access by unauthorized users, and otherwise protected by appropriate security measures;

ii. Reliable, accurate and available at all times as needed for its business operations, including an ability to effect timely recovery and resume operations after a reasonably foreseeable adverse event; and

iii. Designed to ensure adequate support of business operations.

V. Internal controls. An Enterprise should maintain and implement internal controls appropriate to the nature, scope and risk of its business activities that, at a minimum, provide for:

i. An organizational structure and assignment of responsibility for management, employees, consultants and contractors, that provide for accountability and controls, including adherence to policies and procedures;

ii. A control framework commensurate with the Enterprise's risks;

iii. Policies and procedures adequate to safeguard and to manage assets; and

iv. Compliance with applicable laws, regulations and policies.

VI. Audits. An Enterprise should establish and implement internal and external audit programs appropriate to the nature and scope of its business activities that, at minimum, provide for:

i. Adequate monitoring of internal controls through an audit function appropriate to the

Enterprise's size, structure and scope of operations;

- ii. Independence of the audit function;
- iii. Qualified professionals and management for the conduct and review of audit functions;
- iv. Adequate testing and review of audited areas together with adequate documentation of findings and of any recommendations and corrective actions; and
- v. Verification and review of measures and actions undertaken to address identified material weaknesses.

VII. Information reporting and documentation. An Enterprise should establish and implement policies and procedures for generating and retaining reports and documents that:

- i. Enable the Enterprise's board of directors (including appropriate committees) to make informed decisions and to exercise its oversight function, by providing all such relevant information of an appropriate level of detail as necessary;
- ii. Enable the Enterprise's managers to make informed business decisions and to assess risks for all aspects of the Enterprise's business on an ongoing basis, by providing sufficient relevant information of an appropriate level of detail as necessary;
- iii. Ensure decision-makers have appropriate and necessary information about particular transactions and business operations;
- iv. Enable the Enterprise to administer and supervise all assets, liabilities, commitments and other financial obligations appropriately;
- v. Enable the Enterprise to enforce legal claims against borrowers, counterparties and other obligors; and
- vi. Ensure timely and complete submissions of reports of financial condition and operations, as well as annual and other periodic reports and special reports to OFHEO whenever requested or required by OFHEO.

VIII. Board and management responsibilities and function. An Enterprise's board of directors shall ensure that the board (including appropriate committees) works with executive management to establish the Enterprise's strategies and goals in an informed manner, and that the Enterprise's executive managers and other managers, as appropriate, implement such strategies, by ensuring at a minimum that:

- i. The board (including appropriate committees) oversees the development of the Enterprise's strategies in key areas and exercises oversight necessary to ensure that management sets policies and controls to implement such strategies effectively;
- ii. The board (including appropriate committees) hires qualified executive management, and exercises oversight to hold management accountable for meeting the Enterprise's goals and objectives;

- iii. The board (including appropriate committees) is provided with accurate information about the operations and financial condition of the Enterprise in a timely fashion, and sufficient to enable the board to effect its oversight duties and responsibilities;

- iv. Management of the Enterprise sets policies and controls to ensure the Enterprise's strategies are implemented effectively, and that the Enterprise's organization structure and assignment of responsibilities provide clear accountability and controls; and

- v. Management of the Enterprise establishes and maintains an effective risk management framework, including review of such framework to monitor its effectiveness and taking appropriate action to correct any weaknesses.

IX. Format of policies and procedures. i. Generally, the policies of an Enterprise contemplated by this Policy Guidance should be in writing and in such form and detail as appropriate in light of their intended purpose, nature, and potential consequences for the operations and financial condition of the Enterprise, and approved by the board of directors (including appropriate committees) or such responsible officer or officers as designated by the board.

- ii. The policies and procedures of an Enterprise contemplated by this Policy Guidance should be provided to OFHEO at such time and in such format as OFHEO directs.

C—COMPLIANCE PLANS

I. Notice; submission and review of compliance plans. i. *Determination.* The Director of OFHEO may, based upon a report of examination, or other supervisory information however acquired, determine that an Enterprise has failed or is likely to fail to satisfy the minimum supervisory requirements or standards set forth in part B of this appendix.

- ii. *Request for compliance plan.* If the Director determines pursuant to paragraph C.I.i of this appendix that an Enterprise has failed or is likely to fail to satisfy a supervisory requirement or standard, OFHEO may require the submission of a written compliance plan.

- iii. *Schedule for filing compliance plan.* An Enterprise may be required to file a written compliance plan with OFHEO within thirty days of receiving a written request for a compliance plan pursuant to paragraph C.I.ii of this appendix.

- iv. *Contents of plan.* A required compliance plan should include, subject to additional direction by OFHEO, a detailed description of the steps the Enterprise will take to correct a deficiency and any condition resulting therefrom and the time within which such steps will be undertaken and fully implemented.

- v. *Review of compliance plans.* If the compliance plan submitted under this section is deemed to be inadequate or incomplete,

OFHEO may provide written notice of such inadequacy or deficiencies thereof to the Enterprise OFHEO or seek additional information from the Enterprise regarding the plan.

vi. *Amendment of compliance plan.* An Enterprise that has filed a required compliance plan to which no objection has been raised by OFHEO may, after prior written notice to and approval by the Director, amend the plan to reflect changes in circumstance, policies and procedures.

ii. *Failure to submit acceptable plan or to comply with plan.* If an Enterprise does not submit an adequate and complete plan as required by the agency within the time specified by OFHEO or does not implement such an adequate and complete plan, the Director may require the Enterprise to correct any deficiency and may require additional corrective or remedial actions by the Enterprise as deemed to be appropriate pursuant to the Act, including sections 1371 (12 U.S.C. 4631), 1372 (12 U.S.C. 4632), and 1376 (12 U.S.C. 4636).

APPENDIX B TO PART 1720—POLICY GUIDANCE; NON-MORTGAGE LIQUIDITY INVESTMENTS

- A—Purpose
- B—Activities Covered
- C—Standards for Non-mortgage Liquidity Investment Activities
- D—Disclosure of Non-mortgage Liquidity Investment Activities
- E—Summary

A—PURPOSE

1. Fannie Mae and Freddie Mac (the Enterprises) were chartered by Congress as government-sponsored enterprises with public missions. They perform an important role in the United States mortgage market by gathering funds and purchasing mortgages from mortgage originators and guaranteeing mortgage-backed securities. In chartering the Enterprises, Congress charged the Enterprises with: (1) providing stability to mortgage markets; (2) responding to the changing capital markets; (3) assisting the secondary markets including the support of these markets for affordable housing; and (4) promoting access to credit throughout the country by increasing liquidity and improving distribution of investment capital for residential mortgage finance. These functions require the Enterprises, as principals in the secondary mortgage market, to serve as bedrock in providing liquidity to the U.S. housing finance system.

2. For the Enterprises effectively to perform their public purposes, they must be financially sound and liquid. As the Enterprises' financial safety and soundness regulator, OFHEO conducts its regulatory programs to ensure these companies adhere to safety and soundness standards. In addition, OFHEO interprets this to include height-

ening the positive effect of market discipline on the Enterprises by encouraging quality disclosures, appropriate accounting standards, and state-of-the-art risk management further strengthens their safety and soundness. More specifically, OFHEO conducts comprehensive safety and soundness examinations and requires the Enterprises to adhere to regulatory capital requirements. In conducting its regulatory programs, OFHEO applies a series of safety and soundness standards to assess the Enterprises' liquidity management, including their investments in non-mortgage liquidity assets. It is appropriate to issue initial guidance that addresses the safety and soundness standards OFHEO uses to evaluate Enterprise investment activities in non-mortgage liquidity assets.

3. Further, it should be noted that the Secretary of HUD, who has general regulatory power over the Enterprises and who is required to make such rules and regulations as necessary to ensure that the purposes of the GSE's respective Charter Acts are accomplished, has issued an Advanced Notice of Proposed Rulemaking on possible substantive and/or procedural rules governing the GSEs' non-mortgage investment activities. Accordingly, the GSEs may be subject to regulations in this area through future HUD actions, in addition to this initial guidance.

B—ACTIVITIES COVERED

1. The Enterprises must maintain sufficient liquidity to meet both known and unexpected payment demands on borrowings and mortgage securities, for operations and to purchase mortgage assets. Liquidity management is the process by which the Enterprises manage the use and availability of various funding sources to meet current and future needs. Liquidity must be closely managed on a daily basis.

2. The Enterprises manage liquidity through three primary channels: securitizations, issuance of debt and conversion of liquid assets into cash. It is through careful management within and among the three channels, that the Enterprises can effectively meet demands and remain safe and sound under all market conditions. This Guidance specifically addresses "non-mortgage liquidity investments" which are conducted within the liquidity channel whereby the Enterprises are able to convert their own assets into cash.

3. There are various types of investments that may be appropriate for non-mortgage liquidity holdings. Appropriate non-mortgage liquidity investments are characterized by both creditworthiness and low price volatility. Even though an investment may be creditworthy, if the holding is subject to undue price volatility (e.g. common stock), the investment is inappropriate for inclusion

in the non-mortgage liquidity portfolio since the investment may not be readily converted into cash without substantial loss.

4. For the purposes of this Guidance, the types of assets listed below are generally considered to be appropriate non-mortgage liquidity investments. This list is subject to revision over time as new asset types are introduced and/or market activities change. The presence of an asset on the list does not mean that OFHEO will necessarily consider any and all Enterprise investments in these assets to be safe and sound, especially if they fail to meet appropriate credit quality, maturity and diversification objectives:

- a. Debt issued by the United States Treasury,
- b. Debt issued by U.S. Government Agencies,
- c. General obligation debt issued by states and municipal authorities,
- d. Revenue obligations issued by states and municipal authorities,
- e. Corporate debt instruments,
- f. Money market instruments,
- g. Non-mortgage asset-backed securities, and
- h. Reverse repurchase agreements.

5. This Guidance does not address investments in mortgage-backed securities, mortgage revenue bonds, or other investments secured by housing (including commercial mortgage-backed securities with a significant housing component) since these assets are not principally held for liquidity purposes. Also, upon implementation of FAS 133, this Guidance is not intended to address the use of derivative instruments. For activities not covered in this Guidance on non-mortgage liquidity investments, there should be no inferences drawn about OFHEO's views.

C—STANDARDS FOR NON-MORTGAGE LIQUIDITY INVESTMENT ACTIVITIES

To ensure there are sufficient funds available to the mortgage market, the Enterprise must actively manage liquidity across all three channels. OFHEO assesses the safety and soundness of non-mortgage liquidity investment activities against five criteria. The five criteria and details about each of the criteria are:

- Prudent investment policies and procedures that guide the Enterprise's process;
- Quality management information that ensures timely performance measures and governance data;
- Safe & sound investment holdings and investment culture;
- Quality controls and personnel administering and governing the process; and
- Independent testing of the process to assure compliance.

1. Prudent Investment Policies and Procedures That Guide the Enterprise's Process

a. The Enterprise must have a comprehensive written investment policy that clearly expresses the goals for the non-mortgage liquidity investment activities. The Board of Directors and management must evaluate the effectiveness of non-mortgage liquidity investments in meeting the goals set out in the policy; and management must evaluate activities against the procedures and limitations in the policy. At a minimum, the policy should cover:

- i. The purpose of the non-mortgage liquidity investment holdings;
- ii. The institutional goal(s) for the non-mortgage liquidity investment holdings;
- iii. The authorized instruments and activities;
- iv. The internal control standards;
- v. The limits structure;
- vi. The performance standards and measures; and
- vii. The reporting requirements.

b. The policy should clearly document the purpose for non-mortgage liquidity investment holdings. Management should install a series of procedures and controls that produce behaviors and performance that are consistent with the defined purpose for the non-mortgage liquidity investment activities.

c. The policy should establish the primary goals for the non-mortgage liquidity investment activities. For an Enterprise, some primary goals should be to augment liquidity and to generate a rate of return that is reasonable in light of the purpose of such investments. The emphasis placed on individual goals may vary based upon institutional differences. However, non-mortgage liquidity investments made with a goal of maximizing earnings or maximizing arbitrage opportunities would be inconsistent with this Guidance for the maintenance of an Enterprise's liquidity portfolio.

d. The policy should clearly define the authorized investment vehicles and establish guidelines for the introduction of new types of investment vehicles.

e. The Enterprise's procedures should include a framework of controls that provide an appropriate separation of duties and responsibilities. There should be responsibility assigned for an independent review of non-mortgage liquidity investments by a designated unit, such as audit or an independent risk oversight group.

f. The Enterprise should adopt a limit structure to promote diversification in the non-mortgage liquidity investment portfolio and emphasizes strategies for risk mitigation. Additionally, there should be limits for the aggregate size of the non-mortgage liquidity investment portfolio.

g. The Enterprise should adopt measures to evaluate performance against the policy and its objectives.

h. The Enterprise should adopt internal reporting requirements that quantify performance, document exceptions, and serve as a basis for communicating information about activities involving non-mortgage liquidity assets.

i. The Enterprise should periodically evaluate the adequacy and content of its public disclosure for non-mortgage investment liquidity activities.

2. Quality Management Information That Ensures Timely Performance Measures and Governance Data

a. The Enterprise must maintain systems that adequately identify, measure and report the nature and level of exposure associated with their non-mortgage liquidity investments. Management must remain appropriately informed about the activity in non-mortgage liquidity investments. Also, the Board of Directors should periodically be provided a summary of non-mortgage liquidity investment activities. At a minimum, management's reports to the Board should:

i. Summarize non-mortgage investment activity since the last report;

ii. Identify and explain any material changes or trends in the non-mortgage liquidity investment portfolio risk and returns; and

iii. Report and explain exceptions to the policy or risk guidelines for liquidity investments.

b. Meaningful changes in portfolio volume and spreads from period to period should be identified and explained to the Board in terms of why they occurred (*e.g.*, changes in portfolio composition, changes in funding costs, etc.). In overseeing the day-to-day management of non-mortgage liquidity investment activities, management should consider the discrete risks associated with the non-mortgage liquidity investment portfolio as well as the exposure of this portfolio within the context of risks across the entire Enterprise. This includes assessing the non-mortgage liquidity investment portfolio's sensitivity to changes in interest rates, expressed in terms of net interest income sensitivity and portfolio value sensitivity.

3. Safe and Sound Investment Holdings and Investment Culture

a. The Enterprise should implement and enforce policies and/or procedures for non-mortgage liquidity investments. Management should establish limits and procedures in a manner that is consistent with the Board's sanctioned goals and risk appetite. Certain risk-limits for non-mortgage liquidity investments may be expressed in terms of how they affect the Enterprise's overall risk-

profile, such as those pertaining to interest-rate sensitivity. Other risk limits may be more appropriately expressed in terms of individual portfolios and instruments. In addition, limits restricting the size-range and scope of the non-mortgage liquidity investment activities should be established.

b. The limits and procedures should delineate the acceptable investment instruments, acceptable markets, acceptable counterparties, along with unacceptable investment or portfolio activities. The Enterprise should maintain sufficient documentation to demonstrate due diligence in adhering to policies, procedures, limits and guidelines.

c. At a minimum, limits should be established and reviewed annually, for:

i. Credit threshold guidelines: Credit quality is a compelling factor for liquidity investments. Since liquidity investments should be able to be readily converted into cash without substantial exposure to losses, investments should be insulated from price vulnerabilities that are associated with creditworthiness. The most effective means of insulating against price exposure from credit quality concerns is to invest in high-quality instruments and the debt obligations of high-quality issuers. The Enterprise should establish thresholds identifying the minimum credit standards of any security eligible for purchase. Where these standards involve credit ratings, the ratings should come from a nationally recognized rating organization. Procedures should be included that determine the steps to be taken by management if an instrument's credit rating falls below the minimum threshold before maturity.

ii. Maturity guidelines: Because the maturity of an investment significantly affects its exposure to credit risk and price volatility, longer maturity instruments have limited suitability as liquidity investments. The Enterprise should establish the maximum maturity allowable for non-mortgage liquidity investments. It would be appropriate to have different maturity limits for certain types of instruments. For example, management may wish to establish shorter maturity limits for fixed-coupon instruments than for adjustable-rate securities. Management may have different maturity limits for bullet securities and amortizing structures. It would be appropriate to establish a maturity matrix based upon an instrument's credit rating at the time of purchase.

iii. Diversification and concentration guidelines: Credit concentrations can increase credit risk. Accordingly, the Enterprise should establish guidelines that limit investments in the securities of any single issuer. Such limits may be established as a percentage limit (*e.g.*, as a percentage of capital) or as an absolute dollar amount. To enhance portfolio liquidity, there should also

be a limit on the percentage of any particular issue held by the Enterprise.

4. Quality Controls and Personnel Administering and Governing the Process

a. The Enterprise should maintain a comprehensive set of controls to enforce the appropriate separation of duties and responsibilities. These controls should translate into clear procedures for routine operations. At a minimum, the internal control program for non-mortgage liquidity investment activities should include procedures for the following: portfolio valuation, personnel, settlement, physical control and documentation, conflict of interest, and accounting.

i. Portfolio valuation procedures. Portfolio valuation procedures should require pricing that is independent of the investment portfolio managers. Pricing securities provides an indication of the market depth and liquidity for individual instruments, and is an important process for providing data to the risk management function, particularly within a framework of estimating market value sensitivity. Pricing is particularly important for securities that are classified as “available-for-sale” for accounting purposes.

ii. Personnel guidelines. Personnel guidelines should require competent and experienced staff be responsible for conducting transactions and managing the non-mortgage investment portfolio. There should be clear guidance regarding the roles and responsibilities of individuals involved with the non-mortgage liquidity portfolio.

iii. Settlement practices. Procedures should cover standard settlement practices for the various types of non-mortgage liquidity investments in the Enterprise’s portfolio. Inadequate understanding of standard settlement practices, coupled with poor internal controls, could result in unnecessary costs or losses.

iv. Control and documentation. Procedures covering control and documentation should be comprehensive and consistent with the evolving better practices in the marketplace. The procedures should include, for example, standards for: processing and controlling purchased instruments, safeguarding investment documentation and reviewing trade tickets and confirmations.

v. Conflict of interest. Conflict of interest guidelines should govern all Enterprise personnel authorized to purchase or sell non-mortgage liquidity investments. These guidelines should ensure that all directors, officers and employees act in the Enterprise’s best interest. Conflict of interest guidelines should address employee relationships with authorized broker/dealers. Guidelines should also address personnel accepting gifts and travel expenses from broker/dealers.

vi. Accounting. Accounting practices should be evaluated to determine the level of compliance with GAAP standards.

5. Independent Testing and Review of the Process To Assure Compliance

a. An independent review of non-mortgage liquidity investment activities should be conducted periodically to ensure:

i. The accuracy and integrity of information provided to the Board, management and other oversight bodies;

ii. The adherence to policy, procedures, limits and guidelines;

iii. The timeliness, accuracy and usefulness of non-mortgage investment reports;

iv. The adequacy of personnel resources and capabilities; and

v. The non-mortgage liquidity investment activities remain appropriate in the context of the marketplace and the external environment.

b. This review may be conducted by a risk oversight unit or internal audit department, or any party that is independent of the routine risk-taking decisions and should be commensurate with the level of review of other primary Enterprise activities. Independent review findings for non-mortgage liquidity investments should be reported to the Board directly or through one of its committees. The Board should consider the independent review when reaffirming policies, and should address any issues raised.

D—DISCLOSURE OF NON-MORTGAGE LIQUIDITY INVESTMENT ACTIVITIES

1. Sound risk management practices include thorough disclosures about the Enterprise’s risks and further regulators’ efforts to increase financial transparency for regulated financial companies. Quality disclosures about risks and risk management can be an effective deterrent to excessive risk-taking. Three essential elements needed to promote market discipline for non-mortgage liquidity investments are (1) type of issuer and security, (2) maturity, and (3) credit quality or rating. Accordingly, quality disclosure for a portfolio of non-mortgage liquidity investments should include a detailed categorization of the portfolio with respect to each of these elements and cross-categorization, so that (for example) the quantity of any longer-maturity, lower-credit-quality assets is clearly identified. Information about fair values; yields; and narrative discussions of objectives, risk management policies, and controls can also promote transparency of risk and should be included. Such disclosures should be made quarterly, and they should be made using average balances so that average risks can be assessed—not just the risks on a given date.

2. Over the next few quarters, OFHEO will discuss more specifically with the Enterprise

how these disclosures will meet the expectations expressed in this guidance. An example of a disclosure format that may be used by the Enterprise is available on the OFHEO Web site at <http://www.ofheo.gov>. However, the Enterprise may disclose the risks in its non-mortgage liquidity investment activities, consistent with the expectations expressed in this guidance, using a format of its choice.

E—SUMMARY

This Guidance sets forth OFHEO's process for evaluating the safety and soundness of liquidity non-mortgage investment activities. OFHEO remains committed to ensuring the Enterprises remain financially sound, have appropriate control environments, and engage only in financially sound business and investment activities. OFHEO's examiners have been instructed to incorporate this evaluation process into their ongoing safety and soundness examinations. Examiners will evaluate and test the Enterprise's non-mortgage liquidity investment processes and activities to ensure they are in compliance with this guidance.

APPENDIX C TO PART 1720—POLICY GUIDANCE; SAFETY AND SOUNDNESS STANDARDS FOR INFORMATION

A—INTRODUCTION

1. Scope.
2. Preservation of Existing Authority.
3. Definitions.

B—SAFETY AND SOUNDNESS STANDARDS FOR INFORMATION

1. Information Security Program.
2. Objectives.

C—DEVELOPMENT AND IMPLEMENTATION OF INFORMATION SECURITY PROGRAM

1. Involve the Board of Directors.
2. Assess Risk.
3. Manage and Control Risk.
4. Oversee Service Provider Arrangements.
5. Adjust the Program.
6. Report to the Board.
7. Implementation.

A—INTRODUCTION

The Policy Guidance on Safety and Soundness Standards for Information sets forth standards pursuant to section 1313 of the Federal Housing Enterprise Safety and Soundness Act (12 U.S.C. 4513). The Guidance addresses standards for developing and implementing administrative, technical, and physical safeguards to protect the security, confidentiality, and integrity of information.

1. *Scope.* The Guidance applies to information maintained by or on behalf of the Fed-

eral National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac) (collectively, the Enterprises).

2. *Preservation of Existing Authority.* Nothing in the Guidance in any way limits the authority of OFHEO to otherwise address unsafe or unsound conditions or practices or violations of applicable law, regulation or supervisory order. Action referencing the Policy Guidance may be taken separate from, in conjunction with or in addition to any other enforcement action available to OFHEO. Compliance with the Policy Guidance in general would not preclude a finding by the agency that an Enterprise is otherwise engaged in a specific unsafe or unsound practice or is in an unsafe or unsound condition, or requiring corrective or remedial action with regard to such practice or condition. That is, supervisory action is not precluded against an Enterprise that has not been cited for a deficiency under the Policy Guidance. Conversely, an Enterprise's failure to comply with one of the supervisory requirements set forth in the Policy Guidance may not warrant a formal supervisory response from OFHEO, if the agency determines the matter may be otherwise addressed in a satisfactory manner. For example, OFHEO may require the submission of a plan to achieve compliance with the particular requirement or standard without taking any other enforcement action.

3. *Definitions.* For purposes of the Guidance, the following definitions apply:

a. *Information* means any record of an Enterprise, whether in paper, electronic, or other form, that is handled or maintained by or on behalf of an Enterprise;

b. *Information security program* means the administrative, technical, or physical safeguards used by an Enterprise to access, collect, process, store, use, transmit, dispose of, or otherwise handle information;

c. *Information systems* means any methods used to access, collect, store, use, transmit, protect, or dispose of information;

d. *Service provider* means any person or entity, including any third party vendor, that maintains, processes or otherwise is permitted access to information through its provision of services directly or indirectly to an Enterprise.

B—SAFETY AND SOUNDNESS STANDARDS FOR INFORMATION

1. *Information Security Program.* Each Enterprise shall implement a comprehensive written information security program that includes administrative, technical, and physical safeguards appropriate to the nature and scope of its activities. While all parts of the Enterprise are not required to implement a uniform set of policies, all elements of the information security program must be coordinated.

2. *Objectives.* An Enterprise's information security program shall be designed to:

- a. Ensure the security and confidentiality of information;
- b. Protect against any anticipated threats or hazards to the security or integrity of such information; and
- c. Protect against unauthorized access to or use of such information.

C—DEVELOPMENT AND IMPLEMENTATION OF INFORMATION SECURITY PROGRAM

1. *Involve the Board of Directors.* The board of directors or an appropriate committee of the board of each Enterprise shall:

- a. Approve the Enterprise's written information security program; and
- b. Oversee the development, implementation, and maintenance of the Enterprise's information security program, including assigning specific responsibility for its implementation and reviewing reports from management.

2. *Assess Risk.* Each Enterprise shall:

- a. Identify reasonably foreseeable internal and external threats that could result in unauthorized disclosure, misuse, alteration, or destruction of information or information systems;
- b. Assess the likelihood and potential damage of these threats, taking into consideration the sensitivity of nonpublic information; and
- c. Assess the sufficiency of policies, procedures, information systems, and other arrangements in place to control risks.

3. *Manage and Control Risk.* Each Enterprise shall:

- a. Design its information security program to manage and control the identified risks, commensurate with the sensitivity of the information as well as the complexity and scope of the Enterprise's activities. Each Enterprise should consider whether the following security measures are appropriate for the Enterprise and, if so, adopt those measures the Enterprise concludes are appropriate:

- i. Access controls over information systems, including controls to authenticate and permit access only to authorized individuals and controls to prevent employees from providing information to unauthorized individuals who may seek to obtain this information through fraudulent means;
- ii. Access restrictions at physical locations containing information, such as buildings, computer facilities, and records storage facilities to permit access only to authorized individuals;
- iii. Encryption of electronic information, including while in transit or in storage on networks or systems to which unauthorized individuals may have access;
- iv. Procedures designed to ensure that information system modifications are con-

sistent with the Enterprise's information security program;

- v. Dual control procedures, segregation of duties, and employee background checks for employees with responsibilities for or access to information;

vi. Monitoring systems and procedures to detect actual and attempted attacks on or intrusion into information systems;

vii. Response programs that specify actions to be taken when the Enterprise suspects or detects that unauthorized individuals have gained access to information systems, including appropriate reports to regulatory and law enforcement agencies; and

viii. Measures to protect against destruction, loss or damage of information due to potential environmental hazards, such as fire and water damage or technological failures.

b. Train staff to implement the Enterprise's information security program; and

c. Regularly test the key controls, systems and procedures of the information security program. The frequency and nature of such tests should be determined by the Enterprise's risk assessment. Tests should be conducted or reviewed by independent third parties or staff that are independent of those that develop or maintain the security programs.

4. *Oversee Service Provider Arrangements.* Each Enterprise shall:

a. Exercise appropriate due diligence in selecting its service providers;

b. Require its service providers by contract to implement appropriate measures designed to meet the objectives of the Guidance; and

c. Where indicated by the Enterprise's risk assessment, monitor its service providers to confirm that they have satisfied their obligations as required by section 9(b). As part of this monitoring, an Enterprise should review audits, summaries of test results, or other equivalent evaluations of its service providers.

5. *Adjust the Program.* Each Enterprise shall monitor, evaluate, and adjust, as appropriate, the information security program in light of any relevant changes in technology, the sensitivity of its information, internal or external threats to information, and the Enterprise's own changing business arrangements, such as acquisitions, alliances and joint ventures, outsourcing arrangements, and changes to information systems.

6. *Report to the Board.* Each Enterprise shall report to its board or an appropriate committee of the board at least annually. This report should describe the overall status of the information security program and the Enterprise's compliance with the Guidance. The reports should discuss material matters related to its program, addressing issues such as: risk assessment; risk management and control decisions; service provider arrangements; results of testing; security

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breaches or violations and management's responses; and recommendations for changes in the information security program.

7. *Implementation.* a. Each Enterprise should implement an information security program pursuant to the Guidance.

b. Until January 1, 2004, a contract that an Enterprise has entered into with a service provider to perform services for it or functions on its behalf satisfies the provisions of section 9, even if the contract does not include a requirement that the servicer maintain the security and confidentiality of information, as long as the Enterprise entered into the contract on or before the effective date.

PART 1730—DISCLOSURE OF FINANCIAL AND OTHER INFORMATION

Sec.

1730.1 Purpose.

1730.2 Definitions.

1730.3 Periodic disclosures.

1730.4 Submission of disclosures.

AUTHORITY: 12 U.S.C. 4513; 12 U.S.C. 4514; 12 U.S.C. 4631; and, 12 U.S.C. 4632.

SOURCE: 68 FR 16718, Apr. 7, 2003, unless otherwise noted.

§ 1730.1 Purpose.

(a) The purpose of this part is to require the Enterprises to prepare and submit financial and other disclosures as specified by OFHEO.

(b) This part does not limit or restrict the authority of OFHEO to act under its safety and soundness mandate to regulate the Enterprises, including conducting examinations, requiring reports and disclosures, and enforcing compliance with applicable laws, rules and regulations.

§ 1730.2 Definitions.

For purposes of this part, the term:

(a) *Commission* means the Securities and Exchange Commission (or SEC).

(b) *Disclosure or disclosures* means any report[s], form[s], or other information submitted by the Enterprises pursuant to this part and may be used interchangeably with the terms "report[s]" or "form[s]."

(c) *Enterprise* means the Federal National Mortgage Association or the Federal Home Loan Mortgage Corporation; and the term "Enterprises" means, collectively, the Federal Na-

tional Mortgage Association and the Federal Home Loan Mortgage Corporation.

(d) *Exchange Act* means the Securities Exchange Act of 1934.

(e) *OFHEO* means the Office of Federal Housing Enterprise Oversight (or the office).

§ 1730.3 Periodic disclosures.

(a) Each Enterprise shall prepare disclosures relating to its financial condition, results of operation, business developments, and management's expectations that include supporting financial information and certifications.

(b) The requirement of paragraph (a) of this section for disclosures will be satisfied if:

(1) In the case of an Enterprise having a class of securities registered pursuant to Section 12 of the Exchange Act, the Enterprise prepares and makes public an annual report, quarterly report and current reports and such other materials that may be required under the rules and regulations of the Commission, including interpretations of the Commission and its staff and rules governing audited financial statements;

(2) The Enterprise files with the Commission all reports, statements, and forms required pursuant to Sections 14(a) and (c) of the Exchange Act and by rules and regulations adopted by the Commission under those sections that would be required to be filed by the Enterprises if the Enterprises has a class of equity securities registered under Section 12(g) of the Exchange Act that were not exempted securities under the Exchange Act; and,

(3) The officers and directors of the Enterprise file with the Commission all reports and forms relating to the common stock of the Enterprise that would be required to be filed by the officers and directors pursuant to Section 16 of the Exchange Act and by rules and regulations adopted by the Commission under that section if the Enterprises had a class of equity securities registered under Section 12(g) of the Exchange Act that were not exempted securities under the Exchange Act.

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§ 1730.4 Submission of disclosures.

Unless otherwise required by OFHEO, the Enterprises shall provide to OFHEO on a concurrent basis copies of all disclosures filed with the SEC pursuant to §1730.3.

PART 1731—MORTGAGE FRAUD REPORTING

Sec.

1731.1 Purpose and scope.

1731.2 Definitions.

1731.3 Unsafe and unsound conduct.

1731.4 Procedures for reporting.

1731.5 Internal controls, procedures, and training.

1731.6 Supervisory action.

AUTHORITY: 12 U.S.C. 4513(a) and 4513(b)(1), (2), and (7).

SOURCE: 70 FR 43627, July 28, 2005, unless otherwise noted.

§ 1731.1 Purpose and scope.

The purpose of this section is to set forth safety and soundness requirements with respect to the reporting of mortgage fraud in furtherance of the supervisory responsibilities of OFHEO under the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (12 U.S.C. 4501 *et seq.*).

§ 1731.2 Definitions.

For purposes of this part—

(a) *Director* means the Director of OFHEO, or his or her designee.

(b) *Enterprise* means the Federal National Mortgage Association or the Federal Home Loan Mortgage Corporation.

(c) *Mortgage fraud* means a material misstatement, misrepresentation, or omission relied upon by an Enterprise to fund or purchase—or not to fund or purchase—a mortgage, including a mortgage associated with a mortgage-backed security or similar financial instrument issued or guaranteed by an Enterprise. Such mortgage fraud includes, but is not limited to, a material misstatement, misrepresentation, or omission in identification and employment documents, mortgagee or mortgagor identity, and appraisals that are fraudulent.

(d) *OFHEO* means the Office of Federal Housing Enterprise Oversight.

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(e) *Possible mortgage fraud* means that an Enterprise has a reasonable belief, based upon a review of information available to the Enterprise, that mortgage fraud may be occurring or has occurred.

§ 1731.3 Unsafe and unsound conduct.

An Enterprise may not require the repurchase of or may not decline to purchase a mortgage, mortgage backed security, or similar financial instrument because of possible mortgage fraud without promptly reporting to the Director under §1731.4. An Enterprise may decline such purchase or require such repurchase if it is reporting mortgage fraud or possible mortgage fraud in accordance with §1731.4.

§ 1731.4 Procedures for reporting.

(a) *Procedures for reporting*—(1) *Prompt report*. An Enterprise shall report promptly mortgage fraud or possible mortgage fraud in writing to the Director in such format and under such notification procedures as prescribed by OFHEO. The report shall describe the mortgage fraud or possible mortgage fraud in detail sufficient under OFHEO guidance. The Enterprise, at the sole discretion of the Director, may be required to provide additional or continuing information in connection with such mortgage fraud.

(2) *Immediate report*. In addition to reporting in writing under paragraph (a)(1) of this section, in any situation requiring immediate attention by OFHEO, an Enterprise shall report the mortgage fraud or possible mortgage fraud to the Director by telephone or electronic communication.

(b) *Retention of records*. An Enterprise shall maintain a copy of any report submitted to the Director and the original or business record equivalent of any supporting documentation for a period of five years from the date of submission.

(c) *Nondisclosure*. An Enterprise may not disclose, without the prior written approval of the Director, to the party or parties connected with the mortgage fraud or possible mortgage fraud that it has reported such fraud under this part. This restriction does not prohibit an Enterprise from—

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(1) Disclosing or reporting such fraud pursuant to legal requirements, including reporting to appropriate law enforcement or other governmental authorities; or

(2) Taking any legal or business action it may deem appropriate, including any action involving the party or parties connected with the mortgage fraud or possible mortgage fraud.

(d) *Acceptance of other forms.* The Director may, upon written notice to each Enterprise, accept reports of mortgage fraud or possible mortgage fraud in formats promulgated by any Federal agency that has jurisdiction over the reporting of mortgage fraud or possible mortgage fraud by the Enterprises.

(e) *No waiver of privilege.* An Enterprise does not waive any privilege it may claim under law by reporting mortgage fraud or possible mortgage fraud under this part.

§ 1731.5 Internal controls, procedures, and training.

An Enterprise shall establish adequate and efficient internal controls and procedures and an operational training program to assure an effective system to detect and report mortgage fraud or possible mortgage fraud under this part.

§ 1731.6 Supervisory action.

Failure by an Enterprise to comply with §§ 1731.3, 1731.4, and 1731.5 may subject the Enterprise or the board members, officers, or employees thereof to supervisory action by OFHEO under the Federal Housing Enterprises Safety and Soundness Act of 1992 (12 U.S.C. 4501 *et seq.*), including but not limited to, cease-and-desist proceedings and civil money penalties.

PART 1732—RECORD RETENTION

Subpart A—General

Sec.

1732.1 Purpose and scope.

1732.2 Definitions.

1732.3–4 [Reserved]

Subpart B—Record Retention Program

1732.5 Establishment and evaluation of record retention program.

1732.6 Minimum requirements of record retention program.

1732.7 Record hold.

1732.8–1732.9 [Reserved]

Subpart C—Supervisory Action

1732.10 Supervisory action.

AUTHORITY: 12 U.S.C. 4513(a), 4513(b)(1), 4513(b)(5), 4514, 4631, 4632, and 4632.

SOURCE: 71 FR 62884, Oct. 27, 2006, unless otherwise noted.

Subpart A—General

§ 1732.1 Purpose and scope.

In furtherance of the safety and soundness authorities of OFHEO, this part sets forth minimum requirements in connection with the record retention program of each Enterprise. The requirements are intended to ensure that complete and accurate records of an Enterprise are readily accessible by OFHEO for examination and other supervisory purposes. Such access shall be by reasonable means, consistent with the nature and availability of the records and existing information technology.

§ 1732.2 Definitions.

For purposes of this part, the term:

(a) *Act* means the Federal Housing Enterprises Financial Safety and Soundness Act of 1992, Title XIII of the Housing and Community Development Act of 1992, Public Law 102-550, section 1301, Oct. 28, 1992, 106 Stat. 3672, 3941 through 4012 (1993) (12 U.S.C. 4501 *et seq.*).

(b) *Active record* means a record that is necessary to conduct the current business of an office or business unit of an Enterprise and, therefore, is readily available for consultation and reference.

(c) *Director* means the Director of OFHEO, or his or her designee.

(d) *Electronic record* means a record created, generated, communicated, or stored by electronic means.

(e) *Employee* means any officer or employee of an Enterprise or any conservator appointed by OFHEO.

(f) *Enterprise* means the Federal National Mortgage Association or the Federal Home Loan Mortgage Corporation; and the term “Enterprises”

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means, collectively, the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation.

(g) *E-mail* means electronic mail, which is a method of communication in which:

(1) Usually, text is transmitted (but sometimes also graphics and/or audio information);

(2) Operations include sending, storing, processing, and receiving information;

(3) Users are allowed to communicate under specified conditions; and

(4) Messages are held in storage until called for by the addressee, including any attachment of separate electronic files.

(h) *Inactive record* means a record that is seldom used but must be retained by an Enterprise for fiscal, legal, historical, or vital records purposes.

(i) *OFHEO* means the Office of Federal Housing Enterprise Oversight.

(j) *Record* means any information whether generated internally or received from outside sources by an Enterprise or employee maintained in connection with Enterprise business, regardless of the following:

(1) Form or format, including hard copy documents (*e.g.*, files, logs, and reports) and electronic documents (*e.g.*, e-mail, databases, spreadsheets, PowerPoint presentations, electronic reporting systems, electronic tapes and back-up tapes, optical discs, CD-ROMS, and DVDs), and voicemail records;

(2) Where the information is stored or located, including network servers, desktop or laptop computers and handheld computers, other wireless devices with text messaging capabilities, and on-site or off-site at a storage facility;

(3) Whether the information is maintained or used on Enterprise-owned equipment, or personal or home computer systems of an employee; or

(4) Whether the information is active or inactive.

(k) *Record retention schedule* means a schedule that details the categories of records an Enterprise is required to retain and the corresponding retention periods. The record retention schedule includes all media, such as microfilm

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and machine-readable computer records, for each record category. Reproductions are also included for each record category if the original of the official record is not available.

(l) *Retention period* means the length of time that records must be kept before they are destroyed. Records not authorized for destruction have a retention period of “permanent.”

(m) *Vital records* means records that are needed to meet operational responsibilities of an Enterprise under emergency or disaster conditions (emergency operating records) or to protect the legal and financial rights of an Enterprise. Emergency operating records are the type of vital records essential to the continued functioning or reconstitution of an Enterprise during and after an emergency. A vital record may be both an emergency operating record and a legal and financial rights record.

§§ 1732.3–1732.4 [Reserved]

Subpart B—Record Retention Program

§ 1732.5 Establishment and evaluation of record retention program.

(a) *Establishment*. An Enterprise shall establish and maintain a written record retention program and provide a copy of such program to the OFHEO Examiner-in-Charge of the Enterprise within 120 days of the effective date of this part, and annually thereafter, and whenever a significant revision to the program has been made.

(b) *Evaluation*. Management of the Enterprise shall evaluate in writing the adequacy and effectiveness of the record retention program at least every three years and provide a copy of the evaluation to the board of directors and the OFHEO Examiner-in-Charge of the Enterprise.

§ 1732.6 Minimum requirements of record retention program.

(a) *Requirements*. The record retention program established and maintained by an Enterprise under § 1732.5 shall:

(1) Be reasonably designed to assure that retained records are complete and accurate;

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(2) Be reasonably designed to assure that the format of retained records and the retention period—

(i) Are adequate to support litigation and the administrative, business, external and internal audit functions of the Enterprise;

(ii) Comply with requirements of applicable laws and regulations; and

(iii) Permit ready access by the Enterprise and, upon request, by the examination and other staff of OFHEO by reasonable means, consistent with the nature and availability of the records and existing information technology;

(3) Assign in writing the authorities and responsibilities for record retention activities;

(4) Include policies and procedures concerning record holds, consistent with §1732.7;

(5) Include an accurate, current, and comprehensive record retention schedule that lists records by major categories, subcategories, record type, and retention period, which retention period is appropriate to the specific record and consistent with applicable legal, regulatory, fiscal, and operational and business requirements;

(6) Include adequate security and internal controls to protect records from unauthorized access and data alteration; and

(7) Provide for adequate back-up and recovery of electronic records.

(b) *Training.* The record retention program shall provide for training of and notice to all employees on a periodic basis on their record retention responsibilities, including instruction regarding penalties provided by law for the unlawful removal or destruction of records. The record retention program also shall provide for training for the agents or independent contractors of an Enterprise, as appropriate, consistent with their respective roles and responsibilities to the Enterprise.

§ 1732.7 Record hold.

(a) *Definition.* For purposes of this part, the term “record hold” means a requirement, an order, or a directive from an Enterprise or OFHEO that the Enterprise is to retain records relating to a particular issue in connection with an actual or a potential OFHEO examination, investigation, enforcement

proceeding, or litigation of which the Enterprise has received notice from OFHEO.

(b) *Notification by Enterprise.* The record retention program of an Enterprise shall:

(1) Address how employees and, as appropriate, how agents or independent contractors consistent with their respective roles and responsibilities to the Enterprise, will receive prompt notification of a record hold;

(2) Designate an individual to communicate specific requirements and instructions, including, when necessary, the instruction to cease immediately any otherwise permissible destruction of records; and,

(3) Provide that any employee and, as appropriate, any agent or independent contractor consistent with his or her respective role and responsibility to the Enterprise, who has received notice of a potential investigation, enforcement proceeding, or litigation by OFHEO involving the Enterprise or an employee, or otherwise has actual knowledge that an issue is subject to such an investigation, enforcement proceeding or litigation, shall notify immediately the legal department of the Enterprise and shall retain any records that may be relevant in any way to such investigation, enforcement proceeding, or litigation.

(c) *Method of record retention.* The record retention program of an Enterprise shall address the method by which the Enterprise will retain records during a record hold. Specifically, the program shall describe the method for the continued preservation of electronic records, including e-mails, and the conversion of records from paper to electronic format as well as any alternative storage method.

(d) *Access to and retrieval of records.* The record retention program of an Enterprise shall ensure access to and retrieval of records by the Enterprise and access, upon request, by OFHEO, during a record hold. Such access shall be by reasonable means, consistent with the nature and availability of the records and existing information technology.

§§ 1732.8–1732.9 [Reserved]

Subpart C—Supervisory Action

§ 1732.10 Supervisory action.

(a) *Supervisory action.* Failure by an Enterprise to comply with this part may subject the Enterprise or the board members, officers, or employees thereof to supervisory action by OFHEO under the Act, including but not limited to cease-and-desist proceedings, temporary cease-and-desist proceedings, and civil money penalties.

(b) *No limitation of authority.* This part does not limit or restrict the authority of OFHEO to act under its safety and soundness mandate, in accordance with the Act. Such authority includes, but is not limited to, conducting examinations, requiring reports and disclosures, and enforcing compliance with applicable laws, rules, and regulations.

PART 1750—CAPITAL

Subpart A—Minimum Capital

Sec.

1750.1 General.

1750.2 Definitions.

1750.3 Procedure and timing.

1750.4 Minimum capital requirement computation.

APPENDIX A TO SUBPART A OF PART 1750—
MINIMUM CAPITAL COMPONENTS FOR INTEREST RATE AND FOREIGN EXCHANGE RATE CONTRACTS

Subpart B—Risk-Based Capital

1750.10 General.

1750.11 Definitions.

1750.12 Procedures and timing.

1750.13 Risk-based capital level computation.

APPENDIX A TO SUBPART B OF PART 1750—
RISK-BASED CAPITAL TEST METHODOLOGY AND SPECIFICATIONS

APPENDIX B TO SUBPART B OF PART 1750 [RESERVED]

AUTHORITY: 12 U.S.C. 4513, 4514, 4611, 4612, 4614, 4615, 4618.

Subpart A—Minimum Capital

§ 1750.1 General.

The regulation contained in this subpart A sets forth the methodology for computing the minimum capital re-

quirement for each Enterprise. The board of directors of each Enterprise is responsible for ensuring that the Enterprise maintains capital at a level that is sufficient to ensure the continued financial viability of the Enterprise and that equals or exceeds the minimum capital requirement contained in this subpart A.

§ 1750.2 Definitions.

For purposes of this subpart A, the following definitions shall apply:

Affiliate means any entity that controls, is controlled by, or is under common control with, an Enterprise, except as otherwise provided by the Director.

Commitment means any contractual, legally binding agreement that obligates an Enterprise to purchase or to securitize mortgages.

Core Capital—(1) Means the sum of (as determined in accordance with generally accepted accounting principles)—

(i) The par or stated value of outstanding common stock;

(ii) The par or stated value of outstanding perpetual, noncumulative preferred stock;

(iii) Paid-in capital; and

(iv) Retained earnings; and

(2) Does not include debt instruments or any amounts the Enterprise could be required to pay at the option of an investor to retire capital instruments.

Director means the Director of OFHEO.

Enterprise means the Federal National Mortgage Association and any affiliate thereof or the Federal Home Loan Mortgage Corporation and any affiliate thereof.

Foreign exchange rate contracts—

(1) Means cross-currency interest rate swaps, forward foreign exchange contracts, currency options purchased (including currency options purchased over-the-counter), and any other instrument that gives rise to similar credit risks; and

(2) Does not mean foreign exchange rate contracts with an original maturity of 14 calendar days or less and foreign exchange rate contracts traded on exchanges that require daily payment of variation margins.

Interest rate contracts—

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(1) Means single currency interest rate swaps, basis swaps, forward rate agreements, interest rate options purchased (including caps, collars, and floors purchased), over-the-counter options purchased, and any other instrument that gives rise to similar credit risks (including when-issued securities and forward deposits accepted); and

(2) Does not mean such instruments traded on exchanges that require daily payment of variation margins.

Mortgage-backed security means a security, investment, or substantially equivalent instrument that represents an interest in a pool of loans secured by mortgages or deeds of trust where the principal or interest payments to the investor in the security or substantially equivalent instrument are guaranteed or effectively guaranteed by an Enterprise.

Multifamily credit enhancement means any guarantee, pledge, purchase arrangement, or other obligation or commitment provided or entered into by an Enterprise with respect to multifamily mortgages to provide credit enhancement, liquidity, interest rate support, and other guarantees and enhancements for revenue bonds issued by a state or local governmental unit (including a housing finance agency) or other bond issuer.

1992 Act means the Federal Housing Enterprises Financial Safety and Soundness Act of 1992, found at Title XIII of the Housing and Community Development Act of 1992, Pub. L. 102-550, 12 U.S.C. 4501 *et seq.*

Notional amount means the face value of the underlying financial instrument(s) on which an interest rate or foreign exchange rate contract is based.

Off-balance sheet obligation means a binding agreement, contract, or similar arrangement that requires or may require future payment(s) in money or kind by another party to an Enterprise, or that effectively guarantees all or part of such payment(s) to third parties (including commitments), where such agreement or contract is a source of credit risk that is not included on its balance sheet.

OFHEO means the Office of Federal Housing Enterprise Oversight.

Other off-balance sheet obligations means all off-balance sheet obligations of an Enterprise that are not mortgage-backed securities or substantially equivalent instruments and that are not resecuritized mortgage-backed securities, such as real estate mortgage investment conduits or similar resecuritized instruments.

Perpetual, noncumulative preferred stock means preferred stock that—

(1) Does not have a maturity date;

(2) Provides the issuer the ability and the legal right to eliminate dividends and does not permit the accruing or payment of impaired dividends;

(3) Cannot be redeemed at the option of the holder; and

(4) Has no other provisions that will require future redemption of the issue, in whole or in part, or that will reset the dividend periodically based, in whole or in part, on the Enterprise's current credit standing, such as auction rate, money market, or remarketable preferred stock, or that may cause the dividend to increase to a level that could create an incentive for the issuer to redeem the instrument, such as exploding rate stock.

Qualifying collateral means cash on deposit; securities issued or guaranteed by the central governments of the OECD-based group of countries,¹

¹The OECD-based group of countries comprises full members of the Organization for Economic Cooperation and Development (OECD) regardless of entry date, as well as countries that have concluded special lending arrangements with the International Monetary Fund (IMF) associated with the IMF's General Arrangements to Borrow, but excludes any country that has rescheduled its external sovereign debt within the previous 5 years. A rescheduling of external sovereign debt generally would include any renegotiation of terms arising from a country's mobility or unwillingness to meet its external debt service obligations, but generally not include any renegotiation to allow the borrower to take advantage of a decline in interest rate or other change in market conditions. As of November 1995, the OECD countries included the following countries: Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Greece, Iceland, Ireland, Italy, Japan, Luxembourg, Mexico, the Netherlands, New Zealand, Norway, Portugal, Spain, Sweden, Switzerland, Turkey, the United Kingdom, and the United

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United States Government agencies, or United States Government-sponsored agencies; and securities issued by multilateral lending institutions or regional development banks.

§ 1750.3 Procedure and timing.

(a) Each Enterprise shall file with the Director a minimum capital report each quarter or at such other times as the Director requires, in his or her sole discretion. The report shall contain the information that responds to all of the items required by OFHEO in written instructions to the Enterprise, including, but not limited to:

(1) Estimate of the minimum capital requirement;

(2) Estimate of core capital coverage or shortfall relative to the estimated minimum capital requirement;

(3) Such other information as may be required by the Director.

(b) The quarterly minimum capital report shall be submitted not later than April 30, July 30, October 30, and January 30 of each year.

(c) Each minimum capital report shall be submitted in writing and in such other format as may be required by the Director.

(d) In the event an Enterprise makes an adjustment to its financial statements for a quarter or a date for which the information was requested, which would cause an adjustment to a minimum capital report, the Enterprise shall file with the Director an amended minimum capital report not later than 3 business days after the date of such adjustment.

(e) Each minimum capital report or any amended minimum capital report shall contain a declaration by an officer authorized by the board of directors of the Enterprise to make such a declaration, including, but not limited to a president, vice president, or treasurer, that the report is true and correct to the best of such officer's knowledge and belief.

States; and Saudi Arabia has concluded special lending arrangements with the IMF associated with the IMF's General Arrangements to Borrow.

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§ 1750.4 Minimum capital requirement computation.

(a) The minimum capital requirement for each Enterprise shall be computed by adding the following amounts:

(1) 2.50 percent times the aggregate on-balance sheet assets of the Enterprise;

(2) 0.45 percent times the unpaid principal balance of mortgage-backed securities and substantially equivalent instruments that were issued or guaranteed by the Enterprise;

(3) 0.45 percent of 50 percent of the average dollar amount of commitments outstanding each quarter over the preceding four quarters;

(4) 0.45 percent of the outstanding principal amount of bonds with multifamily credit enhancements;

(5) 0.45 percent of the dollar amount of sold portfolio remittances pending;

(6)(i) 3.00 percent of the credit equivalent amount of interest rate contracts and foreign exchange rate contracts, except to the extent of the current market value of posted qualifying collateral, computed in accordance with appendix A to this subpart;

(ii) 1.50 percent of the market value of qualifying collateral posted to secure interest rate and foreign exchange rate contracts, not to exceed the credit equivalent amount of such contracts, computed in accordance with appendix A to this subpart; and

(7) 0.45 percent of the outstanding amount, credit equivalent amount, or other measure determined appropriate by the Director, of other off-balance sheet obligations (excluding commitments, multifamily credit enhancements, sold portfolio remittances pending, and interest rate contracts and foreign exchange rate contracts), except as adjusted by the Director to reflect differences in the credit risk of such obligations in relation to mortgage-backed securities.

(b) Any asset or financial obligation that is properly classifiable in more than one of the categories enumerated in paragraphs (a) (1) through (7) of this section shall be classified in the category that yields the highest minimum capital requirement.

(c) As used in this section, the term "preceding four quarters" means the last day of the quarter just ended (or

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the date for which the minimum capital report is filed, if different), and the three preceding quarter-ends.

APPENDIX A TO SUBPART A OF PART 1750—MINIMUM CAPITAL COMPONENTS FOR INTEREST RATE AND FOREIGN EXCHANGE RATE CONTRACTS

1. The minimum capital components for interest rate and foreign exchange rate contracts are computed on the basis of the credit equivalent amounts of such contracts. Credit equivalent amounts are computed for each of the following off-balance sheet interest rate and foreign exchange rate contracts:

a. Interest Rate Contracts

- i. Single currency interest rate swaps.
- ii. Basis swaps.
- iii. Forward rate agreements.
- iv. Interest rate options purchased (including caps, collars, and floors purchased).
- v. Any other instrument that gives rise to similar credit risks (including when-issued securities and forward deposits accepted).

b. Foreign Exchange Rate Contracts

- i. Cross-currency interest rate swaps.
- ii. Forward foreign exchange rate contracts.
- iii. Currency options purchased.
- iv. Any other instrument that gives rise to similar credit risks.

2. Foreign exchange rate contracts with an original maturity of 14 calendar days or less and foreign exchange rate contracts traded on exchanges that require daily payment of variation margins are excluded from the minimum capital requirement computation. Over-the-counter options purchased, however, are included and treated in the same way as the other interest rate and foreign exchange rate contracts.

3. Calculation of Credit Equivalent Amounts

a. The minimum capital components for interest rate and foreign exchange rate contracts are computed on the basis of the credit equivalent amounts of such contracts. The credit equivalent amount of an off-balance sheet interest rate and foreign exchange rate contract that is not subject to a qualifying bilateral netting contract in accordance with this appendix A is equal to the sum of the current exposure (sometimes referred to as the replacement cost) of the contract and an estimate of the potential future credit exposure over the remaining life of the contract.

b. The current exposure is determined by the mark-to-market value of the contract. If the mark-to-market value is positive, then the current exposure is the mark-to-market value. If the mark-to-market value is zero or negative, then the current exposure is zero. Mark-to-market values are measured in

United States dollars, regardless of the currency or currencies specified in the contract, and should reflect changes in the relevant rates, as well as counterparty credit quality.

c. The potential future credit exposure of a contract, including a contract with a negative mark-to-market value, is estimated by multiplying the notional principal amount of the contract by a credit conversion factor. The effective rather than the apparent or stated notional amount must be used in this calculation. The credit conversion factors are:

Remaining maturity	Interest rate contracts (percent)	Foreign exchange rate contracts (percent)
1 year or less	0.0	1.0
Over 1 year	0.5	5.0

d. Because foreign exchange rate contracts involve an exchange of principal upon maturity, and foreign exchange rates are generally more volatile than interest rates, higher conversion factors have been established for foreign exchange rate contracts than for interest rate contracts.

e. No potential future credit exposure is calculated for single currency interest rate swaps in which payments are made based upon two floating rate indexes, so-called floating/floating or basis swaps. The credit exposure on these contracts is evaluated solely on the basis of their mark-to-market values.

4. Avoidance of Double Counting

In certain cases, credit exposures arising from the interest rate and foreign exchange instruments covered by this appendix A may already be reflected, in part, on the balance sheet. To avoid double counting such exposures in the assessment of capital adequacy, counterparty credit exposures arising from the types of instruments covered by this appendix A may need to be excluded from balance sheet assets in calculating the minimum capital requirement.

5. Collateral

a. The sufficiency of collateral for off-balance sheet items is determined by the market value of the collateral in relation to the credit equivalent amount. Collateral held against a netting contract is not recognized for minimum capital standard purposes unless it is legally available to support the single legal obligation created by the netting contract. Excess collateral held against one contract or a group of contracts for which a recognized netting agreement exists may not be considered.

b. The only forms of collateral that are formally recognized by the minimum capital standard framework are cash on deposit; securities issued or guaranteed by the central

governments of the OECD-based group of countries, United States Government agencies, or United States Government-sponsored agencies; and securities issued by multilateral lending institutions or regional development banks.

6. Netting

a. For purposes of this appendix A, netting refers to the offsetting of positive and negative mark-to-market values in the determination of a current exposure to be used in the calculation of a credit equivalent amount. Any legally enforceable form of bilateral netting (that is, netting with a single counterparty) of interest rate and foreign exchange rate contracts is recognized for purposes of calculating the credit equivalent amount provided that the following criteria are met:

i. Netting must be accomplished under a written netting contract that creates a single legal obligation, covering all included individual contracts, with the effect that the Enterprise would have a claim to receive, or obligation to pay, only the net amount of the sum of the positive and negative mark-to-market values on included individual contracts in the event that a counterparty, or a counterparty to whom the contract has been validly assigned, fails to perform due to default, insolvency, liquidation, or similar circumstances.

ii. The Enterprise must obtain a written and reasoned legal opinion(s) representing that in the event of a legal challenge—including one resulting from default, insolvency, liquidation, or similar circumstances—the relevant court and administrative authorities would find the Enterprise's exposure to be such a net amount under—

A. The law of the jurisdiction in which the counterparty is chartered or the equivalent location in the case of noncorporate entities, and if a branch of the counterparty is involved, then also under the law of the jurisdiction in which the branch is located;

B. The law that governs the individual contracts covered by the netting contract; and

C. The law that governs the netting contract.

iii. The Enterprise must establish and maintain procedures to ensure that the legal characteristics of netting contracts are kept under review in the event of possible changes in relevant law.

iv. The Enterprise must maintain in its files documentation adequate to support the netting of rate contracts, including a copy of the bilateral netting contract and necessary legal opinions.

b. A contract containing a walkaway clause is not eligible for netting for purposes of calculating the credit equivalent amount.¹

c. By netting individual contracts for the purpose of calculating its credit equivalent amount, the Enterprise represents that it has met the requirements of this appendix A and all the appropriate documents are in the Enterprise's files and available for inspection by OFHEO. OFHEO may determine that an Enterprise's files are inadequate or that a netting contract, or any of its underlying individual contracts, may not be legally enforceable under any one of the bodies of law described in this appendix A. If such a determination is made, the netting contract may be disqualified from recognition for minimum capital standard purposes or underlying individual contracts may be treated as though they are not subject to the netting contract.

d. The credit equivalent amount of interest rate and foreign exchange rate contracts that are subject to a qualifying bilateral netting contract is calculated by adding the current exposure of the netting contract and the sum of the estimates of the potential future credit exposures on all individual contracts subject to the netting contract, estimated in accordance with paragraph 3 of this appendix A. Offsetting contracts in the same currency maturing on the same date will have lower potential future exposure as well as lower current exposure. Therefore, for purposes of calculating potential future credit exposure to a netting counterparty for foreign exchange rate contracts and other similar contracts in which notional principal is equivalent to cash flows, total notional principal is defined as the net receipts falling due on each value date in each currency.

e. The current exposure of the netting contract is determined by summing all positive and negative mark-to-market values of the individual contracts included in the netting contract. If the net sum of the mark-to-market values is positive, then the current exposure of the netting contract is equal to that sum. If the net sum of the mark-to-market values is zero or negative, then the current exposure of the netting contract is zero. OFHEO may determine that a netting contract qualifies for minimum capital standard netting treatment even though certain individual contracts may not qualify. In such instances, the nonqualifying contracts should

¹ A walkaway clause is a provision in a netting contract that permits a non-defaulting counterparty to make lower payments than it would make otherwise under the contract, or no payment at all, to a defaulter or to the estate of a defaulter, even if the defaulter or the estate of the defaulter is a net creditor under the contract.

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be treated as individual contracts that are not subject to the netting contract.

f. In the event a netting contract covers contracts that are normally excluded from the minimum capital requirement computation—for example, foreign exchange rate contracts with an original maturity of 14 calendar days or less, or instruments traded on exchanges that require daily payment of variation margin—an Enterprise may elect consistently either to include or exclude all mark-to-market values of such contracts when determining net current exposure.

Subpart B—Risk-Based Capital

SOURCE: 66 FR 47806, Sept. 13, 2001, unless otherwise noted.

§ 1750.10 General.

The regulation contained in this subpart B establishes the methodology for computing the risk-based capital level for each Enterprise. The board of directors of each Enterprise is responsible for ensuring that the Enterprise maintains total capital at a level that is sufficient to ensure the continued financial viability of the Enterprise and is equal to or exceeds the risk-based capital level computed pursuant to this subpart B.

§ 1750.11 Definitions.

Except where a term is explicitly defined differently in this subpart, all terms defined at §1750.2 of subpart A of this part shall have the same meanings for purposes of this subpart. For purposes of subpart B of this part, the following definitions shall apply:

(a) *Benchmark loss experience* means the rates of default and severity for mortgage loans that—

(1) Were originated during a period of two or more consecutive calendar years in contiguous areas that together contain at least five percent of the population of the United States, and

(2) Experienced the highest loss rate for any period of such duration in comparison with the loans originated in any other contiguous areas that together contain at least five percent of the population of the United States.

(b) *Constant maturity Treasury yield* means the constant maturity Treasury yield, published by the Board of Governors of the Federal Reserve System.

(c) *Contiguous areas* means all the areas within a state or a group of two or more states sharing common borders. “Sharing common borders” does not mean meeting at a single point. Colorado, for example, is contiguous with New Mexico, but not with Arizona.

(d) *Credit risk* means the risk of financial loss to an Enterprise from non-performance by borrowers or other obligors on instruments in which an Enterprise has a financial interest, or as to which the Enterprise has a financial obligation.

(e) *Default rate* of a given group of loans means the ratio of the aggregate original principal balance of the defaulted loans in the group to the aggregate original principal balance of all loans in the group.

(f) *Defaulted loan* means a loan that, within ten years following its origination:

- (1) Resulted in pre-foreclosure sale,
- (2) Completed foreclosure,
- (3) Resulted in the acquisition of real estate collateral, or
- (4) Otherwise resulted in a credit loss to an Enterprise.

(g) *Financing costs* of property acquired through foreclosure means the product of:

- (1) The number of years (including fractions) of the period from the completion of foreclosure through disposition of the property,
- (2) The average of the Enterprises’ short-term funding rates, and
- (3) The unpaid principal balance at the time of foreclosure.

(h) *Interest rate risk* means the risk of financial loss due to the sensitivity of earnings and net worth of an Enterprise to changes in interest rates.

(i) *Loss* on a defaulted loan means:

(1) With respect to a loan in category 1, 2, or 3 of the definition of defaulted loan the difference between:

(i) The sum of the principal and interest owed when the borrower lost title to the property securing the mortgage; financing costs through the date of property disposition; and cash expenses incurred during the foreclosure process, the holding period for real estate collateral acquired as a result of default, and the property liquidation process; and

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(ii) The sum of the property sales price and any other liquidation proceeds (except those resulting from private mortgage insurance proceeds or other third-party credit enhancements).

(2) With respect to defaulted loans not in categories 1, 2, or 3, the amount of the financial loss to the Enterprise.

(j) *Mortgage* means any loan secured by such classes of liens as are commonly given or are legally effective to secure advances on, or the unpaid purchase price of, real estate under the laws of the State in which the real estate is located; or a manufactured house that is personal property under the laws of the State in which the manufactured house is located, together with the credit instruments, if any, secured thereby, and includes interests in mortgages.

(k) *Seasoning* means the change over time in the ratio of the unpaid principal balance of a mortgage to the value of the property by which such mortgage loan is secured.

(l) *Severity rate* for any group of defaulted loans means the aggregate losses on all loans in that group divided by the aggregate original principal balances of those loans.

(m) *Stress period* means a hypothetical ten-year period immediately following the day for which capital is being measured, which is a period marked by the severely adverse economic circumstances defined in 12 CFR 1750.13 and Appendix A to this subpart.

(n) *Total capital* means, with respect to an Enterprise, the sum of the following:

- (1) The core capital of the Enterprise;
- (2) A general allowance for foreclosure losses, which—

- (i) Shall include an allowance for portfolio mortgage losses, an allowance for non-reimbursable foreclosure costs on government claims, and an allowance for liabilities reflected on the balance sheet for the Enterprise for estimated foreclosure losses on mortgage-backed securities; and
 - (ii) Shall not include any reserves of the Enterprise made or held against specific assets.
- (3) Any other amounts from sources of funds available to absorb losses incurred by the Enterprise, that the Di-

rector by regulation determines are appropriate to include in determining total capital.

(o) *Type of mortgage product* means a classification of one or more mortgage products, as established by the Director, that have similar characteristics from each set of characteristics under the paragraphs (o)(1) through (o)(7) of this section:

(1) The property securing the mortgage is—

- (i) A residential property consisting of 1 to 4 dwelling units; or

- (ii) A residential property consisting of more than 4 dwelling units.

(2) The interest rate on the mortgage is—

- (i) Fixed; or

- (ii) Adjustable.

(3) The priority of the lien securing the mortgage is—

- (i) First; or

- (ii) Second or other.

(4) The term of the mortgage is—

- (i) 1 to 15 years;

- (ii) 16–30 years; or

- (iii) More than 30 years.

(5) The owner of the property is—

- (i) An owner-occupant; or

- (ii) An investor.

(6) The unpaid principal balance of the mortgage—

- (i) Will amortize completely over the term of the mortgage, and will not increase significantly at any time during the term of the mortgage;

- (ii) Will not amortize completely over the term of the mortgage, and will not increase significantly at any time during the term of the mortgage; or

- (iii) May increase significantly at some time during the term of the mortgage.

(7) Any other characteristics of the mortgage, as specified in Appendix A to this subpart.

§ 1750.12 Procedures and timing.

(a) Each Enterprise shall file with the Director a Risk-Based Capital Report each quarter, and at such other times as the Director may require, in his or her discretion. The report shall contain the information required by the Director in the instructions to the Risk-Based Capital Report in the format or media specified therein and

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such other information as may be required by the Director.

(b) The quarterly Risk-Based Capital Report shall contain information for the last day of the quarter and shall be submitted not later than 30 days after the end of the quarter. Reports required by the Director other than quarterly reports shall be submitted within such time period as the Director shall specify.

(c) When an Enterprise contemplates entering a new activity, as the term is defined in section 3.11 of Appendix A to this subpart, the Enterprise shall notify the Director as soon as possible while the transaction or activity is under consideration, but in no event later than 5 calendar days after settlement or closing. The Enterprises shall provide to the Director such information regarding the activity as the Director may require to determine a stress test treatment. OFHEO will inform the Enterprise as soon as possible thereafter of the proposed stress test treatment of the new activity. In addition, the notice of proposed capital classification required by §1777.21 of this chapter will inform the Enterprise of the capital treatment of such new activity used in the determination of the risk-based capital requirement.

(d) If an Enterprise discovers that a Risk-Based Capital Report previously filed with OFHEO contains any errors or omissions, the Enterprise shall notify OFHEO immediately of such discovery and file an amended Risk-Based Capital Report not later than three days thereafter.

(e) Each capital classification shall be determined by OFHEO on the basis of the Risk-Based Capital Report filed by the Enterprise under paragraph (a) of this section; provided that, in the event an amended Risk-Based Capital Report is filed prior to the issuance of the final notice of capital classification, the Director has the discretion to determine the Enterprise's capital classification on the basis of the amended report.

(f) Each Risk-Based Capital Report or any amended Risk-Based Capital Report shall contain a declaration by the officer who has been designated by the Board as responsible for overseeing the capital adequacy of the Enterprise that

the report is true and correct to the best of such officer's knowledge and belief.

[66 FR 47806, Sept. 13, 2001, as amended at 67 FR 19322, Apr. 19, 2002]

§ 1750.13 Risk-based capital level computation.

(a) *Risk-Based Capital Test*—OFHEO shall compute a risk-based capital level for each Enterprise at least quarterly by applying the risk-based capital test described in Appendix A to this subpart to determine the amount of total capital required for each Enterprise to maintain positive capital during the stress period. In making this determination, the Director shall take into account any appropriate distinctions among types of mortgage products, differences in seasoning of mortgages, and other factors determined appropriate by the Director in accordance with the methodology specified in Appendix A to this subpart. The stress period has the following characteristics:

(1) *Credit risk*—With respect to mortgages owned or guaranteed by the Enterprise and other obligations of the Enterprise, losses occur throughout the United States at a rate of default and severity reasonably related, in accordance with Appendix A to this subpart, to the benchmark loss experience.

(2) *Interest rate risk*—(i) *In general*. Interest rates decrease as described in paragraph (a)(2)(ii) of this section or increase as described in paragraph (a)(2)(iii) of this section, whichever would require more capital in the stress test for the Enterprise. Appendix A to this subpart contains a description of the methodology applied to implement the interest rate scenarios described in paragraphs (a)(2)(ii) and (iii) of this section.

(ii) *Decreases*. The 10-year constant maturity Treasury yield decreases during the first year of the stress period and remains at the new level for the remainder of the stress period. The yield decreases to the lesser of—

(A) 600 basis points below the average yield during the 9 months immediately preceding the stress period, or

(B) 60 percent of the average yield during the 3 years immediately preceding the stress period, but in no case to a yield less than 50 percent of the

average yield during the 9 months immediately preceding the stress period.

(iii) *Increases.* The 10-year constant maturity Treasury yield increases during the first year of the stress period and will remain at the new level for the remainder of the stress period. The yield increases to the greater of—

(A) 600 basis points above the average yield during the 9 months immediately preceding the stress period, or

(B) 160 percent of the average yield during the 3 years immediately preceding the stress period, but in no case to a yield greater than 175 percent of the average yield during the 9 months immediately preceding the stress period.

(iv) *Different terms to maturity.* Yields of Treasury instruments with terms to maturity other than 10 years will change relative to the 10-year constant maturity Treasury yield in patterns and for durations that are reasonably related to historical experience and are judged reasonable by the Director. The methodology used by the Director to adjust the yields of those other instruments is specified in Appendix A to this subpart.

(v) *Large increases in yields.* If the 10-year constant maturity Treasury yield is assumed to increase by more than 50 percent over the average yield during the 9 months immediately preceding the stress period, the Director shall adjust the losses resulting from the conditions specified in paragraph (a)(2)(iii) of this section to reflect a correspondingly higher rate of general price inflation. The method of such adjustment by the Director is specified in Appendix A to this subpart.

(3) *New business.* Any contractual commitments of the Enterprise to purchase mortgages or issue securities will be fulfilled. The characteristics of resulting mortgages purchased, securities issued, and other financing will be consistent with the contractual terms of such commitments, recent experience, and the economic characteristics of the stress period, as more fully specified in Appendix A to this subpart. No other purchases of mortgages shall be assumed.

(4) *Other activities.* Losses or gains on other activities, including interest rate and foreign exchange hedging activi-

ties, shall be determined by the Director, in accordance with Appendix A to this subpart and on the basis of available information, to be consistent with the stress period.

(5) *Consistency.* Characteristics of the stress period other than those specifically set forth in paragraph (a) of this section, such as prepayment experience and dividend policies, will be determined by the Director, in accordance with Appendix A to this subpart, on the basis of available information, to be most consistent with the stress period.

(b) *Risk-Based Capital Level.* The risk-based capital level of an Enterprise, to be used in determining the appropriate capital classification of each Enterprise, as required by section 1364 of the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (12 U.S.C. 4614), shall be equal to the sum of the following amounts:

(1) *Credit and Interest Rate Risk.* The amount of total capital determined by applying the risk-based capital test under paragraph (a) of this section to the Enterprise.

(2) *Management and Operations Risk.* To provide for management and operations risk, 30 percent of the amount of total capital determined by applying the risk-based capital test under paragraph (a) of this section to the Enterprise.

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1.0 IDENTIFICATION OF THE BENCHMARK LOSS EXPERIENCE

OFHEO will use the definitions, data, and methodology described below to identify the Benchmark Loss Experience.

1.1 Definitions

The terms defined in the Glossary to this Appendix shall apply for this Appendix.

1.2 Data

[a] OFHEO identifies the Benchmark Loss Experience (BLE) using historical loan-level data required to be submitted by each of the two Enterprises. OFHEO's analysis is based entirely on the data available through 1995 on conventional, 30-year, fixed-rate loans secured by first liens on single-unit, owner-occupied, detached properties. For this purpose, detached properties are defined as single family properties excluding condominiums, planned urban developments, and cooperatives. The data includes only loans that were purchased by an Enterprise within 12 months after loan origination and loans for which the Enterprise has no recourse to the lender.

[b] OFHEO organizes the data from each Enterprise to create two substantially consistent data sets. OFHEO separately analyzes default and severity data from each Enterprise. Default rates are calculated from loan records meeting the criteria specified above. Severity rates are calculated from the subset of defaulted loans for which loss data are available.

1.3 Procedures

[a] Cumulative ten-year default rates for each combination of states and origination years (state/year combination) that OFHEO examines are calculated for each Enterprise by grouping all of the Enterprise's loans originated in that combination of states and years. For origination years with less than ten-years of loss experience, cumulative-to-date default rates are used. The two Enterprise default rates are averaged, yielding an "average default rate" for that state/year combination.

[b] An "average severity rate" for each state/year combination is determined in the same manner as the average default rate. For each Enterprise, the aggregate severity rate is calculated for all loans in the relevant state/year combination and the two Enterprise severity rates are averaged.

[c] The "loss rate" for any state/year combination examined is calculated by multiplying the average default rate for that state/year combination by the average severity rate for that combination.

[d] The rates of default and Loss Severity of loans in the state/year combination containing at least two consecutive origination years and contiguous areas with a total pop-

ulation equal to or greater than five percent of the population of the United States with the highest loss rate constitutes the Benchmark Loss Experience.

2.0 IDENTIFICATION OF A NEW BENCHMARK LOSS EXPERIENCE

OFHEO will periodically monitor available data and reevaluate the Benchmark Loss Experience using the methodology set forth in this Appendix. Using this methodology, OFHEO may identify a new Benchmark Loss Experience that has a higher rate of loss than the Benchmark Loss Experience identified at the time of the issuance of this regulation. In the event such a Benchmark Loss Experience is identified, OFHEO may incorporate the resulting higher loss rates in the Stress Test.

3.0 COMPUTATION OF THE RISK-BASED CAPITAL REQUIREMENT

3.1 Data

3.1.1 Introduction

[a] The Stress Test requires data on all of an Enterprise's assets, liabilities, stockholders equity, accounting entries, operations and off-balance sheet obligations, as well as economic factors that affect them: interest rates, house prices, rent growth rates, and vacancy rates. The Enterprises are responsible for compiling and aggregating data on at least a quarterly basis into a standard format called the Risk-Based Capital Report (RBC Report). Each Enterprise is required to certify that the RBC Report submission is complete and accurate. Data on economic factors, such as interest rates, are compiled from public sources. The Stress Test uses proprietary and public data directly, and also uses values derived from such data in the form of constants or default values. (See Table 3-1, Sources of Stress Test Input Data.) Data fields from each of these sources for Stress Test computations are described in the following tables and in each section of this Appendix.

[b] The RBC Report includes information for all the loans owned or guaranteed by an Enterprise, as well as securities and derivative contracts, the dollar balances of these instruments and obligations, as well as all characteristics that bear on their behavior under stress conditions. As detailed in the RBC Report, data are required for all the following categories of instruments and obligations:

- Mortgages owned by or underlying mortgage-backed securities (MBS) issued by the Enterprises (whole loans)
- Mortgage-related securities
- Nonmortgage related securities, whether issued by an Enterprise, (e.g., debt) or held as investments
- Derivative contracts

- Other off-balance sheet guarantees (e.g., guarantees of private-issue securities).

TABLE 3-1—SOURCES OF STRESS TEST INPUT DATA

Section of this Appendix	Table	Data Source(s) R = RBC Report P = Public Data F = Fixed Values			Intermediate Outputs
		R	P	F	
3.1.3, Public Data	3-19, Stress Test Single Family Quarterly House Price Growth Rates			F	
	3-20, Multifamily Monthly Rent Growth and Vacancy Rates			F	
3.2.2, Commitments Inputs	Characteristics of securitized single family loans originated and delivered within 6 months prior to the Start of the Stress Test	R			3.3.4, Interest Rates Outputs
3.2.3, Commitments Procedures	3-25, Monthly Deliveries as a Percentage of Commitments Outstanding (MDP)			F	
3.3.2, Interest Rates Inputs	3-18, Interest Rate and Index Inputs		P		
3.3.3, Interest Rates Procedures	3-26, CMT Ratios to the Ten-Year CMT			F	
3.4.2, Property Valuation Inputs	3-28, Property Valuation Inputs				3.1.3, Public Data 3.3.4, Interest Rates Outputs
3.5.3, Counterparty Defaults Procedures	3-30, Rating Agencies Mappings to OFHEO Ratings Categories		P		
	3-31, Stress Test Maximum Haircut by Ratings Classification			F	
3.6.3.3.2, Mortgage Amortization Schedule Inputs	3-32, Loan Group Inputs for Mortgage Amortization Calculation				3.3.4, Interest Rates Outputs
3.6.3.4.2, Single Family Default and Prepayment Inputs	3-34, Single Family Default and Prepayment Inputs	R		F	3.6.3.3.4, Mortgage Amortization Schedule Outputs
3.6.3.4.3.3, Prepayment and Default Rates and Performance Fractions	3-35, Coefficients for Single Family Default and Prepayment Explanatory Variables			F	
3.6.3.5.2, Multifamily Default and Prepayment Inputs	3-38, Loan Group Inputs for Multifamily Default and Prepayment Calculations	R		F	
3.6.3.5.3.3, Default and Prepayment Rates and Performance Fractions	3-39, Explanatory Variable Coefficients for Multifamily Default			F	3.6.3.3.4, Mortgage Amortization Schedule Outputs

TABLE 3–1—SOURCES OF STRESS TEST INPUT DATA—Continued

Section of this Appendix	Table	Data Source(s) R = RBC Report P = Public Data F = Fixed Values			Intermediate Outputs
		R	P	F	
3.6.3.6.2.6, Single Family Gross Loss Severity Inputs	3–42, Loan Group inputs for Gross Loss Severity			F	3.3.4, Interest Rates Outputs 3.6.3.3.4, Mortgage Amortization Schedule Outputs 3.6.3.4.4, Single Family Default and Prepayment Outputs
3.6.3.6.3.6, Multifamily Gross Loss Severity Inputs	3–44, Loan Group Inputs for Multifamily Gross Loss Severity			F	3.3.4, Interest Rates Outputs 3.6.3.3.4, Mortgage Amortization Schedule Outputs
3.6.3.6.4.8, Mortgage Credit Enhancement Inputs	3–46, CE Inputs for each Loan Group	R			3.6.3.3.4, Mortgage Amortization Schedule Outputs 3.6.3.4.4, Single Family Default and Prepayment Outputs 3.6.3.5.4, Multifamily Default and Prepayment Outputs 3.6.3.6.2.3, Single Family Gross Loss Severity Outputs 3.6.3.6.3.3, Multifamily Gross Loss Severity Outputs
	3–47, Inputs for each Distinct CE Combination (DCC)	R			
3.6.3.7.2, Stress Test Whole Loan Cash Flow Inputs	3–51, Inputs for Final Calculation of Stress Test Whole Loan Cash Flows	R			3.3.4, Interest Rates Outputs 3.6.3.3.4, Mortgage Amortization Schedule Outputs 3.6.3.4.4, Single Family Default and Prepayment Outputs 3.6.3.5.4, Multifamily Default and Prepayment Outputs 3.6.3.6.5.6, Single Family and Multifamily Net Loss Severity Outputs
3.6.3.8.2, Whole Loan Accounting Flows Inputs	3–54, Inputs for Whole Loan Accounting Flows	R			3.6.3.7.4, Stress Test Whole Loan Cash Flow Outputs
3.7.2, Mortgage-Related Securities Inputs	3–56, RBC Report Inputs for Single Class MBS Cash Flows	R			
	3–57, RBC Report Inputs for Multi-Class and Derivative MBS Cash Flows	R			
	3–58, RBC Report Inputs for MRBs and Derivative MBS Cash Flows	R			
3.8.2, Nonmortgage Instrument Inputs	3–66, Input Variables for Nonmortgage Instrument Cash flows	R			

TABLE 3-1—SOURCES OF STRESS TEST INPUT DATA—Continued

Section of this Appendix	Table	Data Source(s) R = RBC Report P = Public Data F = Fixed Values			Intermediate Outputs
		R	P	F	
3.9.2, Alternative Modeling Treatments Inputs	3-70, Alternative Modeling Treatment Inputs	R			
3.10.2, Operations, Taxes, and Accounting Inputs	3-71, Operations, Taxes, and Accounting Inputs	R			3.3.4, Interest Rates Outputs 3.6.3.7.4, Stress Test Whole Loan Cash Flow Outputs 3.7.4, Mortgage-Related Securities Outputs 3.8.4, Nonmortgage Instrument Outputs
3.12.2, Risk-Based Capital Requirement Inputs		R			3.3.4, Interest Rates Outputs 3.9.4, Alternative Modeling Treatments Outputs 3.10.4, Operations, Taxes, and Accounting Outputs

3.1.2 Risk-Based Capital Report

The Risk-Based Capital Report is comprised of information on whole loans, mortgage-related securities, nonmortgage instruments (including liabilities and derivatives), and accounting items (including off-balance sheet guarantees). In addition to their reported data, the Enterprises may report scale factors in order to reconcile this reported data with their published financials (see section 3.10.2[b] of this Appendix). If so, specific data items, as indicated, are adjusted by appropriate scale factors before any calculations occur.

3.1.2.1 Whole Loan Inputs

[a] Whole loans are individual single family or multifamily mortgage loans. The Stress Test distinguishes between whole loans that the Enterprises hold in their investment portfolios (retained loans) and those that underlie mortgage-backed securities (sold loans). Consistent with Table 3-2, Whole Loan Classification Variables, each Enterprise aggregates the data for loans with similar portfolio (retained or sold), risk, and product characteristics. The characteristics of these loan groups determine rates of mortgage Default, Prepayment and Loss Severity and cash flows.

[b] The characteristics that are the basis for loan groups are called “classification variables” and reflect categories, e.g., fixed interest rate versus floating interest rate, or identify a value range, e.g., original loan-to-value (LTV) ratio greater than 80 percent and less than or equal to 90 percent.

[c] All loans with the same values for each of the relevant classification variables included in 3-2 (and where applicable 3-3 and 3-4) comprise a single loan group. For example, one loan group includes all loans with the following characteristics:

- Single family
- Sold portfolio
- 30-year fixed rate conventional loan
- Mortgage age greater than or equal to 36 months and less than 48 months
- Original LTV greater than 75 percent and less than or equal to 80 percent
- Current mortgage interest rate class greater than or equal to six percent and less than seven percent
- Secured by property located in the East North Central Census Division
- Relative loan size greater than or equal to 75 percent and less than 100 percent of the average for its state and origination year.

TABLE 3–2—WHOLE LOAN CLASSIFICATION VARIABLES

Variable	Description	Range
Reporting Date	The last day of the quarter for the loan group activity that is being reported to OFHEO	YYYY0331 YYYY0630 YYYY0930 YYYY1231
Enterprise	Enterprise submitting the loan group data	Fannie Mae Freddie Mac
Business Type	Single family or multifamily	Single family Multifamily
Portfolio Type	Retained portfolio or Sold portfolio	Retained Portfolio Sold Portfolio
Government Flag	Conventional or Government insured loan	Conventional Government
Original LTV	Assigned LTV classes based on the ratio, in percent, between the original loan amount and the lesser of the purchase price or appraised value	LTV<=60 60<LTV<=70 70<LTV<=75 75<LTV<=80 80<LTV<=90 90<LTV<=95 95<LTV<=100 100<LTV
Interest-only Flag	Indicates if the loan is currently paying interest-only. Loans that started as I/Os and are currently amortizing should be flagged as 'N'	Yes No
Current Mortgage Interest Rate	Assigned classes for the current mortgage interest rate	0.0<=Rate<4.0 4.0<=Rate<5.0 5.0<=Rate<6.0 6.0<=Rate<7.0 7.0<=Rate<8.0 8.0<=Rate<9.0 9.0<=Rate<10.0 10.0<=Rate<11.0 11.0<=Rate<12.0 12.0<=Rate<13.0 13.0<=Rate<14.0 14.0<=Rate<15.0 15.0<=Rate<16.0 Rate=>16.0
Original Mortgage Interest Rate	Assigned classes for the original mortgage interest rate	0.0<=Rate<4.0 4.0<=Rate<5.0 5.0<=Rate<6.0 6.0<=Rate<7.0 7.0<=Rate<8.0 8.0<=Rate<9.0 9.0<=Rate<10.0 10.0<=Rate<11.0 11.0<=Rate<12.0 12.0<=Rate<13.0 13.0<=Rate<14.0 14.0<=Rate<15.0 15.0<=Rate<16.0 Rate=>16.0

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TABLE 3--2—WHOLE LOAN CLASSIFICATION VARIABLES—Continued

Variable	Description	Range
Mortgage Age	Assigned classes for the age of the loan	0<=Age<=12 12<Age<=24 24<Age<=36 36<Age<=48 48<Age<=60 60<Age<=72 72<Age<=84 84<Age<=96 96<Age<=108 108<Age<=120 120<Age<=132 132<Age<=144 144<Age<=156 156<Age<=168 168<Age<=180 Age>180
Rate Reset Period	Assigned classes for the number of months between rate adjustments	Period=1 1<Period<=4 4<Period<=9 9<Period<=15 15<Period<=60 60<Period<999 Period=999 (not applicable)
Payment Reset Period	Assigned classes for the number of months between payment adjustments after the duration of the teaser rate	Period<=9 9<Period<=15 15<Period<999 Period=999 (not applicable)
ARM Index	Specifies the type of index used to determine the interest rate at each adjustment	FHLB 11th District Cost of Funds. 1 Month Federal Agency Cost of Funds. 3 Month Federal Agency Cost of Funds. 6 Month Federal Agency Cost of Funds. 12 Month Federal Agency Cost of Funds. 24 Month Federal Agency Cost of Funds. 36 Month Federal Agency Cost of Funds. 60 Month Federal Agency Cost of Funds. 120 Month Federal Agency Cost of Funds. 360 Month Federal Agency Cost of Funds. Overnight Federal Funds (Effective). 1 Week Federal Funds 6 Month Federal Funds 1 month LIBOR 3 Month LIBOR 6 Month LIBOR 12 Month LIBOR Conventional Mortgage Rate 15 Year Fixed Mortgage Rate 7 Year Balloon Mortgage Rate Prime Rate 1 Month Treasury Bill 3 Month CMT

TABLE 3–2—WHOLE LOAN CLASSIFICATION VARIABLES—Continued

Variable	Description	Range
		6 Month CMT 12 Month CMT 24 Month CMT 36 Month CMT 60 Month CMT 120 Month CMT 240 Month CMT 360 Month CMT
Cap Type Flag	Indicates if a loan group is rate-capped, payment-capped or uncapped	Payment Capped Rate Capped No periodic rate cap
OFHEO Ledger Code	OFHEO-specific General Ledger account number used in the Stress Test	Appropriate OFHEO Ledger Code based on the chart of accounts.

TABLE 3–3—ADDITIONAL SINGLE FAMILY LOAN CLASSIFICATION VARIABLES

Variable	Description	Range
Single Family Product Code	Identifies the mortgage product types for single family loans	Fixed Rate 30YR Fixed Rate 20YR Fixed Rate 15YR 5 Year Fixed Rate Balloon 7 Year Fixed Rate Balloon 10 Year Fixed Rate Balloon 15 Year Fixed Rate Balloon Adjustable Rate Step Rate ARMs Second Lien Other
Census Division	The Census Division in which the property resides. This variable is populated based on the property's state code	East North Central East South Central Middle Atlantic Mountain New England Pacific South Atlantic West North Central West South Central
Relative Loan Size	Assigned classes for the loan amount at origination divided by the simple average of the loan amount for the origination year and for the State in which the property is located. Average loan size for the appropriate quarter is provided by OFHEO based upon data from both Enterprises. It is expressed as a decimal	0<=Size<=.4 .4<Size<=.6 .6<Size<=.75 .75<Size<=1.0 1.0<Size<=1.25 1.25<Size<=1.5 Size>1.5

TABLE 3–4—ADDITIONAL MULTIFAMILY LOAN CLASSIFICATION VARIABLES

Variable	Description	Range
Multifamily Product Code	Identifies the mortgage product types for multifamily loans	Fixed Rate Fully Amortizing Adjustable Rate Fully Amortizing 5 Year Fixed Rate Balloon 7 Year Fixed Rate Balloon

TABLE 3-4—ADDITIONAL MULTIFAMILY LOAN CLASSIFICATION VARIABLES—Continued

Variable	Description	Range
		10 Year Fixed Rate Balloon 15 Year Fixed Rate Balloon Balloon ARM Other
New Book Flag	“New Book” is applied to Fannie Mae loans acquired beginning in 1988 and Freddie Mac loans acquired beginning in 1993, except for loans that were refinanced to avoid a default on a loan originated or acquired earlier	New Book Old Book
Ratio Update Flag	Indicates if the LTV and DCR were updated at origination or at Enterprise acquisition	Yes No
Current DCR	Assigned classes for the Debt Service Coverage Ratio based on the most recent annual operating statement	DCR<1.00 1.00<=DCR<1.10 1.10<=DCR<1.20 1.20<=DCR<1.30 1.30<=DCR<1.40 1.40<=DCR<1.50 1.50<=DCR<1.60 1.60<=DCR<1.70 1.70<=DCR<1.80 1.80<=DCR<1.90 1.90<=DCR<2.00 2.00<=DCR<2.50 2.50<=DCR<4.00 DCR>=4.00
Prepayment Penalty Flag	Indicates if prepayment of the loan is subject to active prepayment penalties or yield maintenance provisions	Yes No

3.1.2.1.1 Loan Group Inputs

TABLE 3-5—MORTGAGE AMORTIZATION CALCULATION INPUTS

Variable	Description
	Rate Type (Fixed or Adjustable)
	Product Type (30/20/15-Year FRM, ARM, Balloon, Government, etc.)
UPB _{ORIG}	Unpaid Principal Balance at Origination (aggregate for Loan Group)
UPB ₀	Unpaid Principal Balance at start of Stress Test (aggregate for Loan Group), adjusted by UPB scale factor.
MIR ₀	Mortgage Interest Rate for the Mortgage Payment prior to the start of the Stress Test, or Initial Mortgage Interest Rate for new loans (weighted average for Loan Group) (expressed as a decimal per annum)
PMT ₀	Amount of the Mortgage Payment (Principal and Interest) prior to the start of the Stress Test, or first Payment for new loans (aggregate for Loan Group), adjusted by UPB scale factor.

TABLE 3–5—MORTGAGE AMORTIZATION CALCULATION INPUTS—Continued

Variable	Description
AT	Original loan Amortizing Term in months (weighted average for Loan Group)
RM	Remaining term to Maturity in months (i.e., number of contractual payments due between the start of the Stress Test and the contractual maturity date of the loan) (weighted average for Loan Group)
A ₀	Age of the loan at the start of Stress Test, in months (weighted average for Loan Group)
IRP	Initial Rate Period, in months
	Interest-only Flag
RIOP	Remaining Interest-only period, in months (weighted average for loan group)
UPB Scale Factor	Factor determined by reconciling reported UPB to published financials.
Additional Interest Rate Inputs	
GFR	Guarantee Fee Rate (weighted average for Loan Group) (decimal per annum)
SFR	Servicing Fee Rate (weighted average for Loan Group) (decimal per annum)
Additional Inputs for ARMs (weighted averages for Loan Group, except for Index)	
INDEX _m	Monthly values of the contractual Interest Rate Index
LB	Look-Back period, in months
MARGIN	Loan Margin (over index), decimal per annum
RRP	Rate Reset Period, in months
	Rate Reset Limit (up and down), decimal per annum
	Maximum Rate (life cap), decimal per annum
	Minimum Rate (life floor), decimal per annum
NAC	Negative Amortization Cap, decimal fraction of UPB _{ORIG}
	Unlimited Payment Reset Period, in months
PRP	Payment Reset Period, in months
	Payment Reset Limit, as decimal fraction of prior payment

TABLE 3–6—ADDITIONAL INPUTS FOR SINGLE FAMILY DEFAULT AND PREPAYMENT

Variable	Description
PROD	Mortgage Product Type
A ₀	Age <i>immediately prior</i> to start of Stress Test, in months (weighted average for Loan Group)
LTV _{ORIG}	Loan-to-Value ratio at Origination (weighted average for Loan Group)

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TABLE 3–6—ADDITIONAL INPUTS FOR SINGLE FAMILY DEFAULT AND PREPAYMENT—Continued

Variable	Description
UPB _{ORIG}	UPB at Origination (aggregate for Loan Group), adjusted by UPB scale factor.
MIR _{ORIG}	Mortgage Interest Rate at origination (“Initial Rate” for ARMs), decimal per annum (weighted average for loan group)
UPB ₀	Unpaid Principal Balance immediately prior to start of Stress Test (aggregate for Loan Group),
IF	Fraction (by UPB, in decimal form) of Loan Group backed by Investor-owned properties
RLS _{ORIG}	Weighted average Relative Loan Size at Origination (Original UPB as a fraction of average UPB for the state and Origination Year of loan origination)
CHPGF ₀ ^{LG}	Cumulative House Price Growth Factor since Loan Origination (weighted average for Loan Group)

TABLE 3–7—ADDITIONAL INPUTS FOR MULTIFAMILY DEFAULT AND PREPAYMENT

Variable	Description
	Mortgage Product Type
A ₀	Age <i>immediately prior</i> to start of Stress Test, in months (weighted average for Loan Group)
NBF	New Book Flag
RUF	Ratio Update Flag
LTV _{ORIG}	Loan-to-Value ratio at loan origination
DCR ₀	Debt Service Coverage Ratio at the start of the Stress Test
PMT ₀	Amount of the mortgage payment (principal and interest) prior to the start of the Stress Test, or first payment for new loans (aggregate for Loan Group)
PPEM	Prepayment Penalty End Month number in the Stress Test (weighted average for Loan Group)
RM	Remaining term to Maturity in months (i.e., number of contractual payments due between the start of the Stress Test and the contractual maturity date of the loan) (weighted average for Loan Group)

TABLE 3–8—MISCELLANEOUS WHOLE LOAN CASH AND ACCOUNTING FLOW INPUTS

Variable	Description
GF	Guarantee Fee rate (weighted average for Loan Group) (decimal per annum)
FDS	Float Days for Scheduled Principal and Interest (weighted average for Loan Group)
FDP	Float Days for Prepaid Principal (weighted average for Loan Group)
FREP	Fraction Repurchased (weighted average for Loan Group) (decimal)

TABLE 3–8—MISCELLANEOUS WHOLE LOAN CASH AND ACCOUNTING FLOW INPUTS—Continued

Variable	Description
RM	Remaining Term to Maturity in months
UPD ₀	Sum of all unamortized discounts, premiums, fees, commissions, etc. for the loan group, such that the unamortized balance equals the book value minus the face value for the loan group at the start of the Stress Test, adjusted by the Unamortized Balance Scale Factor
Unamortized Balance Scale Factor	Factor determined by reconciling reported Unamortized Balance to published financials

TABLE 3–9—ADDITIONAL INPUTS FOR REPURCHASED MBS

Variable	Description
Wtd Ave Percent Repurchased	For sold loan groups, the percent of the loan group UPB that gives the actual dollar amount of loans that collateralize single class MBSs that the Enterprise holds in its own portfolio
SUPD ₀	The aggregate sum of all unamortized discounts, premiums, fees, commissions, etc. associated with the securities modeled using the Wtd Ave Percent Repurchased, such that the unamortized balance equals the book value minus the face value for the relevant securities at the start of the Stress Test, adjusted by the percent repurchased and the Security Unamortized Balance Scale Factor
Security Unamortized Balances Scale Factor	Factor determined by reconciling reported Security Unamortized Balances to published financials

3.1.2.1.2 Credit Enhancement Inputs

To calculate reductions in mortgage credit losses due to credit enhancements, the following data are required for any credit-en-

hanced loans in a loan group. For this purpose, a Loan Group is divided into Distinct Credit Enhancement Combinations, as further described in section 3.6.3.6.4, Mortgage Credit Enhancement, of this Appendix.

TABLE 3–10—CE INPUTS FOR EACH LOAN GROUP

Variable	Description
UPB _{ORIG^{LG}}	Origination UPB.
LTV _{ORIG^{LG}}	Original LTV.

TABLE 3–11—INPUTS FOR EACH DISTINCT CE COMBINATION (DCC)

Variable	Description
P _{DCC}	Percent of Initial Loan Group UPB represented by individual loan(s) in a DCC
R _{MI,DCC} or R _{LSA,DCC}	Credit rating of Loan Limit CE (MI or LSA) Counterparty
C _{MI,DCC} or C _{LSA,DCC}	Weighted Average Coverage Percentage for MI or LSA Coverage (weighted by Initial UPB)
AB _{0^{DCC,C1}}	DCC Available First Priority CE Balance immediately prior to start of the Stress Test
AB _{0^{DCC,C2}}	DCC Available Second Priority CE Balance immediately prior to start of the Stress Test

TABLE 3–11—INPUTS FOR EACH DISTINCT CE COMBINATION (DCC)—Continued

Variable	Description
R ^{DCC,C1}	DCC Credit Rating of First Priority CE Provider or Counterparty; or Cash/Cash Equivalent (which is not Haircutted)
R ^{DCC,C2}	DCC Credit Rating of Second Priority CE Provider or Counterparty; or Cash/Cash Equivalent (which is not Haircutted)
C ^{DCC,C1}	DCC Loan-Level Coverage Limit of First Priority Contract (If Subtype is MPI; otherwise = 1)
C ^{DCC,C2}	DCC Loan-Limit Coverage Limit of Second Priority Contract (if Subtype is MPI; otherwise = 1)
ExpMo ^{DCC,C1}	Month in the Stress Test (1...120 or after) in which the DCC First Priority Contract expires
ExpMo ^{DCC,C2}	Month in the Stress Test (1...120 or after) in which the DCC Second Priority Contract expires
ELPF ^{DCC,C1}	DCC Enterprise Loss Position Flag for First Priority Contract (Y or N)
ELPF ^{DCC,C2}	DCC Enterprise Loss Position Flag for Second Priority Contract (Y or N)

3.1.2.1.3 Commitments Inputs

[a] The Enterprises report Commitment Loan Group categories based on specific product type characteristics of securitized single family loans originated and delivered during the six months prior to the start of the Stress Test (*see* section 3.2, Commitments, of this Appendix). For each category, the Enterprises report the same information as for Whole Loan Groups with the following exceptions:

1. Amortization term and remaining term are set to those appropriate for newly originated loans;
2. Unamortized balances are set to zero;
3. The House Price Growth Factor is set to one;
4. Age is set to zero;
5. Any credit enhancement coverage other than mortgage insurance is not reported.

3.1.2.2 Mortgage Related Securities Inputs

[a] The Enterprises hold mortgage-related securities, including single class and Derivative Mortgage-Backed Securities (certain multi-class and strip securities) issued by Fannie Mae, Freddie Mac, and Ginnie Mae; mortgage revenue bonds issued by State and local governments and their instrumentalities; and single class and Derivative Mortgage-Backed Securities issued by private entities. The Stress Test models the cash flows of these securities individually. Table 3–12, Inputs for Single Class MBS Cash Flows sets forth the data elements that the Enterprises must compile in the RBC Report regarding each MBS held in their portfolios. This information is necessary for determining associated cash flows in the Stress Test.

TABLE 3–12—INPUTS FOR SINGLE CLASS MBS CASH FLOWS

Variable	Description
Pool Number	A unique number identifying each mortgage pool
CUSIP Number	A unique number assigned to publicly traded securities by the Committee on Uniform Securities Identification Procedures
Issuer	Issuer of the mortgage pool
Government Flag	Indicates Government insured collateral
Original UPB Amount	Original pool balance adjusted by UPB scale factor and multiplied by the Enterprise's percentage ownership

TABLE 3–12—INPUTS FOR SINGLE CLASS MBS CASH FLOWS—Continued

Variable	Description
Current UPB Amount	Initial Pool balance (at the start of the Stress Test), adjusted by UPB scale factor and multiplied by the Enterprise's percentage ownership
Product Code	Mortgage product type for the pool
Security Rate Index	If the rate on the security adjusts over time, the index that the adjustment is based on
Unamortized Balance	The sum of all unamortized discounts, premiums, fees, commissions, etc., such that the unamortized balance equals book value minus face value, adjusted by Unamortized Balance Scale Factor
Wt Avg Original Amortization Term	Original amortization term of the underlying loans, in months (weighted average for underlying loans)
Wt Avg Remaining Term of Maturity	Remaining maturity of the underlying loans at the start of the Stress Test (weighted average for underlying loans)
Wt Avg Age	Age of the underlying loans at the start of the Stress Test (weighted average for underlying loans)
Wt Avg Current Mortgage Interest Rate	Mortgage Interest Rate of the underlying loans at the start of the Stress Test (weighted average for underlying loans)
Wt Avg Pass-Through Rate	Pass-Through Rate of the underlying loans at the start of the Stress Test (Sold loans only) (weighted average for underlying loans)
Wtg Avg Original Mortgage Interest Rate	The current UPB weighted average mortgage interest rate in effect at origination for the loans in the pool
Security Rating	The most current rating issued by any Nationally Recognized Statistical Rating Organization (NRSRO) for this security, as of the reporting date
Wt Avg Gross Margin	Gross margin for the underlying loans (ARM MBS only) (weighted average for underlying loans)
Wt Avg Net Margin	Net margin (used to determine the security rate for ARM MBS) (weighted average for underlying loans)
Wt Avg Rate Reset Period	Rate reset period in months (ARM MBS only) (weighted average for underlying loans)
Wt Avg Rate Reset Limit	Rate reset limit up/down (ARM MBS only) (weighted average for underlying loans)
Wt Avg Life Interest Rate Ceiling	Maximum rate (lifetime cap) (ARM MBS only) (weighted average for underlying loans)
Wt Avg Life Interest Rate Floor	Minimum rate (lifetime floor) (ARM MBS only) (weighted average for underlying loans)
Wt Avg Payment Reset Period	Payment reset period in months (ARM MBS only) (weighted average for underlying loans)
Wt Avg Payment Reset Limit	Payment reset limit up/down (ARM MBS only) (weighted average for underlying loans)
Wt Avg Lockback Period	The number of months to look back from the interest rate change date to find the index value that will be used to determine the next interest rate (weighted average for underlying loans)

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TABLE 3–12—INPUTS FOR SINGLE CLASS MBS CASH FLOWS—Continued

Variable	Description
Wt Avg Negative Amortization Cap	The maximum amount to which the balance can increase before the payment is recast to a fully amortizing amount. It is expressed as a fraction of the original UPB (weighted average for underlying loans)
Wt Avg Original Mortgage Interest Rate	The current UPB weighted average original mortgage interest rate for the loans in the pool
Wt Avg Initial Interest Rate Period	Number of months between the loan origination date and the first rate adjustment date (weighted average for underlying loans)
Wt Avg Unlimited Payment Reset Period	Number of months between unlimited payment resets i.e., not limited by payment caps, starting with origination date (weighted average for underlying loans)
Notional Flag	Indicates if the amounts reported in Original Security Balance and Current Security Balance are notional
UPB Scale Factor	Factor determined by reconciling reported UPB to published financials
Unamortized Balance Scale Factor	Factor determined by reconciling reported Unamortized Balance to published financials
Whole Loan Modeling Flag	Indicates that the Current UPB Amount and Unamortized Balance associated with this repurchased MBS are included in the Wtg Avg Percent Repurchased and Security Unamortized Balance fields
FAS 115 Classification	The financial instrument's classification according to FAS 115
HPGR _k	Vector of House Price Growth Rates for quarters q=1. . .40 of the Stress Period

[b] Table 3–13, Information for Multi-Class and Derivative MBS Cash Flows Inputs sets forth the data elements that the Enterprises must compile regarding multi-class and Derivative MBS (e.g., REMICs and Strips). This information is necessary for determining associated cash flows in the Stress Test.

TABLE 3–13—INFORMATION FOR MULTI-CLASS AND DERIVATIVE MBS CASH FLOWS INPUTS

Variable	Description
CUSIP Number	A unique number assigned to publicly traded securities by the Committee on Uniform Securities Identification Procedures
Issuer	Issuer of the security: FNMA, FHLMC, GNMA or other
Original Security Balance	Original principal balance of the security (notional amount for interest-only securities) at the time of issuance, adjusted by UPB scale factor, multiplied by the Enterprise's percentage ownership
Current Security Balance	Initial principal balance, or notional amount, at the start of the Stress Period, adjusted by UPB scale factor, multiplied by the Enterprise's percentage ownership
Current Security Percentage Owned	The percentage of a security's total current balance owned by the Enterprise
Notional Flag	Indicates if the amounts reported in Original Security Balance and Current Security Balance are notional
Unamortized Balance	The sum of all unamortized discounts, premiums, fees, commissions, etc., such that the unamortized balance equals book value minus face value, adjusted by the Unamortized Balance Scale Factor
Unamortized Balance Scale Factor	Factor determined by reconciling reported Unamortized Balance to published financials

TABLE 3–13—INFORMATION FOR MULTI-CLASS AND DERIVATIVE MBS CASH FLOWS INPUTS—
Continued

Variable	Description
UPB Scale Factor	Factor determined by reconciling the reported current security balance to published financials
Security Rating	The most current rating issued by any Nationally Recognized Statistical Rating Organization (NRSRO) for this security, as of the reporting date

[c] Table 3–14, Inputs for MRBs and Derivative MBS Cash Flows Inputs sets forth the data elements that the Enterprises must compile in the RBC Report regarding mortgage revenue bonds and private issue mortgage related securities (MRS). The data in this table is supplemented with public securities disclosure data. This information is necessary for determining associated cash flows in the Stress Test.

TABLE 3–14—INPUTS FOR MRBs AND DERIVATIVE MBS CASH FLOWS INPUTS

Variable	Description
CUSIP Number	A unique number assigned to publicly traded securities by the Committee on Uniform Securities Identification Procedures
Original Security Balance	Original principal balance, adjusted by UPB scale factor and multiplied by the Enterprise's percentage ownership
Current Security Balance	Initial Principal balance (at start of Stress Period), adjusted by UPB scale factor and multiplied by the Enterprise's percentage ownership
Unamortized Balance	The sum of all unamortized discounts, premiums, fees, commissions, etc., such that the unamortized balance equals book value minus face value, adjusted by Unamortized Balance scale factor
Unamortized Balance Scale Factor	Factor determined by reconciling reported Unamortized Balance to published financials
UPB Scale Factor	Factor determined by reconciling the reported current security balance to published financials
Floating Rate Flag	Indicates the instrument pays interest at a floating rate
Issue Date	The issue date of the security
Maturity Date	The stated maturity date of the security
Security Interest Rate	The rate at which the security earns interest, as of the reporting date
Principal Payment Window Starting Date, Down-Rate Scenario	The month in the Stress Test that principal payment is expected to start for the security under the statutory "down" interest rate scenario, according to Enterprise projections
Principal Payment Window Ending Date, Down-Rate Scenario	The month in the Stress Test that principal payment is expected to end for the security under the statutory "down" interest rate scenario, according to Enterprise projections
Principal Payment Window Starting Date, Up-Rate Scenario	The month in the Stress Test that principal payment is expected to start for the security under the statutory "up" interest rate scenario, according to Enterprise projections
Principal Payment Window Ending Date, Up-Rate Scenario	The month in the Stress Test that principal payment is expected to end for the security under the statutory "up" interest rate scenario, according to Enterprise projections
Notional Flag	Indicates if the amounts reported in Original Security Balance and Current Security Balance are notional

TABLE 3-14—INPUTS FOR MRBS AND DERIVATIVE MBS CASH FLOWS INPUTS—Continued

Variable	Description
Security Rating	The most current rating issued by any Nationally Recognized Statistical Rating Organization (NRSRO) for this security, as of the reporting date
Security Rate Index	If the rate on the security adjusts over time, the index on which the adjustment is based
Security Rate Index Coefficient	If the rate on the security adjusts over time, the coefficient is the number used to multiply by the value of the index
Security Rate Index Spread	If the rate on the security adjusts over time, the spread is added to the value of the index multiplied by the coefficient to determine the new rate
Security Rate Adjustment Frequency	The number of months between rate adjustments
Security Interest Rate Ceiling	The maximum rate (lifetime cap) on the security
Security Interest Rate Floor	The minimum rate (lifetime floor) on the security
Life Ceiling Interest Rate	The maximum interest rate allowed throughout the life of the security
Life Floor Interest Rate	The minimum interest rate allowed throughout the life of security

3.1.2.3 Nonmortgage Instrument Cash Flows Inputs

Table 3-15, Input Variables for Nonmortgage Instrument Cash flows sets forth the data elements that the Enterprises must compile in the RBC Report to identify individual securities (other than Mortgage Related Securities) that are held by the Enterprises in their portfolios. These include debt

securities, preferred stock, and derivative contracts (interest rate swaps, caps, and floors). All data are instrument specific. The data in this table are supplemented by public securities disclosure data. For instruments with complex or non-standard features, the Enterprises may be required to provide additional information such as amortization schedules, interest rate coupon reset formulas, and the terms of the call options.

TABLE 3-15—INPUT VARIABLES FOR NONMORTGAGE INSTRUMENT CASH FLOWS

Data Elements	Description
Amortization Methodology Code	Enterprise method of amortizing deferred balances (e.g., straight line)
Asset ID	CUSIP or Reference Pool Number identifying the asset underlying a derivative position
Asset Type Code	Code that identifies asset type used in the commercial information service (e.g. ABS, Fannie Mae pool, Freddie Mac pool)
Associated Instrument ID	Instrument ID of an instrument linked to another instrument
Coefficient	Indicates the extent to which the coupon is leveraged or de-leveraged
Compound Indicator	Indicates if interest is compounded
Compounding Frequency	Indicates how often interest is compounded
Counterparty Credit Rating	NRSRO's rating for the counterparty
Counterparty Credit Rating Type	An indicator identifying the counterparty's credit rating as short-term ('S') or long-term ('L')
Counterparty ID	Enterprise counterparty tracking ID

TABLE 3–15—INPUT VARIABLES FOR NONMORTGAGE INSTRUMENT CASH FLOWS—Continued

Data Elements	Description
Country Code	Standard country codes in compliance with Federal Information Processing Standards Publication 10–4
Credit Agency Code	Identifies NRSRO (e.g., Moody's)
Current Asset Face Amount	Current face amount of the asset underlying a swap adjusted by UPB scale factor
Current Coupon	Current coupon or dividend rate of the instrument
Current Unamortized Discount	Current unamortized premium or unaccreted discount of the instrument adjusted by Unamortized Balance Scale Factor. If the proceeds from the issuance of debt or derivatives or the amount paid for an asset were greater than par, the value should be positive. If the proceeds or the amounts paid were less than par, the value should be negative
Current Unamortized Fees	Current unamortized fees associated with the instrument adjusted by Unamortized Balance Scale Factor. Generally fees associated with the issuance of debt or derivatives should be negative numbers. Fees associated with the purchase of an asset should generally be reported as positive numbers
Current Unamortized Hedge	Current unamortized hedging gains (positive) or losses (negative) associated with the instrument adjusted by the Unamortized Balance Scale Factor
Current Unamortized Other	Any other unamortized items originally associated with the instrument adjusted by Unamortized Balance Scale Factor. If the proceeds from the issuance of debt or derivatives or the amount paid for an asset were greater than par, the value should be positive. If the proceeds or the amounts paid were less than par, the value should be negative
CUSIP_ISIN	CUSIP or ISIN Number identifying the instrument
Day Count	Day count convention (e.g. 30/360)
End Date	The last index repricing date
EOP Principal Balance	End of Period face, principal or notional, amount of the instrument adjusted by UPB scale factor
Exact Representation	Indicates that an instrument is modeled according to its contractual terms
Exercise Convention	Indicates option exercise convention (e.g., American Option)
Exercise Price	Par = 1.0; Options
First Coupon Date	Date first coupon is received or paid
Index Cap	Indicates maximum index rate
Index Floor	Indicates minimum index rate
Index Reset Frequency	Indicates how often the interest rate index resets on floating-rate instruments
Index Code	Indicates the interest rate index to which floating-rate instruments are tied (e.g., LIBOR)
Index Term	Point on yield curve, expressed in months, upon which the index is based
Instrument Credit Rating	NRSRO credit rating for the instrument

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TABLE 3—15—INPUT VARIABLES FOR NONMORTGAGE INSTRUMENT CASH FLOWS—Continued

Data Elements	Description
Instrument Credit Rating Type	An indicator identifying the instruments credit rating as short-term ('S') or long-term ('L')
Instrument ID	An integer used internally by the Enterprise that uniquely identifies the instrument
Interest Currency Code	Indicates currency in which interest payments are paid or received
Interest Type Code	Indicates the method of interest rate payments (e.g., fixed, floating, step, discount)
Issue Date	Indicates the date that the instrument was issued
Life Cap Rate	The maximum interest rate for the instrument throughout its life
Life Floor Rate	The minimum interest rate for the instrument throughout its life
Look-Back Period	Period from the index reset date, expressed in months, that the index value is derived
Maturity Date	Date that the instrument contractually matures
Notional Indicator	Identifies whether the face amount is notional
Instrument Type Code	Indicates the type of instrument to be modeled (e.g., ABS, Cap, Swap)
Option Indicator	Indicates if instrument contains an option
Option Type	Indicates option type (e.g., Call option)
Original Asset Face Amount	Original face amount of the asset underlying a swap adjusted by UPB scale factor
Original Discount	Original premium or discount associated with the purchase or sale of the instrument adjusted by Unamortized Balance Scale Factor. If the proceeds from the issuance of debt or derivatives or the amount paid for an asset were greater than par, the value should be positive. If the proceeds or the amounts paid were less than par, the value should be negative
Original Face	Original face, principal or notional, amount of the instrument adjusted by UPB scale factor
Original Fees	Fees or commissions paid at the time of purchase or sale adjusted by the Unamortized Balance Scale Factor. Generally fees associated with the issuance of debt or derivatives should be negative numbers. Fees associated with the purchase of an asset should generally be reported as positive numbers
Original Hedge	Gains (positive) or losses (negative) from closing out a hedge associated with the instrument at settlement, adjusted by the Unamortized Balance Scale Factor
Original Other	Any other items originally associated with the instrument to be amortized or accreted adjusted by the Unamortized Balance Scale Factor. If the proceeds from the issuance of debt or derivatives or the amount paid for an asset were greater than par, the value should be positive. If the proceeds of the amounts paid were less than par, the value should be negative
Parent Entity ID	Enterprise internal tracking ID for parent entity
Payment Amount	Interest payment amount associated with the instrument (reserved for complex instruments where interest payments are not modeled) adjusted by UPB scale factor

TABLE 3–15—INPUT VARIABLES FOR NONMORTGAGE INSTRUMENT CASH FLOWS—Continued

Data Elements	Description
Payment Frequency	Indicates how often interest payments are made or received
Performance Date	“As of” date on which the data is submitted
Periodic Adjustment	The maximum amount that the interest rate for the instrument can change per reset
Position Code	Indicates whether the Enterprise pays or receives interest on the instrument
Principal Currency Code	Indicates currency in which principal payments are paid or received
Principal Factor Amount	EOP Principal Balance expressed as a percentage of Original Face
Principal Payment Date	A valid date identifying the date that principal is paid
Settlement Date	A valid date identifying the date the settlement occurred
Spread	An amount added to an index to determine an instrument’s interest rate
Start Date	The date, spot or forward, when some feature of a financial contract becomes effective (e.g., Call Date), or when interest payments or receipts begin to be calculated
Strike Rate	The price or rate at which an option begins to have a settlement value at expiration, or, for interest-rate caps and floors, the rate that triggers interest payments
Submitting Entity	Indicates which Enterprise is submitting information
Trade ID	Unique code identifying the trade of an instrument
Transaction Code	Indicates the transaction that an Enterprise is initiating with the instrument (e.g. buy, issue reopen)
Transaction Date	A valid date identifying the date the transaction occurred
UPB Scale Factor	Factor determined by reconciling reported UPB to published financials
Unamortized Balances Scale Factor	Factor determined by reconciling reported Unamortized Balances to published financials

3.1.2.4 Inputs for Alternative Modeling Treatment Items

TABLE 3–16—INPUTS FOR ALTERNATIVE MODELING TREATMENT ITEMS

Variable	Description
TYPE	Type of item (asset, liability or off-balance sheet item)
BOOK	Book Value of item (amount outstanding adjusted for deferred items)
FACE	Face Value or notional balance of item for off-balance sheet items
REMATUR	Remaining Contractual Maturity of item in whole months. Any fraction of a month equals one whole month
RATE	Interest Rate
INDEX	Index used to calculate Interest Rate

TABLE 3-16—INPUTS FOR ALTERNATIVE MODELING TREATMENT ITEMS—Continued

Variable	Description
FAS115	Designation that the item is recorded at fair value, according to FAS 115
RATING	Instrument or counterparty rating
FHA	In the case of off-balance sheet guarantees, a designation indicating 100% of collateral is guaranteed by FHA
MARGIN	Margin over an Index

3.1.2.5 Operations, Taxes, and Accounting Inputs

[a] Table 3-17, Operations, Taxes, and Accounting Inputs sets forth the data the Enterprises must compile in the RBC Report to permit the calculation of taxes, operating expenses, and dividends. These data include:

- Average monthly Operating Expenses (i.e., administrative expenses, salaries and benefits, professional services, property costs,

equipment costs) for the quarter prior to the beginning of the Stress Test;

- Income for the current year-to-date, one year, and two years prior to the beginning of the stress test, before taxes and provision for income taxes;
- Dividend payout ratio for the four quarters prior to the beginning of the Stress Period;
- Minimum capital requirement as of the beginning of the Stress Period.

TABLE 3-17—OPERATIONS, TAXES, AND ACCOUNTING INPUTS

Input	Description
FAS 115 and 125 fair value adjustment on retained mortgage portfolio	
FAS 133 fair value adjustment on retained mortgage portfolio	
Reserve for losses on retained mortgage portfolio	
FAS 115 and 125 fair value adjustments on non-mortgage investments	
FAS 133 fair value adjustments on non-mortgage investments	
Total cash	
Accrued interest receivable on mortgages	
Accrued interest receivable on non-mortgage investment securities	
Accrued interest receivable on non-mortgage investment securities denominated in foreign currency—hedged	
Accrued interest receivable on non-mortgage investment securities denominated in foreign currency—unhedged	
Accrued interest receivable on mortgage-linked derivatives, gross	
Accrued interest receivable on investment-linked derivatives, gross	

TABLE 3–17—OPERATIONS, TAXES, AND ACCOUNTING INPUTS—Continued

Input	Description
Accrued interest receivable on debt-linked derivatives, gross	
Other accrued interest receivable	
Accrued interest receivable on hedged debt-linked foreign currency swaps	Underlying instrument is GSE issued debt
Accrued interest receivable on unhedged debt-linked foreign currency swaps	
Accrued interest receivable on hedged asset-linked foreign currency swaps	Underlying instrument is an asset
Accrued interest receivable on unhedged asset-linked foreign currency swaps	
Currency transaction adjustments—hedged assets	Cumulative gain or loss due to changes in foreign exchange rates relative to on-balance sheet assets originally denominated in foreign currency
Currency transaction adjustments—unhedged assets	Cumulative gain or loss due to changes in foreign exchange rates relative to unhedged assets and off-balance sheet items originally denominated in foreign currency
Federal income tax refundable	
Accounts receivable	
Fees receivable	
Low income housing tax credit investments	
Fixed assets, net	
Clearing accounts	Net book value of all clearing accounts
Other assets	
Foreclosed property, net	Real estate owned including property acquired through foreclosure proceedings
FAS 133 fair value adjustment on debt securities	
Accrued interest payable on existing fixed-rate debt securities	
Accrued interest payable on existing floating-rate debt securities	
Accrued interest payable on existing debt issued in foreign currency—hedged	
Accrued interest payable on existing debt issued in foreign currency—unhedged	
Accrued interest payable on mortgage-linked derivatives, gross	
Accrued interest payable on investment-linked derivatives, gross	

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TABLE 3-17—OPERATIONS, TAXES, AND ACCOUNTING INPUTS—Continued

Input	Description
Accrued interest payable on debt-linked derivatives, gross	
Other accrued interest payable	
Accrued interest payable debt-linked foreign currency swaps—hedged	
Accrued interest payable debt-linked foreign currency swaps—unhedged	
Accrued interest payable asset-linked foreign currency swaps—hedged	
Accrued interest payable asset-linked foreign currency swaps—unhedged	
Principal and interest due to mortgage security investors	Cash received on sold mortgages for onward submission to mortgage security investors
Currency transaction adjustments—hedged debt	Cumulative gain or loss due to changes in foreign exchange rates relative to on-balance sheet debt originally denominated in foreign currency
Currency transaction adjustments—unhedged debt	Cumulative gain or loss due to changes in foreign exchange rates relative to unhedged liabilities and off-balance sheet items originally denominated in foreign currency
Escrow deposits	Cash balances held in relation to servicing of multi-family loans
Federal income taxes payable	
Preferred dividends payable	
Accounts payable	
Other liabilities	
Common dividends payable	
Reserve for losses on sold mortgages	
Common stock	
Preferred stock, non-cumulative	
Additional paid-in capital	
Retained earnings	
Treasury stock	
Unrealized gains and losses on available-for-sale securities, net of tax, in accordance with FAS 115 and 125	
Unrealized gains and losses due to mark to market adjustments, FAS 115 and 125	
Unrealized gains and losses due to deferred balances related to pre-FAS 115 and 125 adjustments	

TABLE 3–17—OPERATIONS, TAXES, AND ACCOUNTING INPUTS—Continued

Input	Description
Unrealized gains and losses due to other realized gains, FAS 115	
Other comprehensive income, net of tax, in accordance with FAS 133	
OCI due to mark to market adjustments, FAS 133	
OCI due to deferred balances related to pre-FAS 133 adjustments	
OCI due to other realized gains, FAS 133	
Operating expenses	Average of prior three months
Common dividend payout ratio (average of prior 4 quarters)	Sum dollar amount of common dividends paid over prior 4 quarters and divided by the sum of total of after tax income less preferred dividends paid over prior 4 quarters
Common dividends per share paid 1 quarter prior to the beginning of the stress period	
Common shares outstanding	
Common Share Market Price	
Dividends paid on common stock 1 quarter prior to the beginning of the stress period	
Share Repurchases (average of prior 4 quarters)	Sum dollar amount of repurchased shares, net of newly issued shares, over prior 4 quarters and divided by 4
Off-balance-sheet Guarantees	Guaranteed instruments not reported on the balance sheet, such as whole loan REMICs and multifamily credit enhancements, and not 100% guaranteed by the FHA
Other Off-Balance Sheet Guarantees	All other off-balance sheet guaranteed instruments not included in another category, and not 100% guaranteed by the FHA
YTD provision for income taxes	Provision for income taxes for the period beginning January 1 and ending as of the report date
Tax loss carryforward	Net losses available to write off against future years' net income
Tax liability for the year prior to the beginning of the Stress Test	
Tax liability for the year 2 years prior to the beginning of the Stress Test (net of carrybacks)	
Taxable income for the year prior to the beginning of the Stress Test	
Taxable income for the year 2 years prior to the beginning of the Stress Test (net of carrybacks)	
Net after tax income for the quarter preceding the start of the stress test	

TABLE 3-17—OPERATIONS, TAXES, AND ACCOUNTING INPUTS—Continued

Input	Description
YTD taxable income	Total amount of taxable income for the period beginning January 1 and ending as of the report date
Minimum capital requirement at the beginning of the Stress Period	
Specific allowance for loan losses	Loss allowances calculated in accordance with FAS 114
Zero coupon swap receivable	
Unamortized discount on zero coupon swap receivable	

3.1.3 Public Data

3.1.3.1 Interest Rates

[a] The Interest Rates component of the Stress Test projects Treasury yields as well as other interest rate indexes that are needed to calculate cash flows, to simulate the performance of mortgages and other financial instruments, and to calculate capital for each of the 120 months in the Stress Period. Table 3-18, Interest Rate and Index Inputs,

sets forth the interest rate indexes used in the Stress Test

[b] The starting values for all of the Interest Rates are the monthly average of daily rates for the month preceding the start of the stress test.

[c] For the 10-year CMT, monthly values are required for the three years prior to the start of the Stress Test (m = -35, -34...0). For all other indexes, monthly values for the prior two years are required (m = -23, -22...0).

TABLE 3-18—INTEREST RATE AND INDEX INPUTS

Interest Rate Index	Description	Source
1 MO Treasury Bill	One-month Treasury bill yield, monthly simple average of daily rate, quoted as actual/360	Bloomberg Generic 1 Month. U.S. Treasury bill. Ticker: GB1M (index).
3 MO CMT	Three-month constant maturity Treasury yield, monthly simple average of daily rate, quoted as bond equivalent yield	Federal Reserve H.15 Release.
6 MO CMT	Six-month constant maturity Treasury yield, monthly simple average of daily rate, quoted as bond equivalent yield	Federal Reserve H.15 Release.
1 YR CMT	One-year constant maturity Treasury yield, monthly simple average of daily rate, quoted as bond equivalent yield	Federal Reserve H.15 Release.
2 YR CMT	Two-year constant maturity Treasury yield, monthly simple average of daily rate, quoted as bond equivalent yield	Federal Reserve H.15 Release.
3 YR CMT	Three-year constant maturity Treasury yield, monthly simple average of daily rate, quoted as bond equivalent yield	Federal Reserve H.15 Release.
5 YR CMT	Five-year constant maturity Treasury yield, monthly simple average of daily rate, quoted as bond equivalent yield	Federal Reserve H.15 Release.

TABLE 3–18—INTEREST RATE AND INDEX INPUTS—Continued

Interest Rate Index	Description	Source
10 YR CMT	Ten-year constant maturity Treasury yield, monthly simple average of daily rate, quoted as bond equivalent yield	Federal Reserve H.15 Release.
20 YR CMT	Twenty-year constant maturity Treasury yield, monthly simple average of daily rate, quoted as bond equivalent yield	Federal Reserve H.15 Release.
30 YR CMT	Thirty-year constant maturity Treasury yield, monthly simple average of daily rate, quoted as bond equivalent yield; after February 15, 2002, estimated according to the Department of Treasury methodology using long-term average rates and extrapolation factors as referenced in OFHEO guideline 402	Federal Reserve H.15 Release, Extrapolation Factors used for estimation, U.S. Dept. of Treasury.
12-mo Moving Treasury Average (MTA)	12-month Federal Reserve cumulative average 1 year CMT, monthly simple average of daily rate	Bloomberg Ticker: 12MTA (Index).
Overnight Fed Funds (Effective)	Overnight effective Federal Funds rate, monthly simple average of daily rate	Federal Reserve H.15 Release.
Certificate of Deposits Index (CODI)	12-month average of monthly published yields on 3-month certificates of deposit, based on the Federal Reserve Board statistical release, H–15	Bloomberg Ticker: COF CODI (index).
1 Week Federal Funds	1 week Federal Funds rate, monthly simple average of daily rates	Bloomberg Term Fed Funds U.S. Domestic Ticker: GFED01W (index).
6 Month Fed Funds	6 month Federal Funds rate, monthly simple average of daily rates	Bloomberg Term Fed Funds U.S. Domestic Ticker: GFED06M (index).
Conventional Mortgage Rate	FHLMC (Freddie Mac) contract interest rates for 30 YR fixed-rate mortgage commitments, monthly average of weekly rates	Federal Reserve H.15 Release.
Constant Maturity Mortgage (CMM) Index	Bond equivalent yield on TBA mortgage-backed security which prices at the par price	TradeWeb.
1-mo Freddie Mac Reference Bill	1-month Freddie Mac Reference Bill, actual price and yield by auction date	Freddiemac.com website: http://www.freddiemac.com/debt/data/cgi-bin/refbillaucres.cgi?order=AD .
FHLB 11th District COF	11th District (San Francisco) weighted average cost of funds for savings and loans, monthly	Bloomberg Cost of Funds for the 11th District Ticker: COF11 (index).
1 MO LIBOR	One-month London Interbank Offered Rate, average of bid and asked, monthly simple average of daily rates, quoted as actual/360	British Bankers Association Bloomberg Ticker: US0001M (index).

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TABLE 3-18—INTEREST RATE AND INDEX INPUTS—Continued

Interest Rate Index	Description	Source
3 MO LIBOR	Three-month London Interbank Offered Rate, average of bid and asked, monthly simple average of daily rates, quoted as actual/360	British Bankers Association Bloomberg Ticker: US0003M (index).
6 MO LIBOR	Six-month London Interbank Offered Rate, average of bid and asked, monthly simple average of daily rates, quoted as actual/360	British Bankers Association Bloomberg Ticker: US0006M (index).
12 MO LIBOR	One-year London Interbank Offered Rate, average of bid and asked, monthly simple average of daily rates, quoted as actual/360	British Bankers Association Bloomberg Ticker: US0012M (index).
Prime Rate	Prevailing rate as quoted, monthly average of daily rates	Federal Reserve H.15 Release.
1 MO Federal Agency COF	One-month Federal Agency Cost of Funds, monthly simple average of daily rates, quoted as actual/360	Bloomberg Generic 1 Month Agency Discount Note Yield Ticker: AGDN030Y (index).
3 MO Federal Agency COF	Three-month Federal Agency Cost of Funds, monthly simple average of daily rates, quoted as actual/360	Bloomberg Generic 3 Month Agency Discount Note Yield Ticker: AGDN090Y (index).
6 MO Federal Agency COF	Six-month Federal Agency Cost of Funds, monthly simple average of daily rates, quoted as actual/360	Bloomberg Generic 6 Month Agency Discount Note Yield Ticker: AGDN180Y (index).
1 YR Federal Agency COF	One-year Federal Agency Cost of Funds, monthly simple average of daily rates, quoted as actual/360	Bloomberg Generic 12 Month Agency Discount Note Yield. Ticker: AGDN360Y (index).
2 YR Federal Agency COF	Two-year Federal Agency Fair Market Yield, monthly simple average of daily rates	Bloomberg Generic 2 Year Agency Fair Market Yield. Ticker: CO842Y (index).
3 YR Federal Agency COF	Three-year Federal Agency Fair Market Yield, monthly simple average of daily rates	Bloomberg Generic 3 Year Agency Fair Market Yield. Ticker: CO843Y (index).
5 YR Federal Agency COF	Five-year Federal Agency Fair Market Yield, monthly simple average of daily rates	Bloomberg Generic 5 Year Agency Fair Market Yield. Ticker: CO845Y (index).
10 YR Federal Agency COF	Ten-year Federal Agency Fair Market Yield, monthly simple average of daily rates	Bloomberg Generic 10 Year Agency Fair Market Yield. Ticker: CO8410Y (index).
30 YR Federal Agency COF	Thirty-year Federal Agency Fair Market Yield, monthly simple average of daily rates	Bloomberg Generic 30 Year Agency Fair Market Yield. Ticker: CO8430Y (index).
15 YR fixed-rate mortgage	FHLMC (Freddie Mac) contract interest rates for 15 YR fixed-rate mortgage commitments, monthly average of FHLMC (Freddie Mac) contract interest rates for 15 YR	Bloomberg FHLMC 15 YR, 10 day commitment rate Ticker: FHCR1510 (index).

TABLE 3–18—INTEREST RATE AND INDEX INPUTS—Continued

Interest Rate Index	Description	Source	
7-year balloon mortgage rate	Seven-year balloon mortgage, equal to the Conventional Mortgage Rate less 50 basis points	Computed.	
2-yr Swap	2-yr U.S. Dollar Swap Rate, quoted as semi-annually fixed rate vs. 3-mo U.S. dollar	Bloomberg (index).	Ticker: USSWAP2
3-yr Swap	3-yr U.S. Dollar Swap Rate, quoted as semi-annually fixed rate vs. 3-mo U.S. dollar LIBOR	Bloomberg (Index).	Ticker: USSWAP3
5-yr Swap	5-yr U.S. Dollar Swap Rate, quoted as semi-annually fixed rate vs. 3-mo U.S. dollar LIBOR	Bloomberg (Index).	Ticker: USSWAP5
10-yr Swap	10-yr U.S. Dollar Swap Rate, quoted as semi-annually fixed rate vs. 3-mo U.S. dollar LIBOR	Bloomberg (Index).	Ticker: USSWAP10
30-yr Swap	30-yr U.S. Dollar Swap Rate, quoted as semi-annually fixed rate vs. 3-mo U.S. dollar LIBOR	Bloomberg (Index).	Ticker: USSWAP30

3.1.3.2 Property Valuation Inputs

Table 3–19, Stress Test Single Family Quarterly House Price Growth Rates and Table 3–21, HPI Dispersion Parameters, set forth inputs which are used to project single

family mortgage performance. Table 3–20, Multifamily Monthly Rent Growth and Vacancy Rates, sets forth inputs which are used to project multifamily mortgage performance.

TABLE 3–19—STRESS TEST SINGLE FAMILY QUARTERLY HOUSE PRICE GROWTH RATES¹

Stress Test Months	Historical Months	House Price Growth Rate	Stress Test Months	Historical Months	House Price Growth Rate
1–3	Jan-Mar 1984	–0.005048	61–63	Jan-Mar 1989	0.006292
4–6	Apr-Jun 1984	0.001146	64–66	Apr-Jun 1989	0.010523
7–9	Jul-Sep 1984	0.001708	67–69	Jul-Sep 1989	0.017893
10–12	Oct-Dec 1984	–0.007835	70–72	Oct-Dec 1989	–0.004881
13–15	Jan-Mar 1985	–0.006975	73–75	Jan-Mar 1990	–0.000227
16–18	Apr-Jun 1985	0.004178	76–78	Apr-Jun 1990	0.008804
19–21	Jul-Sep 1985	–0.005937	79–81	Jul-Sep 1990	0.003441
22–24	Oct-Dec 1985	–0.019422	82–84	Oct-Dec 1990	–0.003777
25–27	Jan-Mar 1986	0.026231	85–87	Jan-Mar 1991	0.009952
28–30	Apr-Jun 1986	0.022851	88–90	Apr-Jun 1991	0.012616
31–33	Jul-Sep 1986	–0.021402	91–93	Jul-Sep 1991	0.002267
34–36	Oct-Dec 1986	–0.018507	94–96	Oct-Dec 1991	0.012522

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**TABLE 3-19—STRESS TEST SINGLE FAMILY QUARTERLY HOUSE PRICE GROWTH RATES¹—
Continued**

Stress Test Months	Historical Months	House Price Growth Rate	Stress Test Months	Historical Months	House Price Growth Rate
37-39	Jan-Mar 1987	0.004558	97-99	Jan-Mar 1992	0.013378
40-42	Apr-Jun 1987	-0.039306	100-102	Apr-Jun 1992	-0.000519
43-45	Jul-Sep 1987	-0.024382	103-105	Jul-Sep 1992	0.016035
46-48	Oct-Dec 1987	-0.026761	106-108	Oct-Dec 1992	0.005691
49-51	Jan-Mar 1988	-0.003182	109-111	Jan-Mar 1993	0.005723
52-54	Apr-Jun 1988	0.011854	112-114	Apr-Jun 1993	0.010614
55-57	Jul-Sep 1988	-0.020488	115-117	Jul-Sep 1993	0.013919
58-60	Oct-Dec 1988	-0.007260	118-120	Oct-Dec 1993	0.011267

¹ Source: OFHEO House Price Report, 1996:3.

TABLE 3-20—MULTIFAMILY MONTHLY RENT GROWTH¹ AND VACANCY RATES²

Stress Test Month	Historical Month	Rent Growth Rate	Vacancy Rate	Stress Test Month	Historical Month	Rent Growth Rate	Vacancy Rate
1	Jan 1984	0.001367	0.136	61	Jan 1989	0.000052	0.135
2	Feb 1984	0.001186	0.136	62	Feb 1989	0.000284	0.135
3	Mar 1984	0.001422	0.136	63	Mar 1989	0.000404	0.135
4	Apr 1984	0.001723	0.136	64	Apr 1989	0.000150	0.135
5	May 1984	0.001537	0.136	65	May 1989	0.000331	0.135
6	Jun 1984	0.001354	0.136	66	Jun 1989	0.001483	0.135
7	Jul 1984	0.000961	0.136	67	Jul 1989	0.000759	0.135
8	Aug 1984	0.000601	0.136	68	Aug 1989	0.001502	0.135
9	Sep 1984	0.001106	0.136	69	Sep 1989	0.002254	0.135
10	Oct 1984	0.001623	0.136	70	Oct 1989	0.002768	0.135
11	Nov 1984	0.001395	0.136	71	Nov 1989	0.002220	0.135
12	Dec 1984	0.001170	0.136	72	Dec 1989	0.002040	0.135
13	Jan 1985	0.001014	0.150	73	Jan 1990	0.002180	0.120
14	Feb 1985	0.000857	0.150	74	Feb 1990	0.002772	0.120
15	Mar 1985	0.000315	0.150	75	Mar 1990	0.002867	0.120
16	Apr 1985	-0.000225	0.150	76	Apr 1990	0.003243	0.120
17	May 1985	0.000154	0.150	77	May 1990	0.002963	0.120
18	Jun 1985	0.000534	0.150	78	Jun 1990	0.003588	0.120
19	Jul 1985	0.001115	0.150	79	Jul 1990	0.004885	0.120

TABLE 3–20—MULTIFAMILY MONTHLY RENT GROWTH¹ AND VACANCY RATES²—Continued

Stress Test Month	Historical Month	Rent Growth Rate	Va-cancy Rate	Stress Test Month	Historical Month	Rent Growth Rate	Va-cancy Rate
20	Aug 1985	0.001702	0.150	80	Aug 1990	0.004564	0.120
21	Sep 1985	0.001576	0.150	81	Sep 1990	0.005491	0.120
22	Oct 1985	0.001450	0.150	82	Oct 1990	0.005475	0.120
23	Nov 1985	0.001357	0.150	83	Nov 1990	0.005763	0.120
24	Dec 1985	0.001266	0.150	84	Dec 1990	0.005817	0.120
25	Jan 1986	0.001823	0.168	85	Jan 1991	0.005261	0.108
26	Feb 1986	0.002392	0.168	86	Feb 1991	0.005456	0.108
27	Mar 1986	0.002665	0.168	87	Mar 1991	0.005637	0.108
28	Apr 1986	0.002942	0.168	88	Apr 1991	0.005843	0.108
29	May 1986	0.002517	0.168	89	May 1991	0.005970	0.108
30	Jun 1986	0.002105	0.168	90	Jun 1991	0.005719	0.108
31	Jul 1986	0.001372	0.168	91	Jul 1991	0.005533	0.108
32	Aug 1986	0.000652	0.168	92	Aug 1991	0.004512	0.108
33	Sep 1986	0.000110	0.168	93	Sep 1991	0.003916	0.108
34	Oct 1986	-0.000431	0.168	94	Oct 1991	0.003779	0.108
35	Nov 1986	-0.000201	0.168	95	Nov 1991	0.004226	0.108
36	Dec 1986	0.000030	0.168	96	Dec 1991	0.004791	0.108
37	Jan 1987	-0.001448	0.175	97	Jan 1992	0.005361	0.098
38	Feb 1987	-0.002162	0.175	98	Feb 1992	0.004085	0.098
39	Mar 1987	-0.001202	0.175	99	Mar 1992	0.003885	0.098
40	Apr 1987	-0.001136	0.175	100	Apr 1992	0.002992	0.098
41	May 1987	-0.001466	0.175	101	May 1992	0.002941	0.098
42	Jun 1987	-0.002809	0.175	102	Jun 1992	0.002851	0.098
43	Jul 1987	-0.002069	0.175	103	Jul 1992	0.002346	0.098
44	Aug 1987	-0.002530	0.175	104	Aug 1992	0.003850	0.098
45	Sep 1987	-0.001033	0.175	105	Sep 1992	0.003245	0.098
46	Oct 1987	-0.001148	0.175	106	Oct 1992	0.003194	0.098
47	Nov 1987	-0.001617	0.175	107	Nov 1992	0.001931	0.098
48	Dec 1987	-0.002064	0.175	108	Dec 1992	0.001494	0.098
49	Jan 1988	-0.001372	0.158	109	Jan 1993	0.001527	0.104
50	Feb 1988	-0.001524	0.158	110	Feb 1993	0.002317	0.104

TABLE 3–20—MULTIFAMILY MONTHLY RENT GROWTH¹ AND VACANCY RATES²—Continued

Stress Test Month	Historical Month	Rent Growth Rate	Vacancy Rate	Stress Test Month	Historical Month	Rent Growth Rate	Vacancy Rate
51	Mar 1988	-0.001972	0.158	111	Mar 1993	0.001904	0.104
52	Apr 1988	-0.001363	0.158	112	Apr 1993	0.002545	0.104
53	May 1988	-0.001143	0.158	113	May 1993	0.002570	0.104
54	Jun 1988	-0.001194	0.158	114	Jun 1993	0.002449	0.104
55	Jul 1988	-0.001429	0.158	115	Jul 1993	0.002161	0.104
56	Aug 1988	-0.001315	0.158	116	Aug 1993	0.001857	0.104
57	Sep 1988	-0.002581	0.158	117	Sep 1993	0.001664	0.104
58	Oct 1988	-0.002337	0.158	118	Oct 1993	0.002184	0.104
59	Nov 1988	-0.001218	0.158	119	Nov 1993	0.002932	0.104
60	Dec 1988	-0.000203	0.158	120	Dec 1993	0.002776	0.104

¹ Source: U.S. Department of Labor, Bureau of Labor Statistics, Rent of Primary Residence component of the Consumer Price Index—All Urban Consumers.

² Source: U.S. Census Bureau, Housing Vacancy Survey—Annual 1999.

TABLE 3–21—HPI DISPERSION PARAMETERS¹

Dispersion Parameter	Linear (α)	Quadratic (β)
	0.002977	-0.000024322

¹ Source: OFHEO House Price Report, 1996:3.

3.1.4 Constant Values

Certain values are numerical constants that are parameters of the cash flow simulation. These values are established by OFHEO

on the basis of analysis of Benchmark and other historical data.

3.1.4.1 Single Family Loan Performance

TABLE 3–22—LOAN GROUP INPUTS FOR SINGLE FAMILY GROSS LOSS SEVERITY

Variable	Description	Value	Source
MQ	Months Delinquent: time during which Enterprise pays delinquent loan interest to MBS holders	4 for sold loans 0 otherwise	
MF	Months to Foreclosure: number of missed payments through completion of foreclosure	13 months	Average value of BLE data
MR	Months in REO	7 months	Average value of BLE data
F	Foreclosure Costs as a decimal fraction of Defaulted UPB	0.037	Average of historical data from Enterprise loans, 1979–1999

TABLE 3–22—LOAN GROUP INPUTS FOR SINGLE FAMILY GROSS LOSS SEVERITY—Continued

Variable	Description	Value	Source
R	REO Expenses as a decimal fraction of Defaulted UPB	0.163	Average of historical data from Enterprise loans, 1979–1999
RR	Recovery Rate for Defaulted loans in the BLE, as a percent of predicted house price using HPI (decimal)	0.61	Average value of BLE data

See also Table 3–35, Coefficients for Single Family Default and Prepayment Explanatory Variables.

3.1.4.2 Multifamily Loan Performance

TABLE 3–23—LOAN GROUP INPUTS FOR MULTIFAMILY DEFAULT AND PREPAYMENT

Variable	Description	Value	Source
OE	Operating expenses as a share of gross potential rents	0.472	Average ratio of operating expenses to gross rents, 1970–1992 Institute for Real Estate Management annual surveys of apartments.
RVR ₀	Initial rental vacancy rate	0.0623	National average vacancy rate, 1970–1995, from census surveys.

TABLE 3–24—LOAN GROUP INPUTS FOR MULTIFAMILY GROSS LOSS SEVERITY

Variable	Description	Value	Source
MQ	Time during which delinquent loan interest is passed-through to MBS holders	4 for sold loans 0 otherwise	
RHC	Net REO holding costs as a decimal fraction of Defaulted UPB	0.1333	UPB-weighted average, Freddie Mac “old book” REO through 1995.
MF	Time from Default to completion of foreclosure (REO acquisition)	18 months	UPB-weighted average, Freddie Mac “old book” REO through 1995.
MR	Months from REO acquisition to REO disposition	13 months	UPB-weighted average, Freddie Mac “old book” REO through 1995.
RP	REO proceeds as a decimal fraction of Defaulted UPB	0.5888	UPB-weighted average, Freddie Mac “old book” REO through 1995.

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See also Table 3-39, Explanatory Variable Coefficients for Multifamily Default.

3.2 Commitments

3.2.1 Commitments Overview

The Enterprises make contractual commitments to purchase or securitize mortgages. The Stress Test provides for deliveries of mortgages into the commitments that exist at the start of the Stress Period. These mortgages are grouped into “Commitment Loan Groups” that reflect the characteristics of the mortgages that were originated in the six months preceding the start of the Stress Period and securitized by the Enterprise, except that they are assigned coupon rates consistent with the projected delivery month in each interest rate scenario. These Commitment Loan Groups are added to the Enterprise’s sold portfolio and the Stress Test projects their performance during the Stress Period. In the down-rate scenario, the Stress Test provides that 100 percent of the mortgages specified in the commitments are delivered within the first three months. In the up-rate scenario, 75 percent are delivered within the first six months.

3.2.2 Commitments Inputs

The Stress Test uses two sources of data to determine the characteristics of the mortgages delivered under commitments:

- Information from the Enterprises on the characteristics of loans originated and delivered to the Enterprises in the six months preceding the start of the Stress Period, broken out into four categories, scaled by the dollar value of commitments outstanding at the start of the Stress Period;
- Interest Rate series generated by the Interest Rates component of the Stress Test.

3.2.2.1 Loan Data

[a] The Enterprises report Commitment Loan Group categories based on the following product type characteristics of securitized single family loans originated and delivered during the six months prior to the start of the Stress Test:

- 30-year fixed-rate
- 15-year fixed-rate
- One-year CMT ARM
- Seven-year balloon

[b] For each Commitment Loan Group category, the Enterprises report the same information as in section 3.6 for Whole Loan groups with the following exceptions:

- Amortization term and remaining term are set to those appropriate for newly originated loans
- Unamortized balances are set to zero
- The House Price Growth Factor is set to one
- Age is set to zero

- Any credit enhancement coverage other than mortgage insurance is not reported.

[c] For each Commitment Loan Group category, the Enterprises report the Starting UPB defined as follows:

$$\text{Starting UPB} = \left[\frac{\text{Total dollar amount of Commitments Outstanding}}{\text{Total Starting UPB for all Commitment Loan Group Categories}} \right] \times \left[\text{Starting UPB for the Commitment Loan Group Category} \right]$$

3.2.2.2 Interest Rate Data

The Stress Test uses the following Interest Rate series, generated from section 3.3, Interest Rates, of this Appendix, for the first 12 months of the Stress Period:

- One-year Constant Maturity Treasury yield (CMT)
- Conventional mortgage rate (30-year fixed rate)
- 15-year fixed-rate mortgage rate
- Seven-year balloon mortgage rate.

3.2.3 Commitments Procedures

[a] Determine Commitment Loan Groups from the Commitment Loan Group categories as follows:

1. Divide each category into one subcategory for each delivery month. Three subcategories are created in the down-rate scenario and six in the up-rate scenario.
2. Calculate the total starting UPB for each subcategory as follows:

Subcategory Starting UPB =

$$\left[\frac{\text{Starting UPB for Commitment Loan Group Category}}{\text{Total Starting UPB for all Commitment Loan Group Categories}} \right] \times \text{MDP}$$

Where: MDP is taken from Table 3-25.

TABLE 3-25—MONTHLY DELIVERIES AS A PERCENTAGE OF COMMITMENTS OUTSTANDING (MDP)

Delivery Month (DM)	Up-Rate Scenario MDP	Down-Rate Scenario MDP
1	18.75%	62.50%
2	18.75%	25.00%
3	12.50%	12.50%

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TABLE 3-25—MONTHLY DELIVERIES AS A PERCENTAGE OF COMMITMENTS OUTSTANDING (MDP)—Continued

Delivery Month (DM)	Up-Rate Scenario MDP	Down-Rate Scenario MDP
4	12.50%	0.00%
5	6.25%	0.00%
6	6.25%	0.00%
Total	75%	100%

3. Set the Initial Mortgage Interest Rate for each subcategory using the interest rate series consistent with the commitment product type. For fixed rate loans, this rate = INDEX_{DM}. For ARM loans, the Initial Mortgage Interest Rate and the Mortgage Interest Rate at Origination are equal and set to INDEX_{DM-LB-1}+MARGIN, where LB (Lookback Period) and MARGIN for ARM commitment loan groups come from the RBC Report. Calculate the mortgage payment amount consistent with the Initial rate and amortizing term.

[b] Cash flows for the commitment loan groups, broken down by subcategory corresponding to assumed month of delivery to the Enterprises, are to be generated using the same procedures as contained in section 3.6, Whole Loan Cash Flows, of this Appendix, except as follows:

1. For purposes of generating cash flows, treat each commitment loan subcategory as if the loans were newly originated and delivered just prior to the start of the Stress Test (that is, treat them as if mortgage age at time zero, A₀, were zero).

2. Wherever section 3.6, Whole Loan Cash Flows, of this Appendix, refers to interest rate or discount rate adjustments, add Delivery Month (DM) to the Interest Rate or discount rate monthly counter, where constant DM ∈ [1,2,3,4,5,6] refers to the number of months into the Stress Test that the commitment subcategory is assumed to be delivered to the Enterprise. For example,

a. Section 3.6.3.3.3[a]1.b.3) of this Appendix, if m is a rate reset month, then:

$$MIR_m = INDEX_{m-1-LB+DM} + MARGIN$$

b. Section 3.6.3.4.3.1[a]3.a., of this Appendix,

$$B_q = 1 \text{ if } MCON_{m+DM} + 0.02 \leq MIR_m$$

c. Section 3.6.3.4.3.1[a]4., of this Appendix,

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$$RS_q = avg \left(\frac{MIR_{ORIG} - MCON_{m+DM}}{MIR_{ORIG}} \right)$$

d. Section 3.6.3.4.3.1[a]5., of this Appendix,

$$YCS_q = avg \left(\frac{T120Y_{m+DM}}{T12Y_{m+DM}} \right)$$

e. Section 3.6.3.6.5.1, of this Appendix. Throughout this section replace DR_m with DR_{m+DM} wherever it appears.

f. Section 3.6.3.7.3[a]9.b., of this Appendix. The formula for float income received should replace FER_m with FER_{m+DM}

3. For purpose of computing LTV_q as defined in section 3.6.3.4.3.1[a]2.a., of this Appendix, adjust the quarterly index for the vector of house price growth rates by adding DQ=2 if the loans are delivered in the Stress Test month 6, DQ = 1 if the loans are delivered in Stress Test months 3, 4 or 5, and 0 otherwise. That is, in the LTV_q formula:

$$Exp \left(\sum_{k=1}^q HPGR_{k+DQ} \right)$$

Where:

$$DQ = int \left(\frac{DM}{3} \right)$$

4. The note at the end of section 3.6.3.4.3.2[a]5., of this Appendix, should be adjusted to read: for m > 120-DM, use MPR_{120-DM} and MDR_{120-DM}.

5. Adjust the final outputs for each commitment subcategory by adding DM to each monthly counter, m. That is, the outputs in Table 3-52 and 3-55 should be revised to replace each value's monthly counter of m with the new counter of m + DM, which will modify the description of each to read "in month m = 1 + DM, ... RM+DM". (Note that for one variable, PUPB_m, the revised counter will range from DM to RM + DM). The revised monthly counters will now correspond to the months of the Stress Test. For values of m under the revised description which are less than or equal to DM, each variable (except Performing UPB) in these two tables should equal zero. For Performing UPB in month DM, the variable will equal the Original UPB for month DM and will equal zero for months less than DM.

3.2.4 Commitments Outputs

[a] The outputs of the Commitment component of the Stress Test include Commitment Loan Groups specified in the same way as

loan groups in the RBC Report (*See* section 3.6, Whole Loan Cash Flows, of this Appendix) with two exceptions; mortgage insurance is the only available credit enhancement coverage; and delivery month is added to indicate the month in which these loan groups are added to the sold portfolio. The data for these loan groups allow the Stress Test to project the Default, Prepayment and loss rates and cash flows for loans purchased under commitments for the ten-year Stress Period.

[b] The Commitment outputs also include cash flows analogous to those specified for Whole Loans in section 3.6.4, Final Whole Loan Cash Flow Outputs, of this Appendix, which are produced for each Commitment Loan Group.

3.3 Interest Rates

3.3.1 Interest Rates Overview

[a] The Interest Rates component of the Stress Test projects Constant Maturity Treasury yields as well as other interest rates and indexes (collectively, "Interest Rates") that are needed to project mortgage performance and calculate cash flows for mortgages and other financial instruments for each of the 120 months in the Stress Period.

[b] The process for determining Interest Rates is as follows: first, identify the values for the necessary Interest Rates at time zero; second, project the ten-year CMT for each month of the Stress Period as specified in the 1992 Act; third, project the 1-month Treasury yield, the 3-month, 6-month, 1-, 2-, 3-, 5-, 20-year, and 30-year CMTs; fourth, project non-treasury Interest Rates, including the Federal Agency Cost of Funds Index; and fifth, project the Enterprises Cost of Funds Index, which provides borrowing rates for the Enterprises during the Stress Period, by increasing the Agency Cost of Funds Index by 10 basis points for the last 108 months of the Stress Test. Guidance in determining interest rates is available under OFHEO Guideline No. 402, "Risk Based Capital Process for Capturing and Utilizing Interest Rates Files," which is available on OFHEO's Web site, <http://www.OFHEO.Gov>.

[c] In cases where the Stress Test would require interest rates for maturities other than those specifically projected in Table 3-18 of section 3.1.3, Public Data, of this Appendix, the Interest Rates component performs a monthly linear interpolation. In cases where the Stress Test would require an Interest Rate for a maturity greater than the longest maturity specifically projected for that index, the Stress Test would use the longest maturity for that index.

3.3.2 Interest Rates Inputs

The Interest Rates that are input to the Stress Test are set forth in Table 3-18 of sec-

tion 3.1.3, Public Data, of this Appendix. Inputs for the 30-year CMT yield after February 15, 2002 are estimated according to the Department of Treasury methodology using long-term average rates and extrapolation factors.

3.3.3 Interest Rates Procedures

[a] Produce Interest Rates for use in the Stress Test using the following three steps:

1. Project the Ten-Year CMT as specified in the 1992 Act:

a. *Down-Rate Scenario.* In the Stress Test, the ten-year CMT changes from its starting level to its new level in equal increments over the first twelve months of the Stress Period, and remains constant at the new level for the remaining 108 months of the Stress Period. The new level of the ten-year CMT in the last 108 months of the down-rate scenario equals the lesser of:

- 1) The average of the ten-year CMT for the nine months prior to the start of the Stress Test, minus 600 basis points; or
- 2) The average yield of the ten-year CMT for the 36 months prior to the start of the Stress Test, multiplied by 60 percent;

but in no case less than 50 percent of the average for the nine months preceding the start of the Stress Period.

b. *Up-Rate Scenario.* In the Stress Test, the ten-year CMT changes from its starting level to its new level in equal increments over the first twelve months of the Stress Period, and remains at the new level for the remaining 108 months of the Stress Period. The new level of the ten-year CMT in the last 108 months of the up-rate scenario is the greater of:

- 1) The average of the ten-year CMT for the nine months prior to the start of the Stress Test, plus 600 basis points; or
- 2) The average of the ten-year CMT for the 36 months prior to the start of the Stress Test, multiplied by 160 percent;

but in no case greater than 175 percent of the average of the ten-year CMT for the nine months preceding the start of the Stress Period.

2. Project the 1-month Treasury and other CMT yields:

a. *Down-Rate Scenario.* For the down-rate scenario, the new value of each of the other Treasury and CMT yields for the last 108 months of the Stress Test is calculated by multiplying the ten-year CMT by the appropriate ratio from Table 3-26. For the first 12 months of the Stress Period, the other rates are computed in the same way as the ten-year CMT, i.e. from their time zero levels. Each of the other CMTs changes in equal steps in each of the first twelve months of the Stress Period until it reaches the new level for the remaining 108 months of the Stress Test.

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TABLE 3–26—CMT RATIOS TO THE TEN-YEAR CMT¹

1 MO / 10 YR	0.68271
3 MO / 10 YR	0.73700
6 MO / 10 YR	0.76697
1 YR / 10 YR	0.79995
2 YR / 10 YR	0.86591
3 YR / 10 YR	0.89856
5 YR / 10 YR	0.94646
20 YR / 10 YR	1.06246
30 YR / 10 YR	1.03432

¹Source: calculated over the period from May, 1986, through April, 1995.

b. *Up-Rate Scenario.* In the up-rate scenario, all other Treasury and CMT yields are equal to the ten-year CMT in the last 108 months of the Stress Test. Each of the other yields changes in equal increments over the first twelve months of the Stress Test until it equals the ten-year CMT.

3. Project Non-Treasury Interest Rates:

a. *Non-Treasury Rates.* For each of the non-Treasury interest rates with the exception of mortgage rates, rates during the Stress Test are computed as a propor-

tional spread to the nearest maturity Treasury yield as given in Table 3-27. The proportional spread is the average over the two years prior to the start of the Stress Test, of the difference between the non-Treasury rate and the comparable maturity Treasury yield divided by that Treasury yield. For example, the three month LIBOR proportional spread would be calculated as the two year average of the ratio:

$$\frac{\left(\begin{array}{l} \text{3-month LIBOR minus} \\ \text{3-month Treasury} \end{array} \right)}{\text{3-month Treasury}}$$

During the Stress Test, the 3-month LIBOR rate is projected by multiplying the 3-month Treasury yield by 1 plus this average proportional spread.

b. *Mortgage Rates.* Mortgage interest rates are projected as described in this section for other non-Treasury interest rates, except that an average of the additive, not proportional, spread to the appropriate Treasury interest rate is used. For example, the 30-year Conventional Mortgage Rate spread is projected as the average, over the two years preceding the start of the Stress Test, of: (Conventional Mortgage Rate minus the ten-year CMT). This spread is then added to the ten-year CMT for the 120 months of the Stress Test to obtain the projected Conventional Mortgage Rate.

TABLE 3–27—NON-TREASURY INTEREST RATES

Mortgage Rates	Spread Based on
15-year Fixed-rate Mortgage Rate	10-year CMT
30-year Conventional Mortgage Rate	10-year CMT
7-year Balloon Mortgage Rate	(computed from Conventional Mortgage Rate)
Constant Maturity Mortgage Index	10-year CMT
Other Non-Treasury Interest Rates	
Overnight Fed Funds	1-month Treasury Yield
7-day Fed Funds	1-month Treasury Yield
1-month LIBOR	1-month Treasury Yield
1-month Federal Agency Cost of Funds	1-month Treasury Yield
1-mo Freddie Mac Reference Bill	1-month Treasury Yield
3-month LIBOR	3-month CMT
3-month Federal Agency Cost of Funds	3-month CMT
PRIME	3-month CMT

TABLE 3--27—NON-TREASURY INTEREST RATES—Continued

Mortgage Rates	Spread Based on
6-month LIBOR	6-month CMT
6-month Federal Agency Cost of Funds	6-month CMT
6-month Fed Funds	6-month CMT
FHLB 11th District Cost of Funds	1-year CMT
12-month LIBOR	1-year CMT
12-mo Moving Treasury Average	1-year CMT
Certificate of Deposits Index	1-year CMT
1-year Federal Agency Cost of Funds	1-year CMT
2-year Federal Agency Cost of Funds	2-year CMT
3-year Federal Agency Cost of Funds	3-year CMT
5-year Federal Agency Cost of Funds	5-year CMT
10-year Federal Agency Cost of Funds	10-year CMT
30-year Federal Agency Cost of Funds	30-year CMT
2-yr Swap	2-year CMT
3-yr Swap	3-year CMT
5-yr Swap	5-year CMT
10-yr Swap	10-year CMT
30-yr Swap	30-year CMT

c. *Enterprise Borrowing Rates.* In the Stress Test, the Federal Agency Cost of Funds Index is the same as the Enterprise Cost of Funds Index during the Stress Period, except that the Stress Test adds a 10 basis-point credit spread to the Federal Agency Cost of Funds rates to project Enterprise Cost of Funds rates for the last 108 months of the Stress Period.

3.3.4 Interest Rates Outputs

Interest Rate outputs are monthly values for: the projected ten points on the Treasury yield curve (1-month, 3-month, 6-month, 1-year, 2-year, 3-year, 5-year, 10-year, 20-year and 30-year); the 21 non-Treasury rates contained in Table 3-27; and the nine points on the Enterprise Cost of Funds curve.

3.4 Property Valuation

3.4.1 Property Valuation Overview

[a] The Property Valuation component applies inflation adjustments to the single family house price growth rates and multi-

family rent growth rates that are used to determine single family property values and multifamily current debt-service coverage ratios during the up-rate scenario, as required by the 1992 Act.

[b] Single family house price growth rates during the 120 months of the Stress Test are calculated from the HPI series for the West South Central Census Division for the years 1984-1993, as derived from OFHEO's Third Quarter, 1996 HPI Report. The West South Central Census Division includes Texas and all of the Benchmark states except Mississippi. This series is applied to single family loans nationwide during the Stress Test because the 1992 Act applies a regional loss experience (the BLE) to the entire nation. In contrast, house prices are brought forward to the start of the Stress Test based on local Census Division HPI values available at the start of the Stress Test.

[c] Multifamily rent growth rates during the 120 months of the Stress Test are computed using a population-weighted average of the monthly growth of the Rent of Primary

Residence component of the Consumer Price Index-Urban, which is generated by the U.S. Department of Labor Bureau of Labor Statistics. The metropolitan areas used for this computation are the Dallas/Ft. Worth CMSA, the Houston/Galveston/Brazoria CMSA, and the New Orleans MSA.

[d] Multifamily rental vacancy rates during the 120 months of the Stress Test are computed using a population-weighted average of annual rental vacancy rates from the U.S. Department of Commerce, Bureau of the Census' Housing Vacancy Survey. The metropolitan areas used for this computation are the Dallas, Houston and Fort Worth PMSAs and the San Antonio, New Orleans and Oklahoma City MSAs.

[e] *Inflation adjustment.* In the up-rate scenario, if the ten-year CMT rises more than 50

percent above the average yield during the nine months preceding the Stress Period, rent and house price growth rates are adjusted to account for inflation as required by the 1992 Act. The single family House Price Growth Rates and the multifamily Rent Growth Rates are increased by the amount by which the ten-year CMT exceeds 50 percent of its annualized monthly yield averaged over the nine months preceding the Stress Test. The inflation adjustment is applied only in the last 60 months of the Stress Period.

3.4.2 Property Valuation Inputs

The inputs required for the Property Valuation component are set forth in Table 3-28.

TABLE 3-28—PROPERTY VALUATION INPUTS

Variable	Description	Source
CMT10 _m	10-year CMT yield for months m = 1...120 of the Stress Test	section 3.3, Interest Rates
ACMT ₀	Unweighted nine-month average of the ten-year CMT yield for the nine months immediately preceding the Stress Test. (Monthly rates are unweighted monthly averages of daily rates, bond equivalent yield)	section 3.3, Interest Rates
HHPGR _q ^{HSP}	Quarterly single family historical house price growth rates computed from the HPI series for the Benchmark region and time period, unadjusted for inflation. The specific series is the West South Central Census Division for the years 1984–1993, as reported in OFHEO's Third Quarter, 1996 HPI Report	Table 3–19 of section 3.1.3, Public Data
RG _m ^{HSP}	Multifamily Rent Growth Rates for months m = 1...120 of the Benchmark region and time period, unadjusted for inflation	Table 3–20 of section 3.1.3, Public Data
RVR _m ^{HSP}	Multifamily Rental Vacancy Rates for months m = 1...120 of the Benchmark region and time period	Table 3–20 of section 3.1.3, Public Data

3.4.3 Property Valuation Procedures for Inflation Adjustment

[a] Calculate inflation-adjusted House Price Growth Rates and Rent Growth Rates using the following six steps:

1. Calculate the Inflation-Adjustment (IA) for the up-rate stress test, as follows:

$$IA = \max \left[\begin{matrix} CMT10^{MAX} \\ -(1.50 \times ACMT_0), 0 \end{matrix} \right]$$

Where:

CMT10^{MAX} is the value of the ten-year CMT during the last 108 months of the up-rate Stress Test.

2. The Inflation Adjustment (IA) is compounded annually over 9 years and 2

months (110 months) to obtain the Cumulative Inflation Adjustment (CIA) according to the following equation:

$$CIA = (1 + IA)^{\frac{110}{12}}$$

3. For single family house prices, convert the CIA to continuously compounded quarterly factors, the Quarterly House Price Growth Adjustments (QHGA_q), which take on positive values only in the last twenty quarters of the Stress Test, using:

$$QHGA_q = \frac{\ln(CIA)}{20} \text{ for } q = 21 \dots 40$$

in the up-rate Stress Test

$QHGA_q = 0$, otherwise

4. For Multifamily rent growth, the CIA is converted to discrete monthly factors or Monthly Rent Growth Adjustments (MRGA_m), and is applied only in the last 60 months of the Stress Test in the up-rate scenario, as follows:

$$MRGA_m = \left[(CIA)^{\frac{1}{60}} - 1 \right] \text{ for } m = 61 \dots 120$$

in the up-rate Stress Test

$MRGA_m = 0$, otherwise

5. Calculate the inflation-adjusted House Price Growth Rates (HPGR_q), used in updating single family house prices during the Stress Test:

$$HPGR_q = HHPGR_q^{HSP} + QHGA_q$$

6. Calculate inflation-adjusted Rent Growth Rates (RGR_m), used in updating Multifamily debt-service coverage ratios during the Stress Test:

$$RGR_m = RG_m^{HSP} + MRGA_m$$

3.4.4 Property Valuation Outputs

[a] The outputs of the Property Valuation component of the Stress Test are set forth in Table 3-29.

TABLE 3-29—PROPERTY VALUATION OUTPUTS

Variable	Description
HPGR _q	House price growth rates for quarters 1...40 of the Stress Test, adjusted for inflation, if applicable.
RGR _m	Multifamily Rent Growth Rates for months m = 1...120 of the Stress Test, adjusted for inflation, if applicable.
RVR _m	Multifamily Rental Vacancy Rates for months m = 1...120 of the Stress Test.

[b] Inflation-adjusted House Price Growth Rates (HPGR_q) are inputs to the Single Family Default and Prepayment component of the Stress Test (see section 3.6.3.4, of this Appendix). Inflation-adjusted Rent Growth Rates (RGR_m) and Rental Vacancy Rates (RVR_m) are inputs to the Multifamily Default and Prepayment component (see section 3.6.3.5, of this Appendix).

3.5 Counterparty Defaults

3.5.1 Counterparty Defaults Overview

The Counterparty Defaults component of the Stress Test accounts for the risk of default by credit enhancement and derivative contract counterparties, corporate securities, municipal securities, and mortgage-related securities. The Stress Test recognizes five rating categories (“AAA”, “AA”, “A”, “BBB”, and “Below BBB and Unrated”) and establishes appropriate credit loss factors that are applied during the Stress Period. Securities rated below BBB are treated as unrated securities, unless OFHEO determines to specify a different treatment upon

a showing by an Enterprise that a different treatment is warranted.

3.5.2 Counterparty Defaults Input

For counterparties and securities, information on counterparty type and the lowest public rating of the counterparty is required. The Stress Test uses credit ratings issued by Nationally Recognized Statistical Rating Organizations (“NRSROs”) to assign rating categories to counterparties and securities. If a counterparty or security has different ratings from different rating agencies, i.e., a “split rating,” or has a long-term rating and a short-term rating, then the lower rating is used.

3.5.3 Counterparty Defaults Procedures

[a] Apply the following three steps to determine maximum haircuts:

1. *Identifying Counterparties.* The Stress Test divides all sources of credit risk other than mortgage default into two categories—(1) derivative contract counterparties and (2) non-derivative

contract counterparties and instruments. Non-derivative contract counterparties and instruments include mortgage insurance (MI) counterparties, seller-servicers, mortgage-related securities such as mortgage revenue bonds (MRBs) and private label REMICS, and nonmortgage investments such as corporate and municipal bonds and asset-backed securities (ABSs).

2. *Classify Rating Categories.*

a. Stress Test rating categories are defined as set forth in Table 3-30. Organizations frequently apply modifiers (numerical, plus, minus) to the generic rating classifications. In order to determine the correct mapping, ignore these modifiers except as noted in Table 3-30.

TABLE 3–30—RATING AGENCIES MAPPINGS TO OFHEO RATINGS CATEGORIES

OFHEO Ratings Category	AAA	AA	A	BBB	Below BBB and Unrated
Standard & Poor’s Long-Term	AAA	AA	A	BBB	Below BBB and Unrated
Fitch Long-Term	AAA	AA	A	BBB	Below BBB and Unrated
Moody’s Long-Term	Aaa	Aa	A	Baa	Below Baa and Unrated
Standard & Poor’s Short-Term	A-1+ SP-1+	A-1 SP-1	A-2 SP-2	A-3	SP-3, B or Below and Unrated
Fitch Short-Term	F-1+	F-1	F-2	F-3	B and Below and Unrated
Moody’s ¹	Prime-1 MIG1 VMIG1	Prime-1 MIG1 VMIG1	Prime-2 MIG2 VMIG2	Prime-3 MIG3 VMIG3	Not Prime, SG and Unrated
Fitch Bank Individual Ratings	A	B A/B	C B/C	D C/D	E D/E
Moody’s Bank Financial Strength Rating	A	B	C	D	E

¹ Any rating that appears in more than one OFHEO category column is assigned the lower OFHEO rating category.

- b. The Stress Test also includes a ratings classification called cash. This includes cash equivalents as defined in FAS 95, Government securities, and securities of the reporting Enterprise.
- c. Unrated, unsubordinated obligations issued by Government Sponsored Enterprises other than the reporting Enterprise are treated as AAA. Unrated seller-servicers are treated as BBB.
- d. The Stress Test will permit a higher rating to be used for an unrated seller-servicer who participates in a multi-family delegated underwriting and servicing program that requires a loss-sharing agreement when: (1) The loss sharing agreement is collateralized by a fully funded reserve account pledged to the Enterprise; and (2) the reserve account is in an amount that is equal to or exceeds the amount that OFHEO has determined to be adequate to support the seller-servicer’s loss-sharing obligation under the program. Determinations of the reserve requirement and of the rating that will be permitted will be made on a pro-

gram-by-program and Enterprise-by-Enterprise basis by the Director.

- 3. *Determine Maximum Haircuts.* The Stress Test specifies the Maximum Haircut (i.e., the maximum reduction applied to cash flows during the Stress Test to reflect the risk of loss due to counterparty (including security) default) by rating category and counterparty type as shown in Table 3-31.
 - a. The Maximum Haircut for a rating category is the product of its default rate and its loss severity rate. For all counterparties, the default rates are 5 percent for AAA, 12.5 percent for AA, 20 percent for A, 40 percent for BBB and 100 percent for Below BBB and Unrated. For non-derivative counterparties, the loss severity rate is 70 percent; for derivative counterparties, it is 10 percent. For all Below BBB and Unrated counterparties, the loss severity rate is 100 percent.
 - b. For periods prior to the implementation of netting, a separate set of Maximum Haircuts (set forth in Table 3-31) will be applied to derivative contract cash flows

to approximate the impact of the net exposures to derivative contract counterparties (see section 3.8.3, Non-mortgage Instrument Procedures). After the implementation of netting, exposures will be netted as described in section 3.8.3 before the haircut is applied.

c. With the exception of haircuts for the Below BBB and Unrated category, hair-

cuts for all counterparty categories are phased-in linearly over the 120 months of the Stress Period. The Maximum Haircut is applied in month 120 of the Stress Period. Haircuts for the Below BBB and Unrated category are applied fully starting in the first month of the Stress Test.

TABLE 3-31—STRESS TEST MAXIMUM HAIRCUT BY RATINGS CLASSIFICATION

Ratings Classification	Derivative Contract Counterparties prior to Implementation of Netting	Derivative Contract Counterparties after Implementation of Netting	Non-Derivative Contract Counterparties or Instruments	Number of Phase-in Months
Cash	0%	0%	0%	N/A
AAA	0.3%	0.5%	3.5%	120
AA	0.75%	1.25%	8.75%	120
A	1.2%	2%	14%	120
BBB	2.4%	4%	28%	120
Below BBB and Unrated	100%	100%	100%	1

3.5.4 Counterparty Defaults Outputs

The Maximum Haircut for a given Counterparty Type and Rating Classification is used in section 3.6, Whole Loan Cash Flows, section 3.7, Mortgage-Related Securities Cash Flows, and section 3.8, Nonmortgage Instrument Cash Flows, of this Appendix.

3.6 Whole Loan Cash Flows

3.6.1 Whole Loan Cash Flows Overview

[a] *Loan Aggregation.* In the Stress Test calculations (except as described in section 3.6.3.6.4, Mortgage Credit Enhancement, of this Appendix), individual loans having similar characteristics are aggregated into Loan Groups as described in section 3.1.2.1, Whole Loan Inputs, of this Appendix (RBC Report). All individual loans within a Loan Group are considered to be identical for computational purposes. In the discussions in this section, quantities described as “loan level” will actually be computed at the Loan Group level.

[b] *Loan Participations.* In some cases, an Enterprise may hold only a *pari passu* fractional ownership interest in a loan. This interest is referred to as a participation, and is specified by the ownership percentage held by the Enterprise (the participation percentage). In such cases, the Unpaid Principal Balance (UPB) and Mortgage Payment reported in the RBC Report will be only the Enterprise’s participation percentage of the loan’s actual UPB and Mortgage Payment. The ac-

tual UPB is not explicitly used in the calculations described in this section 3.6 but it is used in the creation of the RBC Report.

[c] *Retained Loans vs. Sold Loans.* The Stress Test models cash flows from single family and multifamily mortgage loans that are held in portfolio (Retained Loans) and loans that are pooled into Mortgage-Backed Securities (MBSs) that are sold to investors and guaranteed by the Enterprises (Sold Loans). Together, Retained Loans and Sold Loans are referred to as “Whole Loans.” The treatment of cash flows for loans not guaranteed by the Enterprises, e.g., loans backing GNMA Certificates and private label MBSs and REMICs, is discussed in section 3.7, Mortgage-Related Securities Cash Flows, of this Appendix.

[d] *Repurchased MBSs.* From time to time an Enterprise may repurchase all or part of one of its own previously issued single-class MBSs for its own securities portfolio. At an Enterprise’s option, these “Repurchased MBSs” may be reported with the underlying Whole Loans for computation in this section 3.6 rather than in section 3.7, Mortgage-Related Securities Cash Flows, of this Appendix. In such cases, the Enterprise will report the underlying Whole Loans as sold loans, along with the appropriate Fraction Repurchased and any security unamortized balances associated with the purchase of the MBS (not with the original sale of the underlying loans, which unamortized balances are reported separately).

[e] *Sources of Enterprise Whole Loan Cash Flows.* For Retained Loans, the Enterprises receive all principal and interest payments on the loans, except for a portion of the interest payment retained by the servicer as compensation (the Servicing Fee). For Sold Loans, the Enterprises receive Guarantee Fees and Float Income. Float Income is the earnings on the investment of loan principal and interest payments (net of the Servicing Fee and Guarantee Fee) from the time these payments are received from the servicer until they are remitted to security holders. The length of this period depends on the security payment cycle (the remittance cycle). For both retained and sold loans, the Enterprises retain 100 percent of their credit losses and experience amortization of discounts as income and amortization of premiums as expense. For Repurchased MBSs, the Enterprise receives the Fraction Repurchased of the cash flows it remits to investors, and retains 100 percent of the Credit Losses and the Guarantee Fee. *See* section 3.6.3.7, Stress Test Whole Loan Cash Flows and section 3.6.3.8, Whole Loan Accounting Flows, of this Appendix.

[f] *Required Inputs.* The calculation of Whole Loan cash flows requires mortgage Amortization Schedules, mortgage Prepayment, Default and Loss Severity rates, and Credit Enhancement information. The four mortgage performance components of the Stress Test are single family Default and Prepayment, single family Loss Severity, multifamily Default and Prepayment, and multifamily Loss Severity. Mortgage Amortization Schedules are computed from input data in the RBC Report. (For ARMs, selected interest rate indexes from section 3.3, Interest Rates, of this Appendix, are also used.) Prepayment and Default Rates are computed by combining explanatory variables and weighting coefficients according to a set of logistic equations. The explanatory variables are computed from the mortgage Amortization Schedule and external economic variables such as Interest Rates (section 3.3, Interest Rates, of this Appendix), historical house-price indexes (HPIs) or rental-price indexes (RPIs), and Stress Period HPI growth rate, RPI and Vacancy Rate (RVR) series from section 3.4, Property Valuation, of this Appendix. The weighting coefficients determine the relative importance of the different explanatory variables, and are estimated from a statistical analysis of data from the Benchmark Loss region and time period as described in section 1, Identification of the Benchmark Loss Experience, of this Appendix. Mortgage Amortization information is also combined with HPI, RPI and VR series to determine Gross Loss Severity rates, which are offset by Credit Enhancements. Finally, the Amortization Schedules, Default and Prepayment rates and Net Loss Severity rates are combined to produce Stress Test

Whole Loan Cash Flows to the Enterprises for each Loan Group, as well as amortization of any discounts, premiums and fees.

[g] *Specification of Mortgage Prepayment.* Mortgages are assumed to prepay in full. The model makes no specific provision for partial Prepayments of principal (curtailments).

[h] *Specification of Mortgage Default and Loss.* Mortgage Defaults are modeled as follows: Defaulting loans enter foreclosure after a number of missed payments (MQ, Months in Delinquency), and are foreclosed upon several months later. Months in Foreclosure (MF) is the total number of missed payments through foreclosure. Upon completion of foreclosure, the loan as such ceases to exist and the property becomes Real Estate Owned by the lender (REO). Foreclosure expenses are paid and MI proceeds received when foreclosure is completed. After several more months (MR, Months in REO), the property is sold, REO expenses are paid, and sales proceeds and other credit enhancements are received. These timing differences are not modeled explicitly in the cash flows, but their economic effect is taken into account by calculating the present value of the Default-related cash flows back to the initial month of Default.

[i] *Combining Cash Flows from Scheduled Payments, Prepayments and Defaults.* Aggregate Whole Loan Cash Flows, adjusted for the effects of mortgage performance, are based on the following conceptual equation, which is made more explicit in the calculations in the sections specified in section 3.6.2 of this Appendix:

$$\left[\begin{array}{l} \text{Aggregate Cash Flows from} \\ \text{Whole Loans that Default} \\ \text{and Prepay at Rates that} \\ \text{vary in each month } m \end{array} \right] = \left[\begin{array}{l} \left(\begin{array}{l} \text{scheduled Mortgage} \\ \text{Payment} \end{array} \right) \times \\ \left(\begin{array}{l} \text{fraction of loans that remain} \\ \text{on original schedule} \end{array} \right) \\ \text{plus} \\ \left(\begin{array}{l} \text{entire loan UPB plus} \\ \text{final interest payment} \end{array} \right) \times \\ \left(\begin{array}{l} \text{fraction of loans that} \\ \text{Prepay in month } m \end{array} \right) \\ \text{plus} \\ \left(\begin{array}{l} \text{present value of Default-related} \\ \text{receipts minus expenses} \end{array} \right) \times \\ \left(\begin{array}{l} \text{fraction of loans that} \\ \text{Default in month } m \end{array} \right) \end{array} \right]$$

3.6.2 Whole Loan Cash Flows Inputs

Inputs for each stage of the Whole Loan Cash Flows calculation are found in the following sections:

- Section 3.6.3.3.2, Mortgage Amortization Schedule Inputs
- Section 3.6.3.4.2, Single Family Default and Prepayment Inputs
- Section 3.6.3.5.2, Multifamily Default and Prepayment Inputs
- Section 3.6.3.6.2.2, Single Family Gross Loss Severity Inputs
- Section 3.6.3.6.3.2, Multifamily Gross Loss Severity Inputs
- Section 3.6.3.6.4.2, Mortgage Credit Enhancement Inputs
- Section 3.6.3.7.2, Stress Test Whole Loan Cash Flow Inputs
- Section 3.6.3.8.2, Whole Loan Accounting Flows Inputs, of this Appendix

3.6.3 Whole Loan Cash Flows Procedures

3.6.3.1 Timing Conventions

[a] *Calculations are monthly.* The Stress Test operates monthly, with all events of a given type assumed to take place on the same day of the month. For mortgages, unless otherwise specified, all payments and

other mortgage-related cash flows that are due on the first day of the month are received on the fifteenth. Biweekly loans are mapped into their closest term-equivalent monthly counterpart.

[b] *“Time Zero” for Calculations.* Time Zero refers to the beginning of the Stress Test. For example, if the 2Q2000 Stress Test uses Enterprise Data as of June 30, “month zero” represents conditions as of June 30, the Stress Period begins July 1, and July 2000 is month one of the Stress Test. In this document, UPB₀ is the Unpaid Principal Balance of a loan immediately prior to (as of) the start of the Stress Test, i.e. as reported by the Enterprise in the RBC Report. Origination refers to the beginning of the life of the loan, which will be prior to the start of the Stress Test for all loans except those delivered later under Commitments, for which Origination refers to the delivery month (See section 3.2, Commitments, of this Appendix).

[c] *Definition of Mortgage Age.* The Mortgage Age at a given time is the number of scheduled mortgage payment dates that have occurred prior to that time, whether or not the borrower has actually made the payments. Prior to the first payment date, the Mortgage Age would be zero. From the first payment date until (but not including) the second loan payment date, the Mortgage Age would be one. The Mortgage Age at Time Zero (A₀) is thus the number of scheduled loan payment dates that have occurred prior to the start of the Stress Test. The scheduled payment date for all loans is assumed to be the first day of each month; therefore, the Mortgage Age will be A₁ on the first day of the Stress Test (except for Commitments that are delivered after the start of the Stress Test).

[d] *Interest Rate Setting Procedure.* Mortgage interest is due in arrears, i.e., on the first day following the month in which it is accrued. Thus, a payment due on the first day of month m is for interest accrued during the prior month. For example, for Adjustable Rate Mortgages (ARMs) the Mortgage Interest Rate (MIR_m) applicable to the July reset is set on the first day of June, and is generally based on the May or April value of the underlying Index, as specified in the loan terms. This Lookback Period (LB) is specified in the Stress Test as a period of one or two months, respectively. Thus, PMT_m will be based on MIR_m, which is based on INDEX_{m-1-LB}.

[e] *Prepayment Interest Shortfall.* In some remittance cycles, the period between an Enterprise’s receipt of Prepayments and transmittal to investors exceeds a full month. In those cases, the Enterprise must remit an additional month’s interest (at the Pass-Through Rate) to MBS investors. See section 3.6.3.7.3, Stress Test Whole Loan Cash Flow Procedures, of this Appendix.

[f] *Certain Calculations Extend Beyond the End of the Stress Test.* Even though the Stress Test calculates capital only through the ten year Stress Period, certain calculations (for example, the level yield amortization of discounts, premiums and fees, as described in section 3.10, Operations, Taxes, and Accounting, of this Appendix) require cash flows throughout the life of the instrument. For such calculations in the Stress Test, the conditions of month 120 are held constant throughout the remaining life of the instrument: specifically, Interest Rates (which are already held constant for months 13 through 120), Prepayment and Default rates for months $m > 120$ are taken to be equal to their respective values in month 120.

3.6.3.2 Payment Allocation Conventions

3.6.3.2.1 Allocation of Mortgage Interest

[a] *Components of Mortgage Interest.* The interest portion of the Mortgage Payment is allocated among several components. For all Whole Loans, a Servicing Fee is retained by the servicer. For Sold Loans, the Enterprise retains a Guarantee Fee. An additional amount of interest (Spread)¹ may be deposited into a Spread Account to reimburse potential future credit losses on loans covered by this form of Credit Enhancement, as described further in section 3.6.3.6.4, Mortgage Credit Enhancement, of this Appendix. The remaining interest amount is either retained by the Enterprise (Net Yield on Retained Loans) or passed through to MBS investors (Pass-Through Interest on Sold Loans).

[b] *Effect of Negative Amortization.* If the Mortgage Payment is contractually limited to an amount less than the full amount accrued (as may be the case with loans that permit Negative Amortization), then the Servicing Fee, the Guarantee Fee and the spread are paid in full, and the shortfall is borne entirely by the recipient of the Net Yield or Pass-Through Interest.

[c] *Effect of Variable Rates.* For ARMs, the Servicing Fee, Guarantee Fee and Spread rates are taken to be constant over time, as they are for Fixed Rate Loans. Thus in the Stress Test the Mortgage Interest Rate and the Net Yield or Pass-through Rate will change simultaneously by equal amounts. All other details of the rate and payment reset mechanisms are modeled in accordance with the contractual terms using the inputs specified in section 3.6.3.3.2, Mortgage Amortization Schedule Inputs, of this Appendix.

3.6.3.2.2 Allocation of Mortgage Principal

[a] Scheduled Principal is that amount of the mortgage payment that amortizes principal. For calculational purposes, when a

¹The spread may or may not be embedded in the recorded Servicing Fee.

loan prepays in full the amount specified in the Amortization Schedule is counted as Scheduled Principal, and the rest is Prepayment Principal. For a Balloon Loan, the final Balloon Payment includes the remaining UPB, all of which is counted as Scheduled Principal.

[b] Mortgages that prepay are assumed to prepay in full. Partial Prepayments (curtailments) are not modeled.

[c] Any loan that does not prepay or Default remains on its original Amortization Schedule.

3.6.3.3 Mortgage Amortization Schedule

3.6.3.3.1 Mortgage Amortization Schedule Overview

[a] The Stress Test requires an Amortization Schedule for each Loan Group. A mortgage is paid down, or amortized over time, to the extent that the contractual mortgage payment exceeds the amount required to cover interest due.

[b] *Definitions.*

1. *Fully Amortizing Loans.* The Amortization Schedule for a mortgage with age A_0 at the beginning of the Stress Test is generated using the starting UPB (UPB_0), the Remaining Term to Maturity (RM), the remaining Amortization Term ($AT - A_0$), the remaining Mortgage Payments (PMT_m for $m = 1 \dots RM$) and Mortgage Interest Rates (MIR_m for $m = 1 \dots RM$). The Amortization Schedule is generated by repeating the following three steps iteratively until the UPB is zero:

a. Interest Due =

$UPB \times \text{Mortgage Interest Rate}$

b. Principal Amortization = Payment - Interest Due

c. Next period's UPB =

$UPB - \text{Principal Amortization}$

2. *Balloon Loans.* A Balloon Loan matures prior to its Amortizing Term, i.e. before the UPB is fully amortized to zero. Computationally, $AT - A_0 > RM$, usually by at least 180 months. In order that $UPB_{RM} = 0$, the principal component of the resulting lump sum final payment (the Balloon Payment, equal to UPB_{RM-1}) is counted as Scheduled Principal, not as a Prepayment.

[c] *Special Cases.* In general the UPB of a mortgage decreases monotonically over time, i.e. $UPB_m > UPB_{m+1}$, reaching zero at maturity except for Balloon Loans as described in [b]2. in this section. However, in practice certain exceptions must be handled.

1. *Interest-Only Loans.* Certain loans are interest-only for all or part of their term. The monthly payment covers only the interest due, and the UPB stays constant until maturity (in some cases), in which case a Balloon Payment is due or a changeover date (in other cases) at which

time the payment is recast so that the loan begins to amortize over its remaining term. If the loan does not amortize fully over its remaining term, a Balloon Payment will be due at maturity.

2. *Negative Amortization.* For some loans, the UPB may increase for a period of time if the mortgage payment is contractually limited to an amount that is less than the amount of interest due, and the remainder is added to the UPB. At some point, however, the payment must exceed the interest due or else the loan balance will never be reduced to zero. In the calculation, this is permitted to occur only for payment-capped ARMs that contractually specify negative amortization. Certain types of FRMs, notably Graduated Payment Mortgages (GPMs) and Tiered Payment Mortgages (TPMs), also have variable payment schedules that result in negative amortization, but in the Stress Test all such loans are assumed to have passed their negative amortization periods.
3. *Early Amortization.*
 - a. If a borrower has made additional principal payments (curtailments or partial prepayments) on a FRM prior to the start of the Stress Test, the contractual mortgage payment will amortize the loan prior to its final maturity, i.e. $UPB_m = 0$ for some $m < RM$. *This is an acceptable outcome in the Stress Test. Note:* for ARMs, the mortgage payment is recalculated, and thus the amortization schedule is recast to end exactly at $m = RM$, on each rate or payment reset date.
 - b. When this calculation is performed for a fully amortizing FRM using weighted average values to represent a Loan Group, the final scheduled payment may exceed the amount required to reduce the UPB to zero, or the UPB may reach zero prior to month RM . This is because the mortgage payment calculation is nonlinear, and as a result the average mortgage payment is not mathematically guaranteed to amortize the average UPB using the average MIR. This is an acceptable outcome in the Stress Test.
4. *Late Amortization.* According to its contractual terms, the UPB of a mortgage loan must reach zero at its scheduled maturity. The borrower receives a disclosure schedule that explicitly sets forth such an Amortization Schedule. If the characteristics of a mortgage loan representing a Loan Group in the RBC Report do not result in $UPB_{RM} = 0$, it must be for one of three reasons: a data error, an averaging artifact, or an extension of the Amortization Schedule related to a delinquency prior to the start of the Stress Test. In any such case, the Stress Test does not recognize cash flows beyond the scheduled maturity date and

models the performing portion of UPB_{RM} in month RM as a credit loss.

5. *Biweekly Loans.* Biweekly loans are mapped into the FRM category that most closely approximates their final maturity.
6. *Step-Rate (or "Two-Step") Loans.* Certain loans have an initial interest rate for an extended period of time (typically several years) and then "step" to a final fixed rate for the remaining life of the loan. This final fixed rate may be either a predetermined number or a margin over an index. Such loans can be exactly represented as ARMs with the appropriate Initial Mortgage Interest Rate and Initial Rate Period, Index and Margin (if applicable). If the final rate is a predetermined rate (e.g., 8 percent per annum) then the ARM's Maximum and Minimum Rate should be set to that number. The Rate and Payment Reset Periods should be set equal to the final rate period after the step.
7. *Reverse Mortgages.* In a reverse mortgage, a borrower receives one or more payments from the lender and the lender is repaid with a lump sum when the borrower dies, sells the property or moves out of the home permanently. The stress test models reverse mortgages as a ladder of zero-coupon securities:
 - a. 11 proxy securities for each reverse mortgage program are created.
 - b. A 10% conditional payment rate is used to create the zero-coupon securities that will mature in every year of the stress test. The zero-coupon securities are a ladder series of floating-rate coupon-bearing accreting bonds with a first payment date at maturity.
 - c. The 11th zero-coupon security will mature three months after the stress test to reflect the 35% of UPB not paid down during the stress period.
 - d. An OFHEO credit rating equivalent to AAA for the FHA insured programs and AA for other reverse mortgage programs is assigned.
8. *Split-Rate ARM Loans.* In split-rate ARM loans, the principal portion of the payment is based on a fixed-rate amortization schedule while the interest portion is based on a floating rate index. These multifamily loans are available as fully amortizing product or with a balloon feature. The stress test model does not provide treatment for split-rate ARM loans. Split-rate loans shall be treated as ARMs when they are issued without a balloon payment feature or as Balloon ARMs when the loans contain a balloon payment feature.

3.6.3.3.2 Mortgage Amortization Schedule
Inputs

The inputs needed to calculate the amortization schedule are set forth in Table 3–32:

TABLE 3–32—LOAN GROUP INPUTS FOR MORTGAGE AMORTIZATION CALCULATION

Variable*	Description	Source
	Rate Type (Fixed or Adjustable)	RBC Report
	Product Type (30/20/15-Year FRM, ARM, Balloon, Government, etc.)	RBC Report
UPB _{ORIG}	Unpaid Principal Balance at Origination (aggregate for Loan Group)	RBC Report
UPB ₀	Unpaid Principal Balance at start of Stress Test (aggregate for Loan Group)	RBC Report
MIR ₀	Mortgage Interest Rate for the Mortgage Payment prior to the start of the Stress Test, or Initial Mortgage Interest Rate for new loans (weighted average for Loan Group) (expressed as a decimal per annum)	RBC Report
PMT ₀	Amount of the Mortgage Payment (Principal and Interest) prior to the start of the Stress Test, or first payment for new loans (aggregate for Loan Group)	RBC Report
AT	Original loan Amortizing Term in months (weighted average for Loan Group)	RBC Report
RM	Remaining term to Maturity in months (i.e., number of contractual payments due between the start of the Stress Test and the contractual maturity date of the loan) (weighted average for Loan Group)	RBC Report
A ₀	Age immediately prior to the start of the Stress Test, in months (weighted average for Loan Group)	RBC Report
	Interest-only Flag	RBC Report
RIOP	Remaining Interest-only period, in months (weighted average for loan group)	RBC Report
Additional Interest Rate Inputs		
GFR	Guarantee Fee Rate (weighted average for Loan Group) (decimal per annum)	RBC Report
SFR	Servicing Fee Rate (weighted average for Loan Group) (decimal per annum)	RBC Report
Additional Inputs for ARMs (weighted averages for Loan Group, except for Index)		
INDEX _m	Monthly values of the contractual Interest Rate Index	section 3.3, Interest Rates
LB	Look-Back period, in months	RBC Report
MARGIN	Loan Margin (over index), decimal per annum	RBC Report
RRP	Rate Reset Period, in months	RBC Report
	Rate Reset Limit (up and down), decimal per annum	RBC Report

TABLE 3-32—LOAN GROUP INPUTS FOR MORTGAGE AMORTIZATION CALCULATION—Continued

Variable*	Description	Source
	Maximum Rate (life cap), decimal per annum	RBC Report
	Minimum Rate (life floor), decimal per annum	RBC Report
NAC	Negative Amortization Cap, decimal fraction of UPB _{ORIG}	RBC Report
	Unlimited Payment Reset Period, in months	RBC Report
PRP	Payment Reset Period, in months	RBC Report
	Payment Reset Limit, as decimal fraction of prior payment	RBC Report
IRP	Initial Rate Period, in months	RBC Report

* Variable name is given when used in an equation

3.6.3.3.3 Mortgage Amortization Schedule Procedures

[a] For each Loan Group, calculate a mortgage Amortization Schedule using the inputs in Table 3-32 and the following ten steps. *Note:* Do not round dollar amounts to the nearest penny.)

For months $m = 1 \dots RM$, calculate quantities for month m based on values from month $m - 1$ as follows:

1. Calculate current month's Mortgage Interest Rate (MIR_m).
 - a. For FRMs: $MIR_m = MIR_0$ for all $m = 1$ to RM
 - b. For ARMs, use the following procedure:
 - 1) If $RRP = PRP$ then month m is a rate reset month if:

$$[A_0 + m - (IRP + 1)] \text{ mod } RRP = 0$$

$$\text{and } A_0 + m - 1 \geq IRP$$

- 2) If $RRP \neq PRP$ then month m is a rate reset month if either:
 - a) $A_0 + m - (IRP + 1) = 0$, or
 - b) $[A_0 + m - 1] \text{ mod } RRP = 0$ and $A_0 + m - 1 \geq IRP$
- 3) If m is a rate reset month, then:

$$MIR_m = INDEX_{m-1-LB} + MARGIN,$$

*but not greater than $MIR_{m-1} + \text{Rate Reset Limit}$
nor less than $MIR_{m-1} - \text{Rate Reset Limit}$
and in no case greater than Maximum Rate
and in no case less than Minimum Rate*

- 4) If month m is not a rate reset month, then $MIR_m = MIR_{m-1}$.
- c. In all cases, $MIR_m = MIR_{120}$ for $m > 120$, and $MIR_m = 0$ for $m > RM$.
2. Calculate current month's Payment (PMT_m).

a. For FRMs:

- 1) For Interest-Only Loans, if $m = RIOP + 1$ then month m is a reset month; recompute PMT_m as described for ARMs in step b.4)b), of this section without applying any payment limit.

$$2) PMT_m = PMT_0 \text{ for all } m = 1 \text{ to } RM$$

b. For ARMs, use the following procedure:

- 1) For Interest Only Loans, if $m = RIOP + 1$ then month m is a payment reset month.
- 2) If $PRP = RRP$, then month m is a payment reset month if m is also a rate reset month.
- 3) If $PRP \neq RRP$ then month m is a payment reset month if:

$$[A_0 + m - 1] \text{ mod } PRP = 0$$

- 4) If month m is a payment reset month, then:

a) For loans in an Interest-only Period,

$$PMT_m = UPB_{m-1} \times \frac{MIR_m}{12}$$

- b) Otherwise, PMT_m = the amount that will fully amortize the Loan over its remaining Amortizing Term (i.e. $AT - A_0 - m + 1$ months) with a *fixed* Mortgage Interest Rate equal to MIR_m as determined in Step 1 of this section

but not greater than $PMT_{m-1} \times (1 + \text{Payment Reset Limit Up})$

nor less than $PMT_{m-1} \times (1 - \text{Payment Reset Limit Down})$

unless month m is the month following the end of an Unlimited Payment Reset Period, in which case PMT_m is not subject to any reset limitations.

- 5) If month m is not a payment reset month, then $PMT_m = PMT_{m-1}$
- 6) If, in any month,

$$UPB_{m-1} \times \left(1 + \frac{MIR_m}{12} \right) - PMT_m$$

$$> UPB_{ORIG} \times NAC,$$

then recalculate PMT_m without applying any Payment Reset Limit.

c. For Balloon Loans, or for loans that have $RLOP = RM$, if $m = RM$ then:

$$PMT_m = UPB_{m-1} \times \left(1 + \frac{MIR_m}{12} \right)$$

d. In all cases, PMT_m should amortize the loan within the Remaining Maturity:

$$PMT_m = 0 \text{ for } m > RM \text{ or after } UPB_m = 0$$

3. Determine Net Yield Rate (NYR_m) and, for sold loans, Pass-Through Rate (PTR_m) applicable to the m^{th} payment:

$$NYR_m = MIR_m - SFR$$

$$PTR_m = NYR_m - GFR$$

4. Calculate Scheduled Interest Accrued (during month $m-1$) on account of the m^{th} payment (SIA_m)

$$SIA_m = UPB_{m-1} \times \frac{MIR_m}{12}$$

5. Calculate the Scheduled Interest component of the m^{th} payment (SI_m)

$$SI_m = \min(SIA_m, PMT_m)$$

6. Calculate Scheduled Principal for the m^{th} payment (SP_m):

$$SP_m = \min(PMT_m - SIA_m, UPB_{m-1})$$

Note: Scheduled Principal should not be greater than the remaining UPB. SPM can be negative if the Scheduled Payment is less than Scheduled Interest Accrued.

7. Calculate Loan Unpaid Principal Balance after taking into account the m^{th} monthly payment (UPB_m):

$$UPB_m = \max(UPB_{m-1} - SP_m, 0)$$

8. In the month when UPB_m is reduced to zero, reset

$$PMT_m = UPB_{m-1} \times \left(1 + \frac{MIR_m}{12} \right)$$

9. Repeat all steps for $m = 1 \dots RM$ or until $UPB_m = 0$.

NOTE: If UPB_{RM} is greater than zero, the performing portion is included in Credit Losses (section 3.6.3.7.3, Stress Test Whole Loan Cash Flow Procedures, of this Appendix).

10. Determine Net Yield Rate (NYR_0) and, for sold loans, Pass-Through Rate (PTR_0) for month 0:

$$NYR_0 = MIR_0 - SFR$$

$$PTR_0 = NYR_0 - GFR$$

3.6.3.3.4 Mortgage Amortization Schedule Outputs

The Mortgage Amortization Schedule Outputs set forth in Table 3–33 are used in section 3.6.3.4, Single Family Default and Prepayment Rates, section 3.6.3.5, Multifamily Default and Prepayment Rates, section 3.6.3.6, Calculation of Single Family and Multifamily Mortgage Losses, section 3.6.3.7, Stress Test Whole Loan Cash Flows, and section 3.6.3.8, Whole Loan Accounting Flows, of this Appendix.

TABLE 3–33—MORTGAGE AMORTIZATION SCHEDULE OUTPUTS

Variable	Description
UPB_m	Unpaid Principal Balance for months $m=1 \dots RM$
MIR_m	Mortgage Interest Rate for months $m=1 \dots RM$
NYR_m	Net Yield Rate for months $m=1 \dots RM$
PTR_m	Passthrough Rate for months $m=1 \dots RM$
SP_m	Scheduled Principal (Amortization) for months $m=1 \dots RM$
SI_m	Scheduled Interest for months $m=1 \dots RM$
PMT_m	Scheduled Mortgage Payment for months $m=1 \dots RM$

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3.6.3.4 Single Family Default and Prepayment Rates

3.6.3.4.1 Single Family Default and Prepayment Overview

[a] The Stress Test projects conditional Default and Prepayment rates for each single family Loan Group for each month of the Stress Period. The conditional rate is the percentage (by principal balance) of the remaining loans in a Loan Group that defaults or prepays during a given period of time. Computing Default and Prepayment rates for a Loan Group requires information on the Loan Group characteristics at the beginning of the Stress Test, historical and projected interest rates from section 3.3, Interest Rates, and house price growth rates and volatility measures from section 3.4, Property Valuation, of this Appendix.

[b] *Explanatory Variables.* Several explanatory variables are used in the equations to determine Default and Prepayment rates for single family loans: Mortgage Age, Original Loan-to-Value (LTV) ratio, Probability of Negative Equity, Burnout, the percentage of Investor-owned Loans, Relative Interest Rate Spread, Payment Shock (for ARMs only), Initial Rate Effect (for ARMs only), Yield Curve Slope, Relative Loan Size, and Mortgage Product Type. Regression coeffi-

cients (weights) are associated with each variable. All of this information is used to compute conditional quarterly Default and Prepayment rates throughout the Stress Test. The quarterly rates are then converted to monthly conditional Default and Prepayment rates, which are used to calculate Stress Test Whole Loan cash flows and Default losses. See section 3.6.3.7, Stress Test Whole Loan Cash Flows, of this Appendix.

[c] The regression coefficients for each Loan Group will come from one of three models. The choice of model will be determined by the values of the single family product code and Government Flag in the RBC Report. See section 3.6.3.4.3.2, Prepayment and Default Rates and Performance Fractions, of this Appendix.

[d] *Special Provision for Accounting Calculations.* For accounting calculations that require cash flows over the entire remaining life of the instrument, Default and Prepayment rates for months beyond the end of the Stress Test are held constant at their values for month 120.

3.6.3.4.2 Single Family Default and Prepayment Inputs

The information in Table 3-34 is required for each single family Loan Group:

TABLE 3-34—SINGLE FAMILY DEFAULT AND PREPAYMENT INPUTS

Variable	Description	Source
PROD	Mortgage Product Type	RBC Report
A ₀	Age <i>immediately prior to</i> start of Stress Test, in months (weighted average for Loan Group)	RBC Report
LTV _{ORIG}	Loan-to-Value ratio at Origination (weighted average for Loan Group)	RBC Report
UPB _{ORIG}	UPB at Origination (aggregate for Loan Group)	RBC Report
MIR _{ORIG}	Mortgage Interest Rate at Origination (“Initial Rate” for ARMs), decimal per annum (weighted average for loan group)	RBC Report
UPB ₀	Unpaid Principal Balance immediately prior to start of Stress Test (aggregate for Loan Group)	RBC Report
UPB _m	Unpaid Principal Balance in months m = 1...RM	section 3.6.3.3.4, Mortgage Amortization Schedule Outputs
MIR _m	Mortgage Interest Rate in months m = 1...RM (weighted average for Loan Group)	section 3.6.3.3.4, Mortgage Amortization Schedule Outputs
MCON _m	Conventional (30 Year Fixed-Rate) Mortgage Rate series projected for months 1...RM and for the 24 months prior to the start of the Stress Test	section 3.3.2, Interest Rates Inputs, and section 3.3.4, Interest Rates Outputs

TABLE 3–34—SINGLE FAMILY DEFAULT AND PREPAYMENT INPUTS—Continued

Variable	Description	Source
T12Y _m	1-year CMT series projected for months 1...120 of the Benchmark region and time period	section 3.3.4, Interest Rates Outputs
T120Y _m	10-year CMT series projected for months 1...120 of the Benchmark region and time period	section 3.3.4, Interest Rates Outputs
HPGR _q	Vector of House Price Growth Rates for quarters q = 1...40 of the Stress Period	section 3.4.4, Property Valuation Outputs
CHPGF ₀ ^{LG}	Cumulative House Price Growth Factor since Loan Origination (weighted average for Loan Group)	RBC Report
α, β	HPI Dispersion Parameters for the Stress Period (Benchmark Census Division, currently West South Central Census Division, as published in the OFHEO House Price Report for 1996:3)	α = 0.002977 β = -0.000024322
IF	Fraction (by UPB, in decimal form) of Loan Group backed by Investor-owned properties	RBC Report
RLS _{ORIG}	Weighted average Relative Loan Size at Origination (Original UPB as a fraction of average UPB for the state and Origination Year of loan origination)	RBC Report

3.6.3.4.3 Single Family Default and Prepayment Procedures

3.6.3.4.3.1 Single Family Default and Prepayment Explanatory Variables

[a] Compute the explanatory variables for single family Default and Prepayment in the seven steps as follows:

1. Calculate A_q, the loan Age in quarters, for quarter q:

$$A_q = \text{int} \left(\frac{A_0}{3} \right) + q,$$

Where:

int means to round to the lower integer if the argument is not an integer.

2. Calculate PNEQ_q, the Probability of Negative Equity in quarter q:

$$PNEQ_q = N \left(\frac{\ln LTV_q}{\sigma_q} \right),$$

where:

N designates the cumulative normal distribution function.

- a. LTV_q is evaluated for a quarter q as:

$$LTV_{ORIG} \times \frac{\left(\begin{array}{c} \text{Ratio of current} \\ \text{Loan Group UPB} \\ \text{to Original UPB} \end{array} \right)}{\left(\begin{array}{c} \text{Ratio of current property} \\ \text{value (based on HPI in} \\ \text{quarter q) to original} \\ \text{property value (based on} \\ \text{HPI at Origination)} \end{array} \right)}$$

The HPI at Origination is updated to the beginning of the Stress Test using actual historical experience as measured by the OFHEO HPI; and then updated within the Stress Test using House Price Growth Factors from the Benchmark region and time period:

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$$LTV_q = LTV_{ORIG} \times \left(\frac{UPB_{m=3q-3}}{UPB_{ORIG}} \right) \left[CHPGF_0^{LG} \times \exp \left(\sum_{k=1}^q HPGR_k \right) \right]$$

Where:

$UPB_{m=3q-3}$ = UPB for the month at the end of the quarter prior to quarter q

$CHPGF_0^{LG}$ = 1.0 if the loan was originated in the same quarter as or after the most recently available HPI as of the reporting date

3. Calculate B_q , the Burnout factor in quarter q. A loan's Prepayment incentive is "burned out" (i.e., reduced) if, during at least two of the previous eight full quarters, the borrower had, but did not take advantage of, an opportunity to reduce his or her mortgage interest rate by at least two percentage points. For this purpose, the mortgage interest rate is compared with values of the Conventional Mortgage Rate (MCON) Index.

a. Compare mortgage rates for each quarter of the Stress Test and for the eight quarters prior to the start of the stress test ($q = -7, -6, \dots, 0, 1, \dots, 40$):

$$b_q = 1 \text{ if } MCON_m + 0.02 \leq MIR_m \text{ for all three months in quarter } q \text{ (i.e., } m = 3q - 2, 3q - 1, 3q),$$

$$b_q = 0 \text{ otherwise}$$

Note: For this purpose, $MCON_m$ is required for the 24 months (eight quarters) prior to the start of the Stress Test. Also, $MIR_m = MIR_0$ for $m < 0$.

b. Determine whether the loan is "burned out" in quarter q (Burnout Flag, B_q^f):

$$B_q^f = 1 \text{ if } b_{q'} = 1 \text{ for two or more quarters } q' \text{ between } q-8 \text{ and } q-1 \text{ inclusive, or since Origination if } 2 < A_q < 8 \text{ (Note: by definition, } B_q = 0 \text{ if } A_q < 3);$$

$$B_q^f = 0 \text{ otherwise}$$

Where:

q' = index variable for prior 8 quarters

c. Adjust for recently originated loans as follows:

$$B_q = 0.25 \times B_q^f \text{ if } A_q = 3 \text{ or } 4$$

$$= 0.50 \times B_q^f \text{ if } A_q = 5 \text{ or } 6$$

$$= 0.75 \times B_q^f \text{ if } A_q = 7 \text{ or } 8$$

$$= B_q^f \text{ otherwise}$$

4. Calculate RS_q , the Relative Spread in quarter q, as the average value of the monthly Relative Spread of the Original mortgage interest rate to the Conventional (30-Year Fixed Rate) Mortgage Rate series for the three months in the quarter.

NOTE: Use the Current MIR for Fixed Rate Loans and the Original MIR for Adjustable Rate Loans.

$$RS_q = \text{avg} \left(\frac{MIR - MCON_m}{MIR} \right)$$

over all three months m in quarter q

If $MIR = 0$, then $RS_q = -0.20$ for all q.

5. Calculate YCS_q , the Yield Curve Slope in quarter q, as the average of the monthly ratio of the 10-Year CMT to the One-Year CMT for the three months in the quarter:

$$YCS_q = \text{avg} \left(\frac{T120Y_m}{T12Y_m} \right)$$

for all three months in quarter q

6. Evaluate the Payment Shock Indicator (PS_q) for ARMs only:

$$PS_q = RS_q \text{ if } PROD = ARM$$

7. Evaluate the Initial Rate Effect Flag ($IREF_q$) for ARMS only:

$$IREF_q = 1 \text{ if } A_q \leq 12 \text{ and } PROD = ARM$$

$$= 0 \text{ otherwise}$$

3.6.3.4.3.2 Prepayment and Default Rates and Performance Fractions

[a] Calculate Prepayment and Default Rates and Performance Fractions using the following five steps:

1. Compute the logits for Default and Prepayment using the formulas for simultaneous processes using inputs from Table 3-34 and explanatory variable coefficients in Table 3-35.

NOTE: $\beta_{B_{Calc},TV}$ is the LTV-specific constant used to calibrate the Default rates to the BLE.

$$X\beta_q = \beta_{A_q} + \beta_{LTV_{ORIG}} + \beta_{PNEQ_q} + \beta_{B_q} B_q + \beta_{IF} IF + \beta_{PS_q} \\ + \beta_{IREF} \times IREF_q + \beta_{Prod} + \beta_{BCal_{LTV}} + \beta_0$$

$$X\gamma_q = \gamma_{A_q} + \gamma_{LTV_{ORIG}} + \gamma_{PNEQ_q} + \gamma_{B_q} B_q + \gamma_{IF} IF + \gamma_{RS_q} + \gamma_{PS_q} \\ + \gamma_{YCS_q} + \gamma_{IREF} \times IREF_q + \gamma_{RLS_{ORIG}} + \gamma_{Prod} + \gamma_0$$

TABLE 3–35—COEFFICIENTS FOR SINGLE FAMILY DEFAULT AND PREPAYMENT EXPLANATORY VARIABLE

Explanatory Variable (V)	30-Year Fixed-Rate Loans		Adjustable-Rate Loans (ARMs)		Other Fixed-Rate Loans	
	Default Weight (β_v)	Prepayment Weight (γ_v)	Default Weight (β_v)	Prepayment Weight (γ_v)	Default Weight (β_v)	Prepayment Weight (γ_v)
A_q						
$0 \leq A_q \leq 4$	-0.6276	-0.6122	-0.7046	-0.5033	-0.7721	-0.6400
$5 \leq A_q \leq 8$	-0.1676	0.1972	-0.2259	0.1798	-0.2738	0.1721
$9 \leq A_q \leq 12$	-0.05872	0.2668	0.01504	0.2744	-0.09809	0.2317
$13 \leq A_q \leq 16$	0.07447	0.2151	0.2253	0.2473	0.1311	0.1884
$17 \leq A_q \leq 20$	0.2395	0.1723	0.3522	0.1421	0.3229	0.1900
$21 \leq A_q \leq 24$	0.2773	0.2340	0.4369	0.1276	0.3203	0.2356
$25 \leq A_q \leq 36$	0.2740	0.1646	0.2954	0.1098	0.3005	0.1493
$37 \leq A_q \leq 48$	0.1908	-0.2318	0.06902	-0.1462	0.2306	-0.2357
$49 \leq A_q$	-0.2022	-0.4059	-0.4634	-0.4314	-0.1614	-0.2914
LTV_{ORIG}						
$LTV_{ORIG} \leq 60$	-1.150	0.04787	-1.303	0.08871	-1.280	0.02309
$60 < LTV_{ORIG} \leq 70$	-0.1035	-0.03131	-0.1275	-0.005619	-0.06929	-0.02668
$70 < LTV_{ORIG} \leq 75$	0.5969	-0.09885	0.4853	-0.09852	0.6013	-0.05446
$75 < LTV_{ORIG} \leq 80$	0.2237	-0.04071	0.1343	-0.03099	0.2375	-0.03835
$80 < LTV_{ORIG} \leq 90$	0.2000	-0.004698	0.2576	0.004226	0.2421	-0.01433
$90 < LTV_{ORIG}$	0.2329	0.1277	0.5528	0.04220	0.2680	0.1107
$PNEQ_q$						
$0 < PNEQ_q \leq 0.05$	-1.603	0.5910	-1.1961	0.4607	-1.620	0.5483
$0.05 < PNEQ_q \leq 0.1$	-0.5241	0.3696	-0.3816	0.2325	-0.5055	0.3515
$0.1 < PNEQ_q \leq 0.15$	-0.1805	0.2286	-0.1431	0.1276	-0.1249	0.2178
$0.15 < PNEQ_q \leq 0.2$	0.07961	-0.02000	-0.04819	0.03003	0.07964	-0.02137
$0.2 < PNEQ_q \leq 0.25$	0.2553	-0.1658	0.2320	-0.1037	0.2851	-0.1540
$0.25 < PNEQ_q \leq 0.3$	0.5154	-0.2459	0.2630	-0.1829	0.4953	-0.2723

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TABLE 3–35—COEFFICIENTS FOR SINGLE FAMILY DEFAULT AND PREPAYMENT EXPLANATORY VARIABLE—Continued

Explanatory Variable (V)	30-Year Fixed-Rate Loans		Adjustable-Rate Loans (ARMs)		Other Fixed-Rate Loans	
	Default Weight (β_v)	Prepayment Weight (γ_v)	Default Weight (β_v)	Prepayment Weight (γ_v)	Default Weight (β_v)	Prepayment Weight (γ_v)
$0.3 < PNEQ_q \leq 0.35$	0.6518	-0.2938	0.5372	-0.2075	0.5979	-0.2714
$0.35 < PNEQ_q$	0.8058	-0.4636	0.7368	-0.3567	0.7923	-0.3986
B_q	1.303	-0.3331	0.8835	-0.2083	1.253	-0.3244
RLS						
$0 < RLS_{ORIG} \leq 0.4$	.....	-0.5130	.....	-0.4765	.....	-0.4344
$0.4 < RLS_{ORIG} \leq 0.6$	.....	-0.3264	.....	-0.2970	.....	-0.2852
$0.6 < RLS_{ORIG} \leq 0.75$	.....	-0.1378	.....	-0.1216	.....	-0.1348
$0.75 < RLS_{ORIG} \leq 1.0$	.....	0.03495	.....	0.04045	.....	0.01686
$1.0 < RLS_{ORIG} \leq 1.25$	.....	0.1888	.....	0.1742	.....	0.1597
$1.25 < RLS_{ORIG} \leq 1.5$	.....	0.3136	.....	0.2755	.....	0.2733
$1.5 < RLS_{ORIG}$	.....	0.4399	.....	0.4049	.....	0.4045
IF	0.4133	-0.3084	0.6419	-0.3261	0.4259	-0.3035
RS_q						
$RS_q \leq -0.20$	.....	-1.368	.....	-0.5463	.....	-1.195
$-0.20 < RS_q \leq -0.10$	.....	-1.023	.....	-0.4560	.....	-0.9741
$-0.10 < RS_q \leq 0$	.....	-0.8078	.....	-0.4566	.....	-0.7679
$0 < RS_q \leq 0.10$	.....	-0.3296	.....	-0.3024	.....	-0.2783
$0.10 < RS_q \leq 0.20$	.....	0.8045	.....	0.3631	.....	0.7270
$0.20 < RS_q \leq 0.30$	.....	1.346	.....	0.7158	.....	1.229
$0.30 < RS_q$	.....	1.377	.....	0.6824	.....	1.259
PS_q						
$PS_q \leq -0.20$	.....	.....	0.08490	0.6613	.....	.....
$-0.20 < PS_q \leq -0.10$	.....	.....	0.3736	0.4370	.....	.....
$-0.10 < PS_q \leq 0$	.....	.....	0.2816	0.2476	.....	.....
$0 < PS_q \leq 0.10$	.....	.....	0.1381	0.1073	.....	.....
$0.10 < PS_q \leq 0.20$	.....	.....	-0.1433	-0.3516	.....	.....
$0.20 < PS_q \leq 0.30$	.....	.....	-0.2869	-0.5649	.....	.....
$0.30 < PS_q$	.....	.....	-0.4481	-0.5366	.....	.....
YCS_q						
$YCS_q < 1.0$	.....	-0.2582	.....	-0.2947	.....	-0.2917

TABLE 3–35—COEFFICIENTS FOR SINGLE FAMILY DEFAULT AND PREPAYMENT EXPLANATORY VARIABLE—Continued

Explanatory Variable (V)	30-Year Fixed-Rate Loans		Adjustable-Rate Loans (ARMs)		Other Fixed-Rate Loans	
	Default Weight (β _v)	Prepayment Weight (γ _v)	Default Weight (β _v)	Prepayment Weight (γ _v)	Default Weight (β _v)	Prepayment Weight (γ _v)
1.0 ≤ YCS _q < 1.2	.....	–0.02735	.....	–0.1996	.....	–0.01395
1.2 ≤ YCS _q < 1.5	.....	–0.04099	.....	0.03356	.....	–0.03796
1.5 ≤ YCS _q	.....	0.3265	.....	0.4608	.....	0.3436
IREF _q	.....	.....	0.1084	–0.01382	.....	.....
PROD ARMs	.....	.....	0.8151	0.2453	.....	.....
Balloon Loans	.....	.....	.....	.....	1.253	0.9483
15–Year FRMs	.....	.....	.....	.....	–1.104	0.07990
20–Year FRMs	.....	.....	.....	.....	–0.5834	0.06780
Government Loans	.....	.....	.....	.....	0.9125	–0.5660
B _{Cal} LTV LTV _{ORIG} ≤ 60	2.045	.....	2.045	.....	2.045	.....
60 < LTV _{ORIG} ≤ 70	0.3051	.....	0.3051	.....	0.3051	.....
70 < LTV _{ORIG} ≤ 75	–0.07900	.....	–0.07900	.....	–0.07900	.....
75 < LTV _{ORIG} ≤ 80	–0.05519	.....	–0.05519	.....	–0.05519	.....
80 < LTV _{ORIG} ≤ 90	–0.1838	.....	–0.1838	.....	–0.1838	.....
90 < LTV _{ORIG}	0.2913	.....	0.2913	.....	0.2913	.....
Intercept (β ₀ , γ ₀)	–6.516	–4.033	–6.602	–3.965	–6.513	–3.949

2. The choice of coefficients from Table 3–35 will be governed by the single family product code and Government Flag, according to Table 3–36.

TABLE 3–36—SINGLE FAMILY PRODUCT CODE COEFFICIENT MAPPING

Single Family Product Code	Model Coefficient Applied
Non-Government Loans	
Fixed Rate 30YR	30-Year FRMs
Fixed Rate 20YR	20-Year FRMs
Fixed Rate 15YR	15-Year FRMs
5-Year Fixed Rate Balloon	Balloon Loans
7-Year Fixed Rate Balloon	Balloon Loans
10-Year Fixed Rate Balloon	Balloon Loans

TABLE 3-36—SINGLE FAMILY PRODUCT CODE COEFFICIENT MAPPING—Continued

Single Family Product Code	Model Coefficient Applied
15-Year Fixed Rate Balloon	Balloon Loans
Adjustable Rate	ARMs
Second Lien	Balloon Loans
Other	Balloon Loans
Government Loans	
Government Flag	Model Coefficient Applied
All government loans except for ARMs	Government Loans
Government ARMs	ARMs

3. Compute Quarterly Prepayment and Default Rates (QPR, QDR) from the logistic expressions as follows:

$$QDR_q = \frac{\exp\{X\beta_q\}}{1 + \exp\{X\beta_q\} + \exp\{X\gamma_q\}}$$

$$QPR_q = \frac{\exp\{X\gamma_q\}}{1 + \exp\{X\beta_q\} + \exp\{X\gamma_q\}}$$

4. Convert quarterly rates to monthly rates using the following formulas for simultaneous processes. The quarterly rate for q = 1 gives the monthly rate for months m = 1,2,3, and so on through q = 40:

$$MDR_m = \frac{QDR_q}{QDR_q + QPR_q} \times \left[1 - \left(1 - QDR_q - QPR_q \right)^{\frac{1}{3}} \right]$$

$$MPR_m = \frac{QPR_q}{QDR_q + QPR_q} \times \left[1 - \left(1 - QDR_q - QPR_q \right)^{\frac{1}{3}} \right]$$

5. Calculate Defaulting Fraction (DEF), Pre-paying Fraction (PRE), and Performing Fraction (PERF) of the Initial Loan Group. Initially (at the beginning of the Stress Test), all loans are assumed to be performing, i.e. PERF₀ = 1.0. For each month m = 1...RM, calculate the following quantities. *Note:* For m > 120, use and MPR₁₂₀ and MDR₁₂₀:

$$PRE_m = PERF_{m-1} \times MPR_m$$

$$DEF_m = PERF_{m-1} \times MDR_m$$

$$PERF_m = PERF_{m-1} - PRE_m - DEF_m$$

3.6.3.4.4 Single Family Default and Prepayment Outputs

Single family Default and Prepayment outputs are set forth in Table 3-37. Prepayment, Default and Performing Fractions for single family loans for months m = 1...RM are used in section 3.6.3.6, Calculation of Single Family and Multifamily Mortgage Losses; and section 3.6.3.7, Stress Test Whole Loan Cash Flows, of this Appendix. Quarterly LTV ratios are used in section 3.6.3.6.2.3, Single Family Gross Loss Severity Procedures, of this Appendix.

TABLE 3–37—SINGLE FAMILY DEFAULT AND PREPAYMENT OUTPUTS

Variable	Description
LTV_q	Current Loan-to-Value ratio in quarter $q = 1...40$
PRE_m^{SF}	Prepaying Fraction of Initial Loan Group in month $m = 1...RM$ (single family Loans)
DEF_m^{SF}	Defaulting Fraction of Initial Loan Group in month $m = 1...RM$ (single family Loans)
$PERF_m^{SF}$	Performing Fraction of Initial original Loan Group in month $m = 1...RM$ (single family loans)

3.6.3.5 Multifamily Default and Prepayment Rates

3.6.3.5.1 Multifamily Default and Prepayment Rates Overview

[a] The Stress Test projects conditional Default and Prepayment rates for each multifamily Loan Group for each month of the Stress Period. Computing Default rates for a Loan Group requires information on the Loan Group characteristics at the beginning of the Stress Test and the economic conditions of the Stress Period—interest rates (section 3.3 of this Appendix), vacancy rates and rent growth rates (section 3.4 of this Appendix). These input data are used to create values for the explanatory variables in the Multifamily Default component.

[b] *Explanatory Variables for Default Rates.* Eight explanatory variables are used as specified in the equations in section 3.6.3.5.3.1, of this Appendix, to determine Default rates for multifamily loans: Mortgage Age, Mortgage Age Squared, New Book indicator, Not Ratio-updated ARM indicator, current Debt-Service Coverage Ratio, Underwater Current Debt-Service Coverage indicator, Loan-To-Value Ratio at origination/acquisition, and a Balloon Maturity indicator. Regression coefficients (weights) are associated with each

variable. All of this information is used to compute conditional annual Default rates throughout the Stress Test. The annualized Default rates are converted to monthly conditional Default rates and are used together with monthly conditional Prepayment rates to calculate Stress Test Whole Loan Cash Flows. (See section 3.6.3.7, Stress Test Whole Loan Cash Flows, of this appendix).

[c] *Specification of Multifamily Prepayment Rates.* Multifamily Prepayment rates are not generated by a statistical model but follow a set of Prepayment rules that capture the effect of yield maintenance, Prepayment penalties and other mechanisms that effectively curtail or eliminate multifamily Prepayments for a specified period of time.

[d] *Special Provision for Accounting Calculations.* For accounting calculations, which require cash flows over the entire remaining life of the instrument, Default and Prepayment rates for months beyond the end of the Stress Test are held constant at their values for month 120.

3.6.3.5.2 Multifamily Default and Prepayment Inputs

The information in Table 3-38 is required for each multifamily Loan Group:

TABLE 3–38—LOAN GROUP INPUTS FOR MULTIFAMILY DEFAULT AND PREPAYMENT CALCULATIONS

Variable	Description	Source
	Mortgage Product Type	RBC Report
A_0	Age immediately prior to start of Stress Test, in months (weighted average for Loan Group)	RBC Report
NBF	New Book Flag	RBC Report
RUF	Ratio Update Flag	RBC Report
LTV_{ORIG}	Loan-to-Value ratio at loan Origination	RBC Report
DCR_0	Debt Service Coverage Ratio at the start of the Stress Test	RBC Report

TABLE 3-38—LOAN GROUP INPUTS FOR MULTIFAMILY DEFAULT AND PREPAYMENT CALCULATIONS—Continued

Variable	Description	Source
PMT ₀	Amount of the mortgage Payment (principal and interest) prior to the start of the Stress Test, or first Payment for new loans (aggregate for Loan Group)	RBC Report
PPEM	Prepayment Penalty End Month number in the Stress Test (weighted average for Loan Group)	RBC Report
RM	Remaining term to Maturity in months (i.e., number of contractual payments due between the start of the Stress Test and the contractual maturity date of the loan) (weighted average for Loan Group)	RBC Report
RGR _m	Benchmark Rent Growth for months m = 1...120 of the Stress Test	section 3.4.4, Property Valuation Outputs
RVR _m	Benchmark Vacancy Rates for months m = 1...120 of the Stress Test	section 3.4.4, Property Valuation Outputs
PMT _m	Scheduled Payment for months m = 1... RM	section 3.6.3.3.4, Mortgage Amortization Schedule Outputs
OE	Operating expenses as a share of gross potential rents (0.472)	fixed decimal from Benchmark region and time period
RVR ₀	Initial rental vacancy rate	0.10

3.6.3.5.3 Multifamily Default and Prepayment Procedures

3.6.3.5.3.1 Explanatory Variables

[a] Compute the explanatory variables for multifamily Default and Prepayment in five steps as follows:

1. Calculate Loan Age in Years for months m = 0...120 of the Stress Test (AY_m):

$$AY_m = \frac{A_0 + m}{12}$$

Where:

A₀ + m is Loan Age in months at the beginning of month m of the Stress Test.

NOTE: AY_m is calculated for each month m, whereas the corresponding Age variable for single family Loans A_q is calculated only quarterly.

2. Assign product and ratio update flags (NBF, NRAF). Note: these values do not change over time for a given Loan Group.

a. New Book Flag (NBF):

NBF = 1 for Fannie Mae loans acquired after 1987 and Freddie Mac loans acquired after 1992, except for loans that were refinanced to avoid a Default on a loan originated or acquired earlier.

NBF = 0 otherwise.

b. Not Ratio-updated Arm Flag (NRAF):

NRAF = 1 if both ARMF = 1 and RUF = 0, NRAF = 0 otherwise.

Where:

ARMF = 1 for ARMs (including Balloon ARMs)

ARMF = 0 otherwise, and

RUF = 1 if the LTV and DCR were calculated or delegated to have been calculated at origination or recalculated or delegated to have been recalculated at Enterprise acquisition according to current Enterprise standards.

RUF = 0 otherwise

3. Calculate Debt Service Coverage Ratio in month m (DCR_m):

The standard definition of Debt Service Coverage Ratio is current net operating income divided by current mortgage payment. However, for the Stress Test, update DCR_m each month from the prior month's value using Rent Growth Rates (RGR_m) and Rental Vacancy Rates (RVR_m) starting with DCR_m from Table 3-38, as follows:

$$DCR_m = DCR_{m-1}$$

$$\times \left[\frac{(1 + RGR_m) \left(\frac{1 - OE - RVR_m}{1 - OE - RVR_{m-1}} \right)}{\frac{PMT_m}{PMT_{m-1}}} \right]$$

4. Assign Underwater Debt-Service Coverage Flag (UWDCRF_m):

UWDCRF_m = 1 if DCR_m < 0.98 in month m
 UWDCRF_m = 0 otherwise.

5. Assign Balloon Maturity Flag (BMF_m) for any Balloon Loan that is within twelve months of its maturity date:

$$BMF_m = 1 \text{ if } RM - m < 12$$

$$BMF_m = 0 \text{ otherwise.}$$

3.6.3.5.3.2 Default and Prepayment Rates and Performance Fractions

[a] Compute Default and Prepayment Rates and Performance Fractions for multifamily loans in the following four steps:

1. Compute the logits for multifamily Default using inputs from Table 3-38 and coefficients from Table 3-39. For indexing purposes, the Default rate for a period m is the likelihood of missing the m_m payment; calculate its corresponding logit (Xδ_m) based on Loan Group characteristics as of the period prior to m, i.e. prior to making the mth payment.

$$\begin{aligned} X\delta_m = & \delta_{AY}AY_{m-1} + \delta_{AY^2}AY_{m-1}^2 \\ & + \delta_{NBF}NBF + \delta_{NRAF}NRAF \\ & + \delta_{DCR} \ln(DCR_{m-1}) \\ & + \delta_{UWDCRF}UWDCRF_{m-1} \\ & + \delta_{LTV} \ln(LTV_{ORIG}) \\ & + \delta_{BMF}BMF_{m-1} + \delta_0 \end{aligned}$$

TABLE 3-39—EXPLANATORY VARIABLE COEFFICIENTS FOR MULTIFAMILY DEFAULT

Explanatory Variable (V)	Default Weight (δ _v)
AY	0.5256
AY ²	0.0284
NBF	-1.219
NRAF	0.4193
DCR	-2.368
UWDCRF	1.220
LTV	0.8165

TABLE 3-39—EXPLANATORY VARIABLE COEFFICIENTS FOR MULTIFAMILY DEFAULT—Continued

Explanatory Variable (V)	Default Weight (δ _v)
BMF Intercept (δ ₀)	1.518 -4.553

2. Compute Annual Prepayment Rate (APR) and Annual Default Rate (ADR) as follows:

$$ADR_m = \frac{\exp\{X\delta_m\} \times (1 - APR_m)}{1 + \exp\{X\delta_m\}}$$

APR_m is a constant, determined as follows:

- For the up-rate scenario, APR_m = 0 for all months m
- For the down-rate scenario, APR_m = 0 percent during the Prepayment penalty period (i.e., when m ≤ PPEM)
 APR_m = 25 percent after the Prepayment penalty period (i.e., when m > PPEM)

3. Convert annual Prepayment and Default rates to monthly rates (MPR and MDR) using the following formulas for simultaneous processes:

$$\begin{aligned} MPR_m = & \frac{APR_m}{ADR_m + APR_m} \\ & \times \left[1 - (1 - ADR_m - APR_m)^{\frac{1}{12}} \right] \end{aligned}$$

If both ARMF = 0 and RUF = 0, then

$$\begin{aligned} MDR_m = & \left[\frac{ADR_m}{ADR_m + APR_m} \right. \\ & \left. \times \left[1 - (1 - ADR_m - APR_m)^{\frac{1}{12}} \right] \right] \times 1.2 \end{aligned}$$

otherwise,

$$\begin{aligned} MDR_m = & \frac{ADR_m}{ADR_m + APR_m} \\ & \times \left[1 - (1 - ADR_m - APR_m)^{\frac{1}{12}} \right] \end{aligned}$$

4. Calculate Defaulting Fraction (DEF_m), Prepaying Fraction (PRE_m), and Performing Fraction (PERF_m) of the Initial Loan Group for each month m = 1...RM. Initially (immediately prior to the beginning of the Stress Test), all loans are assumed to be performing, i.e. PERF₀ = 1.0. Note: For m > 120, use MPR₁₂₀ and MDR₁₂₀.

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$$PRE_m = PERF_{m-1} \times MPR_m$$

$$DEF_m = PERF_{m-1} \times MDR_m$$

$$PERF_m = PERF_{m-1} - PRE_m - DEF_m$$

3.6.3.5.4 Multifamily Default and Prepayment Outputs

[a] Multifamily Default and Prepayment Outputs are set forth in Table 3-40.

TABLE 3-40—MULTIFAMILY DEFAULT AND PREPAYMENT OUTPUTS

Variable	Description
PRE_m^{MF}	Prepaying Fraction of initial Loan Group in month $m=1...RM$ (multifamily Loans)
DEF_m^{MF}	Defaulting Fraction of initial Loan Group in month $m=1...RM$ (multifamily Loans)
$PERF_m^{MF}$	Performing Fraction of initial Loan Group in month $m=1...RM$ (multifamily Loans)

[b] Multifamily monthly Prepayment Fractions (PRE_m^{MF}) and monthly Default Fractions (DEF_m^{MF}) for months $m=1...RM$ are used in section 3.6.3.6, Calculation of Single Family and Multifamily Mortgage Losses; section 3.6.3.7, Stress Test Whole Loan Cash Flows, and section 3.6.3.8, Whole Loan Accounting Flows, of this Appendix.

3.6.3.6 Calculation of Single Family and Multifamily Mortgage Losses

3.6.3.6.1 Calculation of Single Family and Multifamily Mortgage Losses Overview

[a] *Definition.* Loss Severity is the net cost to an Enterprise of a loan Default. Though losses may be associated with delinquency, loan restructuring and/or modification and other loss mitigation efforts, foreclosures are the only loss events modeled during the Stress Test.

[b] *Calculation.* The Loss Severity rate is expressed as a fraction of the Unpaid Principal Balance (UPB) at the time of Default. The Stress Test calculates Loss Severity rates for each Loan Group for each month of the Stress Period. Funding costs (and offsetting revenues) of defaulted loans are captured by discounting the Loss Severity elements using a cost-of-funds interest rate

that varies during the Stress Period. Table 3-41 specifies the Stress Test Loss Severity timeline. Loss Severity rates also depend upon the application of Credit Enhancements and the credit ratings of enhancement providers.

TABLE 3-41—LOSS SEVERITY EVENT TIMING

Month	Event
1	First missed payment
4 (= MQ)	Loan is repurchased from securitized pool and UPB is passed through to MBS investors (Sold Loans only)
13 (= MF^{SF})	Single family foreclosure
18 (= MF^{MF})	Multifamily foreclosure
20 (= $MF^{SF} + MR^{SF}$)	Single family property disposition
31 (= $MF^{MF} + MR^{MF}$)	Multifamily property disposition

[c] *Timing of the Default Process.* Mortgage Defaults are modeled as follows: defaulting loans enter foreclosure after a number of months (MQ, Months in Delinquency) and are foreclosed upon several months later. MF (Months in Foreclosure) is the total number of missed payments. Upon completion of foreclosure, the loan as such ceases to exist and the property becomes Real Estate Owned by the lender (REO). After several more months (MR, Months in REO), the property is sold. Foreclosure expenses are paid and MI proceeds (and, for multifamily loans, loss sharing proceeds) are received when foreclosure is completed. REO expenses are paid, and sales proceeds and other Credit Enhancements are received, when the property is sold. These timing differences are not modeled explicitly in the cash flows, but their economic effect is taken into account by present-valuing the default-related cash flows to the month of Default.

[d] *Gross Loss Severity, Credit Enhancement, and Net Loss Severity.* The calculation of mortgage losses is divided into three parts. First, Gross Loss Severity is determined by expressing the principal loss plus unpaid interest plus expenses as a percentage of the loan UPB at the time of Default (section 3.6.3.6.2, Single Family Gross Loss Severity, and section 3.6.3.6.3, Multifamily Gross Loss Severity, of this Appendix). Second, Credit Enhancements (CEs) are applied according to their terms to offset losses on loans that are covered by one or more CE arrangements (section 3.6.3.6.4, Mortgage Credit Enhancement, of this Appendix). Finally, to account for the timing of these different cash flows,

net losses are discounted back to the month in which the Default initially occurred (section 3.6.3.6.5, Single Family and Multifamily Net Loss Severity, of this Appendix).

3.6.3.6.2 Single Family Gross Loss Severity

3.6.3.6.2.1 Single Family Gross Loss Severity Overview

The Loss Severity calculation adds the discounted present value of various costs and offsetting revenues associated with the foreclosure of single family properties, expressed as a fraction of UPB on the date of Default. The loss elements are:

[a] *Unpaid Principal Balance*. Because all Loss Severity elements are expressed as a fraction of Default date UPB, the outstanding loan balance is represented as 1.

[b] *Unpaid Interest*. Unpaid interest at the Mortgage Interest Rate is included in the MI claim amount. Unpaid interest at the Pass-

Through Rate must be paid to MBS holders until the Defaulted loan is repurchased from the MBS pool.

[c] *Foreclosure Expenses and REO Expenses*. Foreclosure expenses are reimbursed by MI. REO expenses are incurred in connection with the maintenance and sale of a property after foreclosure is completed. Stress Test values for these quantities are derived from historical Enterprise REO experience.

[d] *Net Recovery Proceeds from REO sale (RP)*. This amount is less than the sale price for ordinary properties as predicted by the HPI, because of the distressed nature of the sale.

3.6.3.6.2.2 Single Family Gross Loss Severity Inputs

The inputs in Table 3–42 are used to compute Gross Loss Severity for single family loans:

TABLE 3–42—LOAN GROUP INPUTS FOR GROSS LOSS SEVERITY

Variable	Description	Definition or Source
	Government Flag	RBC Report
MQ	Months Delinquent: time during which Enterprise pays delinquent loan interest to MBS holders	4 for sold loans 0 otherwise
MF	Months to Foreclosure: number of missed payments through completion of foreclosure	13 months
MR	Months from REO acquisition to REO disposition	7 months
F	Foreclosure Costs as a decimal fraction of Defaulted UPB	0.037
R	REO Expenses as a decimal fraction of Defaulted UPB	0.163
DR _m	Discount Rate in month m (decimal per annum)	6-month Enterprise Cost of Funds from section 3.3, Interest Rates
LTV _q	Current LTV in quarter q = 1...40	section 3.6.3.4.4, Single Family Default and Prepayment Outputs
MIR _m	Mortgage Interest Rate in month m (decimal per annum)	section 3.6.3.3.4, Mortgage Amortization Schedule Outputs
PTR _m	Pass-Through Rate applicable to payment due in month m (decimal per annum)	section 3.6.3.3.4, Mortgage Amortization Schedule Outputs
RR	Recovery Rate for Defaulted loans in the BLE, as a percent of predicted house price using HPI (decimal)	0.61

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3.6.3.6.2.3 Single Family Gross Loss Severity Procedures

[a] Calculate single family gross Loss Severity using the following three steps:

1. Compute REO Proceeds in month m (RP_m) as a fraction of Defaulted UPB:

$$RP_m = \frac{RR}{LTV_q}$$

2. Compute MI Claim Amount on loans that Defaulted in month m (CLM_m^{MI}) as a fraction of Defaulted UPB:

$$CLM_m^{MI} = 1 + \left(\frac{MF}{12} \times MIR_m \right) + F$$

for all loans other than Government Loans

$$= 1 + \left(0.75 \times \frac{MF}{12} \times MIR_m \right) + (0.67 \times F) \text{ for Government Loans}$$

Where:

0.67 = FHA reimbursement rate on foreclosure-related expenses

0.75 = adjustment to reflect that FHA reimbursement on unpaid interest is at a government debenture rate, not MIR.

3. Compute Gross Loss Severity of loans that Defaulted in month m (GLS_m) as a fraction of Defaulted UPB:

$$GLS_m = 1 + \left(\frac{MQ}{12} \times PTR_m \right) + F + R - RP_m \text{ but not } < 0$$

3.6.3.6.2.4 Single Family Gross Loss Severity Outputs

The single family Gross Loss Severity outputs in Table 3-43 are used in the Credit Enhancement calculations in section 3.6.3.6.4 of this Appendix.

TABLE 3-43—SINGLE FAMILY GROSS LOSS SEVERITY OUTPUTS

Variable	Description
GLS _m	Gross Loss Severity for loans that defaulted in month m = 1...120
CLM _m ^{MI}	MI claim on account of loans that defaulted in month m = 1...120
RP _m	REO Proceeds on account of loans that defaulted in month m = 1...120

3.6.3.6.3 Multifamily Gross Loss Severity

3.6.3.6.3.1 Multifamily Gross Loss Severity Overview

The multifamily Loss Severity calculation adds the discounted present value of various costs and offsetting revenues associated with the foreclosure of multifamily properties, expressed as a fraction of Defaulted UPB. The loss elements are:

[a] *Unpaid Principal Balance (UPB)*. Because all Loss Severity elements are expressed as a fraction of Default date UPB, the outstanding loan balance is represented as 1.

[b] *Unpaid Interest*. Unpaid interest at the Net Yield Rate is included in the Loss Sharing Claim amount. Unpaid interest at the Pass-Through Rate must be paid to MBS holders until the defaulted loan is repurchased from the MBS pool.

[c] *Net REO Holding Costs (RHC)*. Foreclosure costs, including attorneys fees and other liquidation expenses are incurred between the date of Default and the date of foreclosure completion (REO acquisition). Operating and capitalized expenses are incurred and rental and other income are received between REO acquisition and REO disposition. As a result, half of the Net REO Holding Costs (RHC) are expensed at REO acquisition and the remainder are expensed at REO disposition.

[d] *Net Proceeds from REO sale (RP)*. The gross sale price of the REO less all costs associated with the disposition of the REO asset are discounted from the date of REO sale.

3.6.3.6.3.2 Multifamily Gross Loss Severity Inputs

The inputs in Table 3-44 are used to compute Gross Loss Severity for multifamily Loans:

TABLE 3-44—LOAN GROUP INPUTS FOR MULTIFAMILY GROSS LOSS SEVERITY

Variable	Description	Value or Source
	Government Flag	RBC Report
DR _m	Discount Rate in month m (decimal per annum)	6-month Enterprise Cost of Funds from Section 3.3, Interest Rates
MQ	Time during which delinquent loan interest is passed-through to MBS holders	4 for sold loans 0 otherwise
PTR _m	Pass Through Rate applicable to payment due in month m (decimal per annum)	section 3.6.3.3.4, Mortgage Amortization Schedule Outputs
NYR _m	Net Yield Rate applicable to payment due in month m (decimal per annum)	section 3.6.3.3.4, Mortgage Amortization Schedule Outputs
RHC	Net REO holding costs as a decimal fraction of Defaulted UPB	0.07
MF	Time from Default to completion of foreclosure (REO acquisition)	9 months
MR	Months from REO acquisition to REO disposition	15 months
RP	REO proceeds as a decimal fraction of Defaulted UPB	0.63

3.6.3.6.3.3 Multifamily Gross Loss Severity Procedures

[a] Calculate multifamily gross loss severity in the following two steps:

1. For Conventional Loans, compute the Loss Sharing Claim Amount (CLM_m^{LSA}) and Gross Loss (GLS_m) on loans that Defaulted in month m, as a fraction of Defaulted UPB:

$$CLM_m^{LSA} = 1.75 + \left(\frac{MF}{12} \times NYR_m \right) + RHC - RP$$

$$GLS_m = 1 + \frac{MQ}{12} \times PTR_m + RHC - RP$$

2. For FHA-insured (i.e., government) multifamily Loans, separate Gross Loss Severity and Credit Enhancement calculations are not necessary. Net Loss Severity is determined explicitly in section 3.6.3.6.5,

Single Family and Multifamily Net Loss Severity, of this Appendix).

3.6.3.6.3.4 Multifamily Gross Loss Severity Outputs

Multifamily Gross Loss Severity Outputs in Table 3-45 are used in the Credit Enhancements Calculations section 3.6.3.6.4, of this Appendix.

TABLE 3-45—MULTIFAMILY GROSS LOSS SEVERITY OUTPUTS FOR USE IN CREDIT ENHANCEMENT CALCULATIONS

Variable	Description
GLS _m	Gross Loss Severity for loans that Defaulted in month m = 1...120
CLM _m ^{LSA}	Loss Sharing Claim on account of loans that Defaulted in month m = 1...120

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3.6.3.6.4 Mortgage Credit Enhancement

3.6.3.6.4.1 Mortgage Credit Enhancement Overview

[a] *Types of Mortgage Credit Enhancements.* Credit Enhancements (CE) reimburse losses on individual loans. The CE most often utilized by the Enterprises at the present time is primary Mortgage Insurance (MI) including both private and government MI or loan guarantees (e.g. FHA, VA), which pays claims up to a given limit on each loan. Most other types of CE do not limit the amount payable on each loan individually, but do limit the aggregate amount available under a given CE arrangement or Contract. These two types of CE must be computed differently. To denote this distinction, this Appendix will refer to “Loan Limit” and “Aggregate Limit” CE types. Loan Limit CE includes Mortgage Insurance for single family loans and Loss-Sharing Arrangements (LSA) for multifamily loans. Aggregate Limit CE includes Pool Insurance, Spread Accounts, Letters of Credit, Cash or Collateral Accounts, and Subordination Agreements. For operational convenience in the Stress Test, the Aggregate Limit classification also includes Unlimited Recourse, which has neither loan-level nor aggregate-level coverage limits, and Modified Pool Insurance, Limited Recourse, Limited Indemnification and FHA risk-sharing, which may have both loan-level and aggregate-level coverage limits.

[b] *Loan Limit Credit Enhancements.* Loan Limit Credit Enhancements are applied to every covered loan individually, without regard to how much has been paid on any other covered loan. For example, an MI policy covers losses on an individual loan up to a specified limit. If every loan with MI were to Default, every claim would be payable regardless of the total outlay on the part of the MI provider. Loss Sharing Arrangements on multifamily loans operate the same way.

[c] *Aggregate Limit Credit Enhancements.* Aggregate Limit Credit Enhancements cover a group of loans on an aggregate basis. In most such arrangements, the coverage for any individual loan is unlimited, except that the total outlay by the provider cannot exceed a certain aggregate limit. Thus, the amount of Aggregate Limit coverage available to an individual loan depends, in practice, on how much has been paid on all previous claims under the specified Contract.

[d] *Credit Enhancement Counterparty Defaults.* CE payments from a rated counterparty are subject to Haircuts to simulate counterparty failures during the Stress Test. These Haircuts are based on the rating of the counterparty or guarantor immediately prior to the Stress Test, and are applied each month as described in section 3.5, Counterparty Defaults, of this Appendix.

[e] *Stress Test Application of Credit Enhancement.* The Stress Test calculates mortgage

cash flows for aggregated Loan Groups, within which individual loans are assumed to have identical characteristics, and therefore are not differentiated in the computations. However, a single Loan Group may include loans with Loan Limit CE and/or one or more types of Aggregate Limit CE. Additionally, this coverage may come from a rated provider or from cash or cash-equivalent collateral. Therefore, for computational purposes it is necessary to distinguish among the different possible CE combinations that each loan or subset of loans in a Loan Group may have. In the Stress Test, this is accomplished by creating Distinct Credit Enhancement Combinations (DCCs).

1. *Distinct Credit Enhancement Combinations.*

When aggregating individual loans into Loan Groups for the RBC Report, the applicable CE arrangements will have been identified for each loan:

- a. Loan Group (LG) Number
- b. Initial UPB of individual loan
- c. Rating of MI or LSA Counterparty
- d. Loan-Limit Coverage Percentage for MI or LSA
- e. Contract Number for Aggregate Limit CE, First Priority
- f. Contract Number for Aggregate Limit CE, Second Priority
- g. Contract Number for Aggregate Limit CE, Third Priority
- h. Contract Number for Aggregate Limit CE, Fourth Priority

2. Individual loans for which all of the entries in step 1) of this section (except UPB and Loan-Limit Coverage Percent) are identical, are aggregated into a DCCs. For example, all loans in a given Loan Group with MI from a AAA-rated provider and no other CE would comprise one DCC whose balance is the aggregate of the included loans and whose MI Coverage Percent is the weighted average of that of the included loans. In each month, within each Loan Group, for each DCC, each applicable form of CE is applied in priority order to reduce Gross Loss Severity as much as possible to zero. The total CE payment for each DCC, as a percentage of Defaulted UPB is converted to a total CE payment for each Loan Group and then factored into the calculation of Net Loss Severity in section 3.6.3.6.5, Single Family and Multifamily Net Loss Severity, of this Appendix.

3. *DCC First and Second Priority Available Aggregate CE Balance.* In the Stress Test, First and Second Priority Available Aggregate CE Balances are allocated to the DCCs that are parties to each Contract on a pro-rata basis. Third and Fourth Priority Aggregate Limit Contracts are not modeled because they are extremely rare. In each month of the Stress Test

these CE Balances, adjusted by appropriate Haircuts, are reduced by the losses incurred by each DCC that is a party to each Contract. Spread Account deposits, if applicable, are included in the First and Second Priority DCC Available Aggregate CE Balances.

- a. Spread Accounts may take one of two forms: Balance-Limited, or Deposit-Limited. A Balance-Limited Spread Account receives monthly spread payments based on the UPB of the covered loans until a required balance is achieved and maintained. Any amounts paid to cover losses must be replenished by future spread payments from the covered loans that are still performing. Thus, there is no known limit to the amount of spread deposits that may be made over the life of the covered loans. In contrast, for a Deposit-Limited Spread Account the limit is similar to a customary coverage limit. The total amount of spread deposits made into the account is limited to a maximum amount specified in the Contract.
- b. In the Stress Test, the Available Contract Balance of a Spread Account is adjusted prior to the calculation of the DCC Available Balance as reported in the RBC Report. For each Spread Account contract, the Enterprises report the Remaining Limit Amount, which represents the maximum dollar amount of additional spread deposits that could be required under the Contract. For Deposit-Limited Spread Accounts, this amount is the maximum remaining dollar amount of spread deposits required under the Contract. For Balance-Limited Spread Accounts, this amount is defined as one-twelfth of the annualized spread rate times the UPB of the covered loans at the start of the Stress Test times the weighted average Remaining term to Maturity of those loans. However, the maximum amount of spread deposits that could be received will generally be higher than the amount reasonably expected to be received during the Stress Test, because the UPB of the covered loans, which is the basis for determining the amounts of future spread deposits, declines over the term of the Contract due to Amortization, Defaults, and Prepayments. Therefore, the Enterprises report an adjusted Available Contract Balance for both types of Spread Accounts before reporting the DCC Available Balance by adding the lesser of the Remaining Limit Amount or one-twelfth of the spread rate times the UPB of the covered loans at the start of the stress test times 60 months.
- c. Modified Pool Insurance, Limited Recourse, Limited Indemnification and FHA risk-sharing contracts may have

both loan-level and aggregate-level coverage limits. To account for this aspect of these types of Aggregate Limit CE, the Enterprises report a DCC Loan Level Coverage Limit Amount, which represents the share of each loss after deductibles (such as MI or First Priority Contract payments) covered by a given MPI Contract. (The Loan Level Coverage Limit Amount takes the value of one if the Contract is not of this type, representing that 100 percent of losses are covered by other types of Contracts).

- d. In practice, Unlimited Recourse Contracts have neither loan-level nor aggregate-level coverage limits. However, the Enterprises report the Available Aggregate CE Balance of Unlimited Recourse Contracts as the summation of the Original UPB of all covered loans.
- e. The Available Aggregate CE Balances of Collateral Account Contracts funded with anything other than Cash or Cash-equivalents are discounted by thirty percent to account for market risk in securities that are not cash equivalents.
- f. Enterprise Loss Positions are treated as Aggregate Limit CE in terms of reducing remaining losses eligible to be covered by a next-priority Contract. However, since Enterprise Loss Positions are typically a deductible for other forms of supplementary coverage, payments from such accounts do not reduce loss severity.

[F] *Multiple Layers of Credit Enhancement.* For loans with more than one type of Credit Enhancement, MI or Loss Sharing is applied first, and then other types of CE (if available) are applied in priority order to the remaining losses. MI and Loss Sharing claims are payable regardless of whether (and to what extent) a loan is also covered by other forms of CE. MI is unique in that the MI payment is based on a percentage of a Claim Amount equal to the entire Defaulted UPB plus expenses, not the actual loss incurred upon liquidation. Therefore, an Enterprise can receive MI payments on a defaulted loan in excess of the actual realized loss on that loan. However, it is frequently the case that MI payments are insufficient to cover the entire loss amount. In such cases, one or more types of Aggregate Limit CE may be available to make up the deficiency. Unlike MI claims, however, the Claim Amounts for Loss Sharing and for all Aggregate Limit CE types do depend on the actual losses incurred; and unlike Loss Sharing and MI, Claim Amounts payable under other forms of CE are net of payments received on account of other forms of CE. When a single loan is covered by multiple forms of CE, the order in which they are to be applied (First Priority, Second Priority, etc.) must be specified. To avoid double-counting, a higher-numbered

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priority CE only covers losses that were not covered by a lower-numbered priority CE.

3.6.3.6.4.2 Mortgage Credit Enhancement Inputs

[a] For each Loan Group, the inputs in Table 3-46 are required:

TABLE 3-46—CE INPUTS FOR EACH LOAN GROUP

Variable	Description	Source
UPB_{ORIG}^{LG}	Origination UPB	RBC Report
UPB_0^{LG} and UPB_m^{LG}	Initial UPB and UPB in month $m = 0, 1, \dots, 120$	section 3.6.3.3.4, Mortgage Amortization Schedule Outputs
LTV_{ORIG}^{LG}	Original LTV	RBC Report
DEF_m^{LG} and $PERF_m^{LG}$	Defaulting and Performing Fractions of Initial Loan Group UPB in month $m = 1, \dots, 120$	section 3.6.3.4.4, Single Family Default and Prepayment Outputs and section 3.6.3.5.4, Multifamily Default and Prepayment Outputs
$CLM_m^{ML, LG}$ $CLM_m^{LSA, LG}$	MI Claim Amount and LSA Claim Amount	section 3.6.3.6.2, Single Family Gross Loss Severity and section 3.6.3.6.3, Multifamily Gross Loss Severity
GLS_m^{LG}	Gross Loss Severity	section 3.6.3.6.2, Single Family Gross Loss Severity and section 3.6.3.6.3, Multifamily Gross Loss Severity

[b] For each DCC covering loans in the Loan Group, the inputs in Table 3-47 are required:

TABLE 3-47—INPUTS FOR EACH DISTINCT CE COMBINATION (DCC)

Variable	Description	Source
P^{DCC}	Percent of Initial Loan Group UPB represented by individual loan(s) in a DCC	RBC Report
$R^{ML, DCC}$ or $R^{LSA, DCC}$	Credit rating of Loan Limit CE (MI or LSA) Counterparty	RBC Report
$C^{ML, DCC}$ or $C^{LSA, DCC}$	Weighted Average Coverage Percentage for MI or LSA Coverage (weighted by Initial UPB)	RBC Report
$AB_0^{DCC, C1}$	DCC Available First Priority CE Balance immediately prior to start of the Stress Test	RBC Report
$AB_0^{DCC, C2}$	DCC Available Second Priority CE Balance immediately prior to start of the Stress Test	RBC Report
$R^{DCC, C1}$	DCC Credit Rating of First Priority CE Provider or Counterparty; or Cash/Cash Equivalent (which is not Haircutted)	RBC Report
$R^{DCC, C2}$	DCC Credit Rating of Second Priority CE Provider or Counterparty; or Cash/Cash Equivalent (which is not Haircutted)	RBC Report
$C^{DCC, C1}$	DCC Loan-Level Coverage Limit of First Priority Contract (if Subtype is MPI; otherwise = 1)	RBC Report
$C^{DCC, C2}$	DCC Loan-Limit Coverage Limit of Second Priority Contract (if Subtype is MPI; otherwise = 1)	RBC Report

TABLE 3–47—INPUTS FOR EACH DISTINCT CE COMBINATION (DCC)—Continued

Variable	Description	Source
ExpMo ^{DCC,C1}	Month in the Stress Test (1...120 or after) in which the DCC First Priority Contract expires	RBC Report
ExpMo ^{DCC,C2}	Month in the Stress Test (1...120 or after) in which the DCC Second Priority Contract expires	RBC Report
ELPF ^{DCC,C1}	DCC Enterprise Loss Position Flag for First Priority Contract (Y or N)	RBC Report
ELPF ^{DCC,C2}	DCC Enterprise Loss Position Flag for Second Priority Contract (Y or N)	RBC Report

[c] In the RBC Report, Aggregate Limit CE Subtypes are grouped as illustrated in Table 3–48.

TABLE 3–48—AGGREGATE LIMIT CE SUBTYPE GROUPING

Symbol	Subtype	Also Includes
REC	Unlimited Recourse	Unlimited Indemnification
PI	Pool Insurance	Pool Insurance
		Letter of Credit
		Subordination Arrangements
MPI	Modified Pool Insurance	Modified Pool Insurance
		Limited Recourse
		Limited Indemnification
		FHA Risk-sharing Agreements
CASH	Cash Account	Cash Account
COLL	Collateral Account	Collateral
ELP	Enterprise Loss Position	GSE Loss Position (ledger item)
SA	Spread Account	Spread Account

3.6.3.6.4.3 Mortgage Credit Enhancement Procedures

[a] For each month m of the Stress Test, for each Loan Group (LG), carry out the following six steps [a] 1–6 for each DCC.

NOTE: Process the Loan Groups and DCCs using the numerical order assigned to them in the RBC Report.

1. Determine Mortgage Insurance Payment (MI_m) for single family loans in the DCC, or Loss Sharing Payment (LSA_m) for multifamily loans in the DCC, as a percentage of Defaulted UPB, applying appropriate counterparty Haircuts from section 3.5., of this Appendix:

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$$MI_m^{DCC} = \left(1 - MIExp_m^{LG}\right) \times C^{MI,DCC} \times CLM_m^{MI, LG} \times \left[1 - \frac{m'}{120} \times \text{MaxHct} \left(R^{MI,DCC}\right)\right]$$

$$LSA_m^{DCC} = C^{LSA,DCC} \times CLM_m^{LSA, LG} \times \left[1 - \frac{m'}{120} \times \text{MaxHct} \left(R^{LSA,DCC}\right)\right]$$

Where:

$m' = m$, except for counterparties rated below BBB, where $m' = 120$

$$MIExp_m^{LG} = 1 \text{ if } \left(LTV_{\text{ORIG}} \times \frac{UPB_m^{LG}}{UPB_{\text{ORIG}}^{LG}}\right) < 0.78$$

$$MIExp_m^{LG} = 0 \text{ otherwise}$$

0.78 (78%) = the LTV at which MI is cancelled if payments are current

2. Determine Remaining Loss in Dollars (RLD) after application of MI or LSA and prior to application of other Aggregate Limit CE:

$$RLD_m^{DCC, (MI-LSA)} = \max\left[\left(GLS_m^{LG} - MI_m^{DCC}\right), 0\right] \times P^{DCC} \times UPB_{m-1}^{LG} \times DEF_m^{LG}$$

3. Determine the contractual CE Payment in Dollars under the First Priority Contract C1. Determine Payment after Haircut. Update Remaining Loss Dollars and DCC Available Balance.

- a. Determine CE Payment as the minimum of the Remaining Loss Dollars after MI or LSA (if applicable) times the DCC Loan-Level Coverage Limit (=1 if not MPI Contract) or the previous month's ending DCC Available Balance:

$$PD_m^{DCC, C1} = \min\left(RLD_m^{DCC, (MI-LSA)} \times C^{DCC, C1}, AB_{m-1}^{DCC, C1}\right)$$

- b. Determine CE Payment in Dollars after application of Haircuts:

$$PD_m^{DCC, C1, H} = PD_m^{DCC, C1} \times \left[1 - \frac{m'}{120} \times \text{MaxHct} \left(R^{DCC, C1}\right)\right]$$

Where:

$m' = m$, except for counterparties rated below BBB, where $m' = 120$

- c. Update DCC Remaining Loss Dollars and DCC Available Balance under the First Priority Contract C1:

$$RLD_m^{DCC,C1} = \max\left(RLD_m^{DCC,(MI-LSA)} - PD_m^{DCC,C1,H}, 0\right)$$

$$AB_m^{DCC,C1} = \max\left(\left[AB_{m-1}^{DCC,C1} - PD_m^{DCC,C1}\right] \times \left(1 - Exp_m^{DCC,C1}\right), 0\right)$$

Where:

$Exp_m^c = 1$ if the Contract has expired, i.e. if the calendar month corresponding to the m^{th} month of the Stress Test is on or after the expiration month ($ExpMo^c$)

$Exp_m^c = 0$ otherwise

4. Determine the contractual CE Payment in Dollars under the Second Priority Con-

tract C2. Determine Payment after Haircut. Update Remaining Loss Dollars and DCC Available Balance.

a. Determine CE Payment as the minimum of the Remaining Loss Dollars after C1 Payment (if applicable) times a DCC Loan-Level Coverage Limit (=1 if not MPI Contract) or the previous month's ending DCC Available Balance:

$$PD_m^{DCC,C2} = \min\left(RLD_m^{DCC,C1} \times C^{DCC,C2}, AB_{m-1}^{DCC,C2}\right)$$

b. Determine CE Payment in Dollars after application of Haircuts:

$$PD_m^{DCC,C2,H} = PD_m^{DCC,C2} \times \left[1 - \frac{m'}{120} \times \text{MaxHct}\left(R^{DCC,C2}\right)\right]$$

Where:

$m' = m$, except for counterparties rated below BBB, where $m' = 120$

c. Update DCC Remaining Loss Dollars and DCC Available Balance under the Second Priority Contract C2:

$$RLD_m^{DCC,C2} = \max\left(RLD_m^{DCC,C1} - PD_m^{DCC,C2,H}, 0\right)$$

$$AB_m^{DCC,C2} = \max\left(\left[AB_{m-1}^{DCC,C2} - PD_m^{DCC,C2}\right] \times \left(1 - Exp_m^{DCC,C2}\right), 0\right)$$

Where:

$Exp_m^c = 1$ if the Contract has expired, i.e. if the calendar month corresponding to the m^{th} month of the Stress Test is on or after the expiration month ($ExpMo^c$)

$Exp_m^c = 0$ otherwise

5. Convert Aggregate Limit First and Second Priority Contract receipts in Dollars for each DCC in month m to a percentage of DCC Defaulted UPB:

If $DEF_m = 0$, then $ALPD_m^{DCC} = 0$

$$ALPD_m^{DCC} = \frac{\left(PD_m^{DCC,C1,H} \times ELPI^{DCC,C1} \right) + \left(PD_m^{DCC,C2,H} \times ELPI^{DCC,C2} \right)}{DEF_m \times UPB_{m-1}^{LG} \times P^{DCC}}$$

Where:

ELPI^{DCC,C} = 0 if ELPP^{DCC,C} = Y (Yes, indicating that Contract C is an Enterprise Loss Position)
 ELPI^{DCC,C} = 1 otherwise

6. Add the Loan Limit CE (MI and LSA) and Aggregate Limit CE (ALPD), each expressed as a share of DCC Defaulted UPB, separately for each DCC to increment the respective Loan Group totals:

$$MI_m^{LG} = MI_m^{LG} + \left(P^{DCC} \times MI_m^{DCC} \right) \text{ for single family Loans; or}$$

$$LSA_m^{LG} = LSA_m^{LG} + \left(P^{DCC} \times LSA_m^{DCC} \right) \text{ for multifamily Loans; and}$$

$$ALCE_m^{LG} = ALCE_m^{LG} + \left(P^{DCC} \times ALPD_m^{DCC} \right) \text{ for both single family and multifamily Loans}$$

3.6.3.6.4.4 Mortgage Credit Enhancement Outputs [a] Mortgage Credit Enhancement Outputs are set forth in Table 3-49.

TABLE 3-49—SINGLE FAMILY AND MULTIFAMILY CREDIT ENHANCEMENT OUTPUTS

Variable	Description
MI _m	MI payments applied to reduce single family Gross Loss Severity in month m of the Stress Test (as a fraction of Defaulted UPB in month m)
LSA _m	LSA payments applied to reduce multifamily Gross Loss Severity in month m of the Street Test (as a fraction of Defaulted UPB in month m)
ALCE _m	Aggregate receipts from all forms of Aggregate Limit Credit Enhancement applied to reduce single- and multifamily Gross Loss Severity in month m of the Stress Test (as a fraction of Defaulted UPB in month m)

[b] MI_m^{LG} or LSA_m^{LG} and ALCE_m^{LG} for months m = 1...120 of the Stress Test are used in section 3.6.3.6.5, Single Family and Multifamily Net Loss Severity, of this Appendix.

Combine inputs and outputs from Gross Loss Severity and Credit Enhancements (Table 3-42 through Table 3-49) in the following formulas for each Loan Group in month m:

3.6.3.6.5 Single Family and Multifamily Net Loss Severity

[a] For Conventional single family Loan Groups:

3.6.3.6.5.1 Single Family and Multifamily Net Loss Severity Procedures

$$LS_m^{SF} = \frac{1}{\left(1 + \frac{DR_m}{2} \right)^{\frac{MQ}{6}}} + \frac{\left(\frac{MQ}{12} \times PTR_m \right) + F - MI_m}{\left(1 + \frac{DR_m}{2} \right)^{\frac{MF}{6}}} + \frac{R - RP_m - ALCE_m}{\left(1 + \frac{DR_m}{2} \right)^{\frac{MF+MR}{6}}}$$

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[b] For Government single family Loan Groups, complete the following three steps:

1. Compute a Loss Severity value for FHA-insured loans using the Conventional formula for all government loans. FHA reimbursement rates will be reflected in

the value of MI_m , as computed in section 3.6.3.6.4.3, Mortgage Credit Enhancement Procedures, of this Appendix.

2. Compute a Loss Severity value for VA-insured loans as follows for all government loans:

$$LS_m^{VA} = \frac{1 + F + \left(\frac{MQ}{12} \times PTR_m\right) + (R - RP_m) - 0.30}{\left(1 + \frac{DR_m}{2}\right)^{\frac{MF}{6}}}$$

Where:

0.30 is a fixed percentage representing the VA guarantee coverage percentage. (The VA coverage rate is a function of the initial loan size.)

3. Compute Net Loss Severity by combining FHA-insured and VA-insured Loss Severity values as follows:

$$LS_m^{SF,GVT} = \left(\frac{2}{3} \times LS_m^{SF}\right) + \left(\frac{1}{3} \times LS_m^{VA}\right)$$

[c] For multifamily Loan Groups other than FHA-Insured:

$$LS_m^{MF} = \frac{1 + \left(\frac{MQ}{12} \times PTR_m\right)}{\left(1 + \frac{DR_m}{2}\right)^{\frac{MQ}{6}}} + \frac{\frac{RHC}{2} - LSA_m}{\left(1 + \frac{DR_m}{2}\right)^{\frac{MF}{6}}} + \frac{\frac{RHC}{2} - RP - ALCE_m}{\left(1 + \frac{DR_m}{2}\right)^{\frac{MF+MR}{6}}}$$

[d] For FHA-Insured multifamily Loan Groups:

$$LS_m^{MF} = 0.03 \text{ (3 percent) for all months}$$

3.6.3.6.5.2 Single Family and Multifamily Net Loss Severity Outputs Net Loss Severity outputs are set forth in Table 3-50:

TABLE 3-50—SINGLE FAMILY AND MULTIFAMILY LOSS SEVERITY OUTPUTS

Variable	Description
LS_m^{SF}	Loss Severity (as a fraction of Defaulted UPB) for single family loans in month m
LS_m^{MF}	Loss Severity (as a fraction of Defaulted UPB) for multifamily loans in month m

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Single family and multifamily Loss Severities for months 1...120 of the Stress Test are used in section 3.6.3.7, Stress Test Whole Loan Cash Flows, of this Appendix.

and Net Loss Severity Rates to produce performance-adjusted cash flows for Enterprise Whole Loans in the Stress Test.

3.6.3.7 Stress Test Whole Loan Cash Flows

3.6.3.7.2 Stress Test Whole Loan Cash Flow Inputs

3.6.3.7.1 Stress Test Whole Loan Cash Flow Overview

The inputs required to compute Stress Test Whole Loan Cash Flows for each Loan Group are listed in Table 3-51.

This section combines the mortgage Amortization Schedules with Default, Prepayment

TABLE 3-51—INPUTS FOR FINAL CALCULATION OF STRESS TEST WHOLE LOAN CASH FLOWS

Variable	Description	Source
UPB _m	Aggregate Unpaid Principal Balance in month m = 0 ... RM	section 3.6.3.3.4, Mortgage Amortization Schedule Outputs
NYR _m	Net Yield Rate in month m = 1 ... RM	section 3.6.3.3.4, Mortgage Amortization Schedule Outputs
GF	Guarantee Fee rate (weighted average for Loan Group) (decimal per annum)	RBC Report
PTR _m	Pass-Through Rate in month m = 1 ... RM	section 3.6.3.3.4, Mortgage Amortization Schedule Outputs
SP _m	Aggregate Scheduled Principal (Amortization) in month m = 1 ... RM	section 3.6.3.3.4, Mortgage Amortization Schedule Outputs
PRE _m ^{SF} PRE _m ^{MF}	Prepaying Fraction of original Loan Group in month m = 1 ... RM	section 3.6.3.4.4, Single Family Default and Prepayment Outputs and, section 3.6.3.5.4, Multifamily Default and Prepayment Outputs
DEF _m ^{SF} DEF _m ^{MF}	Defaulting Fraction of original Loan Group in month m = 1 ... RM	section 3.6.3.4.4, Single Family Default and Prepayment Outputs and, section 3.6.3.5.4, Multifamily Default and Prepayment Outputs
PERF _m ^{SF} PERF _m ^{MF}	Performing Fraction of original Loan Group in month m = 1 ... RM	section 3.6.3.4.4, Single Family Default and Prepayment Outputs and, section 3.6.3.5.4, Multifamily Default and Prepayment Outputs
FDS	Float Days for Scheduled Principal and Interest (weighted average for Loan Group)	RBC Report
FDP	Float Days for Prepaid Principal (weighted average for Loan Group)	RBC Report
FER _m	Float Earnings Rate in month m = 1 ... RM	1 week Fed Funds Rate; section 3.3, Interest Rates

TABLE 3–51—INPUTS FOR FINAL CALCULATION OF STRESS TEST WHOLE LOAN CASH FLOWS—
Continued

Variable	Description	Source
LS _m ^{SF}	Loss Severity Rate in month m = 1 ... RM	section 3.6.3.6.5.2, Single Family and Multifamily Net Loss Severity Outputs
FREP	Fraction Repurchased (weighted average for Loan Group) (decimal)	RBC Report

3.6.3.7.3 Stress Test Whole Loan Cash Flow Procedures

[a] Calculate Stress Test whole loan cash flows using the following nine steps:

1. Calculate Scheduled Principal Received (SPR) in month m:

$$SPR_m = \max(SP_m, 0) \times (PERF_m + PRE_m)$$

NOTE: Scheduled Principal Received is zero, not negative, when amortization is negative.

2. Calculate Net Interest Received (NIR) in month m. Any interest shortfall due to Negative Amortization reduces Net Yield directly. Note: NIR includes loans that default in month m, because lost interest is included in Credit Losses in step 6) of this section. (See section 3.6.3.6, Calculation of Single Family and Multifamily Mortgage Losses, of this Appendix.)

$$NIR_m = \left[\left(UPB_{m-1} \times \frac{NYR_m}{12} \right) + \min(SP_m, 0) \right] \times PERF_{m-1}$$

3. Calculate Prepaid Principal Received (PPR) in month m:

$$PPR_m = UPB_m \times PRE_m$$

4. Calculate newly Defaulted Principal (DP) in month m:

$$DP_m = UPB_{m-1} \times DEF_m$$

5. Calculate Recovery Principal Received (RPR) on account of loans that Defaulted in month m:

$$RPR_m = UPB_{m-1} \times DEF_m \times (1 - LS_m)$$

6. Calculate Credit Losses (CL) on account of loans that Defaulted in month m:

$$CL_m = UPB_{m-1} \times DEF_m \times LS_m$$

In addition, if m = RM and UPB_{RM} > 0 then,

$$CL_{RM} = (UPB_{RM} \times PERF_{RM}) + (UPB_{RM-1} \times DEF_{RM} \times LS_{RM}),$$

and

$$PUPB_{RM} = 0$$

7. Calculate Performing Loan Group UPB in month m (PUPB_m), including PUPB₀.

NOTE: All loans are assumed to be performing in month 0; therefore PUPB₀ = UPB₀.

$$PUPB_m = UPB_m \times PERF_m$$

8. Calculate Total Principal Received (TPR) and Total Interest Received (TIR) in month m:

$$TPR_m = SPR_m + PPR_m + RPR_m$$

$$TIR_m = NIR_m$$

9. For Sold Loans, calculate the following cash flow components:

- a. Guarantee Fee (GF) received in month m:

$$GF_m = UPB_{m-1} \times \frac{GFR}{12} \times (PERF_m + PRE_m)$$

- b. Float Income (FI) received in month m

$$FI_m = \left(\left((SPR_m + NIR_m - GF_m) \times \frac{FDS}{365} \right) + \left[PPR_m \times \frac{FDP}{365} \right] \times FER_m \right) - PIS_m \times (1 - FREP)$$

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where: Prepayment Interest Shortfall (PIS) in month m is:

$$PIS_m = UPB_{m-1} \times PRE_m \times \frac{PTR_m}{12}$$

if FDP ≥ 30

$$PIS_m = UPB_{m-1} \times PRE_m \times \frac{PTR_m}{24}$$

if 15 ≤ FDP < 30

3.6.3.7.4 Stress Test Whole Loan Cash Flow Outputs

The Whole Loan Cash Flows in Table 3-52 are used to prepare pro forma balance sheets and income statements for each month of the Stress Period (see section 3.10 Operations, Taxes and Accounting, of this Appendix). For Retained Loan groups, cash flows consist of Scheduled Principal, Prepaid Principal, Defaulted Principal, Credit Losses, and Interest. For Sold Loan groups, cash flow consists of Credit Losses, Guarantee Fees and Float Income. For Repurchased MBSS, cash flows are allocated according to the Fraction Repurchased. Table 3-52 covers all cases; for Retained Loans FREP = 1.0.

TABLE 3-52—OUTPUTS FOR WHOLE LOAN CASH FLOWS

Variable	Description
SPR _m	Scheduled Principal Received in month m = 1...RM
PPR _m	Prepaid Principal Received in month m = 1...RM
DP _m	Defaulted Principal in month m = 1...RM
CL _m	Credit Losses in month m = 1...RM
PUPB _m	Performing Loan Group UPB in month m = 0...RM
TPR _m	Total Principal Received in month m = 1...RM
TIR _m	Total Interest Received in month m = 1...RM
GF _m	Guarantee Fees received in month m = 1...RM
FI _m	Float Income received in month m = 1...RM

TABLE 3-53—ADDITIONAL OUTPUTS FOR REPURCHASED MBSS

Variable	Quantity	Description
STPR _m	FREP × (SPR _m + PPR _m + DP _m)	Enterprise's portion of Total Principal Received in months m = 1...RM, reflecting its fractional ownership of the MBS
STIR _m	FREP × (TIR _m - GF _m)	Enterprise's portion of Total Interest Received (at the Pass-Through Rate) in months m = 1...RM, reflecting its fractional ownership of the MBS
SPUPB _m	FREP × PUPB _m	Enterprise's portion of the Performing UPB of the repurchased MBS in months m = 0...RM, reflecting its fractional ownership of the MBS

3.6.3.8 Whole Loan Accounting Flows

3.6.3.8.1 Whole Loan Accounting Flows Overview

[a] For accounting purposes, cash flows are adjusted to reflect (1) the value over time of discounts, premiums and fees paid or received (Deferred Balances) when an asset was acquired; and (2) the fact that mortgage in-

terest is paid in arrears, i.e. it is received in the month after it is earned. In the Stress Test calculations, payments are indexed by the month in which they are received. Therefore, interest received in month m was earned in month m-1. However, principal is accounted for in the month received.

[b] Deferred Balances are amortized over the remaining life of the asset. Therefore,

these calculations go beyond the end of the Stress Test if the Remaining Maturity (RM) is greater than the 120 months of the Stress Test. The projection of cash flows beyond the end of the Stress Test is discussed in the individual sections where the cash flows are first calculated. In general, for interest rate indexes, monthly Prepayment rates and

monthly Default rates, the value for $m = 120$ is used for all months $120 < m \leq RM$, but $LS = 0$ for $m > 120$.

3.6.3.8.2 Whole Loan Accounting Flows Inputs

The inputs in Table 3-54 are required to compute Accounting Flows:

TABLE 3-54—INPUTS FOR WHOLE LOAN ACCOUNTING FLOWS

Variable	Description	Source
RM	Remaining Term to Maturity in months	RBC Report
UPD ₀	Sum of all unamortized discounts, premiums, fees, commissions, etc. for the loan group, such that the unamortized balance equals the book value minus the face value for the loan group at the start of the Stress Test, adjusted by the Unamortized Balance Scale Factor	RBC Report
NYR ₀	Net Yield Rate at time zero	section 3.6.3.3.4, Mortgage Amortization Schedule Outputs
PUPB _m	Performing Loan Group UPB in months $m = 0 \dots RM$	section 3.6.3.7.4, Stress Test Whole Loan Cash Flow Outputs
PTR ₀	Pass-Through Rate at time zero	section 3.6.3.3.4, Mortgage Amortization Schedule Outputs
SPUPB _m	Security Performing UPB in months $m = 0 \dots RM$	section 3.6.3.7.4, Stress Test Whole Loan Cash Flow Outputs
SUPD ₀	The sum of all unamortized discounts, premiums, fees, commissions, etc. associated with the securities modeled using the Wtd Ave Percent Repurchased, such that the unamortized balance equals the book value minus the face value for the relevant securities at the start of the Stress Test, adjusted by the percent repurchased and the Security Unamortized Balance Scale Factor	RBC Report

3.6.3.8.3 Whole Loan Accounting Flows Procedures

3.6.3.8.3.1 Accounting for Retained and Sold Whole Loans

[a] Complete the following three steps to account for Retained and Sold loans:

1. Compute Allocated Interest in month m (AI^m) as follows:

$$AI_m = PUPB_{m-1} \times \frac{NYR_0}{12}$$

NOTE: Allocated Interest is used only to determine the allocation of Amortization Expense over time, not to generate actual cash flows)

2. Calculate the monthly Internal Rate of Return (IRR) that equates the adjusted cash flows (actual principal plus Allocated Interest) to the Initial Book Value (BV_0) of the Loan Group. A single IRR is used for all months m . Solve for IRR such that:

$$BV_0 = \sum_{m=1}^{RM} \frac{ACF_m}{(1 + IRR)^m}$$

Where:

$$BV_0 = PUPB_0 + UPD_0$$

$$ACF_m = AI_m - PUPB_m + PUPB_{m-1}$$

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3. Calculate the monthly Amortization Expense for each month m:

- a. If $BV_0 < 0$, or if $12 \times IRR > 1.0$ (100%), or if

$$BV_0 > \sum_{m=1}^{RM} ACF_m$$

then the full amount of UPD_0 is realized in the first month ($AE_1 = -UPD_0$)

- b. Otherwise:

$$AE_m = (BV_{m-1} \times IRR) - AI_m$$

if $PUPB_m > 0$

$$AE_m = -UPD_{m-1} \text{ if } PUPB_m = 0$$

$$UPD_m = UPD_{m-1} + AE_m$$

$$BV_m = PUPB_m + UPD_m$$

3.6.3.8.3.2 Additional Accounting for Repurchased MBSs

[a] Complete the following three steps to account for Repurchased MBSs:

1. Compute Security Allocated Interest in month m (SAI_m) as follows:

$$SAI_m = SPUPB_{m-1} \times \frac{PTR_0}{12}$$

Note: Security Allocated Interest is used only to determine the allocation of Security Amortization Expense over time, not to generate actual cash flows.

2. Calculate the monthly Internal Rate of Return (IRR) that equates the adjusted cash flows (actual principal plus Allocated Interest) to the Initial Book Value (SBV_0) of the Loan Group. A single IRR is used for all months m. Solve for IRR such that:

$$SBV_0 = \sum_{m=1}^{RM} \frac{SACF_m}{(1 + IRR)^m}$$

Where:

$$SBV_0 = SPUPB_0 + SUPD_0$$

$$SACF_m = SAI_m - SPUPB_m + SPUPB_{m-1}$$

3. Calculate the monthly Security Amortization Expense for each month m:

- a. If $SBV_0 < 0$, or if $12 \times IRR > 1.0$ (100%), or if

$$SBV_0 > \sum_{m=1}^{RM} SACF_m$$

then the full amount of $SUPD_0$ is realized in the first month ($SAE_1 = -SUPD_0$).

- b. Otherwise:

$$SAE_m = (SBV_{m-1} \times IRR) - SAI_m$$

if $SPUPB_m > 0$

$$SAE_m = -SUPD_{m-1} \text{ if } SPUPB_m = 0$$

$$SUPD_m = SUPD_{m-1} + SAE_m$$

$$SBV_m = SPUPB_m + SUPD_m$$

3.6.3.8.4 Whole Loan Accounting Flows Outputs

Whole loan accounting flows outputs are set forth in Table 3-55. Amortization Expense for months $m = 1 \dots RM$ are used in section 3.10, Operations, Taxes, and Accounting, of this Appendix.

TABLE 3-55—OUTPUTS FOR WHOLE LOAN ACCOUNTING FLOWS

Variable	Description
AE_m	Amortization Expense for months $m = 1 \dots RM$
SAE_m	Security Amortization Expense for months $m = 1 \dots RM$

3.6.4 Final Whole Loan Cash Flow Outputs

The final outputs for section 3.6, Whole Loan Cash Flows, of this Appendix are as specified in Table 3-52, and Table 3-55.

3.7 Mortgage-Related Securities Cash Flows

3.7.1 Mortgage-Related Securities Overview

[a] Mortgage-Related Securities (MRSs) include Single Class MBSs, Multi-class MBSs (REMICs or Collateralized Mortgage Obligations (CMOs)), Mortgage Revenue Bonds (MRBs), and Derivative Mortgage Securities such as Interest-Only and Principal-Only Stripped MBSs. MBSs and Derivative Mortgage Securities are issued by the Enterprises, Ginnie Mae and private issuers. MRBs are issued by State and local governments or their instrumentalities. For computational purposes, certain Asset-Backed Securities (ABS) backed by mortgages (Mortgage ABSs backed by manufactured housing loans, second mortgages or home equity loans) are treated as REMICs in the Stress Test.

[b] Cash flows from Single Class MBSs represent the pass-through of all principal and interest payments, net of servicing and guarantee fees, on the underlying pools of mortgages. Cash flows from Multi-Class MBSs and Derivative Mortgage Securities represent a specified portion of the cash flows produced by an underlying pool of mortgages and/or

Mortgage-Related Securities, determined according to rules set forth in offering documents for the securities. MRBs may have specific maturity schedules and call provisions, whereas MBSs have only expected maturities and, in most cases, no issuer call provision (other than “cleanup calls” if the pool balance becomes quite small). However, the timing of principal payments for MRBs is still closely related to that of their underlying mortgage collateral. The Stress Test treats most MRBs in a manner similar to single class MBSs. Finally, a small number of Enterprise and private label REMIC securities for which modeling information is not readily available and which are not modeled by a commercial information service (referred to as “miscellaneous MRS”) are treated separately.

[c] In addition to reflecting the defaults of mortgage borrowers during the Stress Period, the Stress Test considers the possibility of issuer Default on Mortgage-Related Securities. Credit impairments throughout the Stress Period are based on the rating of these securities, and are modeled by reducing contractual interest payments and “writing down” principal. No Credit Losses are assumed for the Enterprise’s own securities and Ginnie Mae securities (see section

3.5.3, Counterparty Defaults Procedures, of this Appendix).

[d] The calculation of cash flows for Mortgage-Related Securities requires information from the Enterprises identifying their holdings, publicly available information characterizing the securities, and information on the interest rate, mortgage performance and credit rating (for rated securities).

[e] Cash and accounting flows—monthly principal and interest payments and amortization expense—are produced for each month of the Stress Period for each security. (Principal- and interest-only securities pay principal or interest respectively.) These cash flows are input to the Operations, Taxes, and Accounting component of the Stress Test.

3.7.2 Mortgage-Related Securities Inputs

3.7.2.1 Inputs Specifying Individual Securities

3.7.2.1.1 Single Class MBSs

The information in Table 3–56 is required for single class MBSs held by an Enterprise at the start of the Stress Test. This information identifies the Enterprise’s holdings and describes the MBS and the underlying mortgage loans.

TABLE 3–56—RBC REPORT INPUTS FOR SINGLE CLASS MBS CASH FLOWS

Variable	Description
Pool Number	A unique number identifying each mortgage pool
CUSIP Number	A unique number assigned to publicly traded securities by the Committee on Uniform Securities Identification Procedures
Issuer	Issuer of the mortgage pool
Original UPB Amount	Original pool balance multiplied by the Enterprise’s percentage ownership
Current UPB Amount	Initial Pool balance (at the start of the Stress Test), multiplied by the Enterprise’s percentage ownership
Product Code	Mortgage product type for the pool
Security Rate Index	If the rate on the security adjusts over time, the index that the adjustment is based on
Unamortized Balance	The sum of all unamortized discounts, premiums, fees, commissions, etc., such that the unamortized balance equals book value minus face value, adjusted by the Unamortized Balance Scale Factor
Wt Avg Original Amortization Term	Original amortization term of the underlying loans, in months (weighted average for underlying loans)
Wt Avg Remaining Term of Maturity	Remaining Maturity of the underlying loans at the start of the Stress Test (weighted average for underlying loans)
Wt Avg Age	Age of the underlying loans at the start of the Stress Test (weighted average for underlying loans)

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TABLE 3--56--RBC REPORT INPUTS FOR SINGLE CLASS MBS CASH FLOWS--Continued

Variable	Description
Wt Avg Current Mortgage Interest rate	Mortgage Interest Rate of the underlying loans at the start of the Stress Test (weighted average for underlying loans)
Wt Avg Pass-Through Rate	Pass-Through Rate of the underlying loans at the start of the Stress Test (weighted average for underlying loans)
Wtg Avg Original Mortgage Interest Rate	The current UPB weighted average Mortgage Interest Rate in effect at Origination for the loans in the pool
Security Rating	The most current rating issued by any Nationally Recognized Statistical Rating Organization (NRSRO) for this security, as of the reporting date. In the case of a "split" rating, the lowest rating should be given
Wt Avg Gross Margin	Gross margin for the underlying loans (ARM MBS only) (weighted average for underlying loans)
Wt Avg Net Margin	Net margin (used to determine the security rate for ARM MBS) (weighted average for underlying loans)
Wt Avg Rate Reset Period	Rate reset period in months (ARM MBS only) (weighted average for underlying loans)
Wt Avg Rate Reset Limit	Rate reset limit up/down (ARM MBS only) (weighted average for underlying loans)
Wt Avg Life Interest Rate Ceiling	Maximum rate (lifetime cap) (ARM MBS only) (weighted average for underlying loans)
Wt Avg Life Interest Rate Floor	Minimum rate (lifetime floor) (ARM MBS only) (weighted average for underlying loans)
Wt Avg Payment Reset Period	Payment reset period in months (ARM MBS only) (weighted average for underlying loans)
Wt Avg Payment Reset Limit	Payment reset limit up/down (ARM MBS only) (weighted average for underlying loans)
Wt Avg Lookback Period	The number of months to look back from the interest rate change date to find the index value that will be used to determine the next interest rate (ARM MBS only) (weighted average for underlying loans)
Wt Avg Negative Amortization Cap	The maximum amount to which the balance can increase before the payment is recast to a fully amortizing amount. It is expressed as a fraction of the original UPB. (ARM MBS only) (weighted average for underlying loans)
Wt Avg Initial Interest Rate Period	Number of months between the loan origination date and the first rate adjustment date (ARM MBS only) (weighted average for underlying loans)
Wt Avg Unlimited Payment Reset Period	Number of months between unlimited payment resets, <i>i.e.</i> , not limited by payment caps, starting with Origination date (ARM MBS only) (weighted average for underlying loans)
Notional Flag	Indicates that amounts reported in Original UPB Amount and Current UPB Amount are notional
UPB Scale Factor	Factor applied to the current UPB that offsets any timing adjustments between the security level data and the Enterprise's published financials

TABLE 3–56—RBC REPORT INPUTS FOR SINGLE CLASS MBS CASH FLOWS—Continued

Variable	Description
Whole Loan Modeling Flag	Indicates that the Current UPB Amount and Unamortized Balance associated with this Repurchased MBS are included in the Wtg Avg Percent Repurchased and Security Unamortized Balance fields
FAS 115 Classification	The financial instrument's classification according to FAS 115
HPGR _k	Vector of House Price Growth Rates for quarters q=1...40 of the Stress Period

3.7.2.1.2 Multi-Class MBSs and Derivative Mortgage Securities

[a] The information in Table 3-57 is required for Multi-Class MBSs and Derivative Mortgage Securities held by an Enterprise at the start of the Stress Test. This information identifies the MBS and an Enterprise's holdings.

TABLE 3–57—RBC REPORT INPUTS FOR MULTI-CLASS AND DERIVATIVE MBS CASH FLOWS

Variable	Description
CUSIP Number	A unique number assigned to publicly traded securities by the Committee on Uniform Securities Identification Procedures
Issuer	Issuer of the security: FNMA, FHLMC, GNMA or other
Original Security Balance	Original principal balance of the security (notional amount for Interest-Only securities) at the time of issuance, multiplied by the Enterprise's percentage ownership
Current Security Balance	Initial principal balance, or notional amount, at the start of the Stress Period multiplied by the Enterprise's percentage ownership
Current Security Percentage Owned	The percentage of a security's total current balance owned by the Enterprise
Unamortized Balance	The sum of all unamortized discounts, premiums, fees, commissions, etc., such that the unamortized balance equals book value minus face value, adjusted by the Unamortized Balance Scale Factor.

[b] The Stress Test requires sufficient information about the cash flow allocation rules among the different classes of a Multi-Class MBS to determine the cash flows for the individual class(es) owned by an Enterprise, including descriptions of the component classes of the security, the underlying collateral, and the rules directing cash flows to the component classes. This information is obtained from offering documents or securities data services. In the Stress Test, this information is used either as an input to a commercial modeling service or, for securities that are not so modeled, to derive an approximate modeling treatment as described more fully in this section.

[c] If a Derivative Mortgage Security is itself backed by one or more underlying securities, sufficient information is required for each underlying security as described in the preceding paragraph.

3.7.2.1.3 Mortgage Revenue Bonds and Miscellaneous MRSs

[a] The Stress Test requires two types of information for Mortgage Revenue Bonds and miscellaneous MRS held by an Enterprise at the start of the Stress Test: information identifying the Enterprise's holdings and the contractual terms of the securities. The inputs required for these instruments are set forth in Table 3–58.

TABLE 3–58—RBC REPORT INPUTS FOR MRBS AND DERIVATIVE MBS CASH FLOWS

Variable	Description
CUSIP Number	A unique number assigned to publicly traded securities by the Committee on Uniform Securities Identification Procedures

TABLE 3-58—RBC REPORT INPUTS FOR MRBS AND DERIVATIVE MBS CASH FLOWS—Continued

Variable	Description
Original Security Balance	Original principal balance, multiplied by the Enterprise's percentage ownership
Current Security Balance	Initial principal balance (at start of Stress Period), multiplied by the Enterprise's percentage ownership
Unamortized Balance	The sum of all unamortized discounts, premiums, fees, commissions, etc., such that the unamortized balance equals book value minus face value, adjusted by the Unamortized Balance Scale Factor
Issue Date	The Issue Date of the security
Maturity Date	The stated Maturity Date of the security
Security Interest Rate	The rate at which the security earns interest, as of the reporting date
Principal Payment Window Starting Date, Down-Rate Scenario	The month in the Stress Test that principal payment is expected to start for the security under the statutory "down" interest rate scenario, according to Enterprise projections
Principal Payment Window Ending Date, Down-Rate Scenario	The month in the Stress Test that principal payment is expected to end for the security under the statutory "down" interest rate scenario, according to Enterprise projections
Principal Payment Window Starting Date, Up-Rate Scenario	The month in the Stress Test that principal payment is expected to start for the security under the statutory "up" interest rate scenario, according to Enterprise projections
Principal Payment Window Ending Date, Up-Rate Scenario	The month in the Stress Test that principal payment is expected to end for the security under the statutory "up" interest rate scenario, according to Enterprise projections
Security Rating	The most current rating issued by any Nationally Recognized Statistical Rating Organization (NRSRO) for this security, as of the reporting date. In the case of a "split" rating, the lowest rating should be given.
Security Rate Index	If the rate on the security adjusts over time, the index on which the adjustment is based
Security Rate Index Coefficient	If the rate on the security adjusts over time, the coefficient is the number used to multiply by the value of the index
Security Rate Index Spread	If the rate on the security adjusts over time, the spread is added to the value of the index multiplied by the coefficient to determine the new rate
Security Rate Adjustment Frequency	The number of months between rate adjustments
Security Interest Rate Ceiling	The maximum rate (lifetime cap) on the security
Security Interest Rate Floor	The minimum rate (lifetime floor) on the security

[b] The Payment Window Starting and Ending Dates are projected by the Enterprise on the basis of prospectus information or simulations from a dealer in the securities or other qualified source, such as the structured finance division of an accounting firm, for the two statutory scenarios.

3.7.2.2 Interest Rate Inputs

Interest rates projected for each month of the Stress Period are used to calculate principal amortization and interest payments for ARM MBSs and MRBs, and for Derivative Mortgage Securities with indexed coupon rates. This information is produced in section 3.3, Interest Rates, of this Appendix.

3.7.2.3 Mortgage Performance Inputs

Default and Prepayment rates for the loans underlying a single- or multiclass MBS are computed according to the characteristics of the loans as specified in this section 3.7.2, Mortgage-Related Securities Inputs. LTV and Census Region are not uniquely specified for the loans underlying a given security; instead, the Prepayment and Default rates are averaged over all LTV categories, weighted according to the distribution of LTVs given in Table 3–59. (This weighting applies to Time Zero, i.e., the start of the Stress Test; the weightings will change over time as individual LTV groups pay down at different rates. See section 3.7.3, Mortgage-Related Securities Procedures, of this Appendix.) Instead of Census Division, the national average HPI is used for all calculations in this section.

TABLE 3–59—AGGREGATE ENTERPRISE AMORTIZED ORIGINAL LTV (AOLTV₀) DISTRIBUTION¹

Original LTV	UPB Distribution	Wt Avg AOLTV for Range
00<LTV<=60		
60<LTV<=70		
70<LTV<=75		
75<LTV<=80		
80<LTV<=90		
90<LTV<=95		
95<LTV<=100		
100<LTV		

¹ SOURCE: RBC Report, combined Enterprises single-family sold loan portfolio. Table 3–59 is updated as necessary with combined Enterprises single-family sold loan group data from the RBC Report in accordance with OFHEO guideline #404. The contents of the table appear at <http://www.OFHEO.gov>.

NOTE: Amortized Original LTV (also known as the “current-loan-to-original-value” ratio) is the Original LTV adjusted for the change in UPB but not for changes in property value.

3.7.2.4 Third-Party Credit Inputs

For securities not issued by the Enterprise or Ginnie Mae, issuer Default risk is reflected by haircutting the instrument cash flows based on the rating of the security, as described in section 3.5, Counterparty Defaults, of this Appendix.

3.7.3 Mortgage-Related Securities Procedures

The following sections describe the calculations for (1) single class MBSs, (2) Multi-Class MBSs and derivative mortgage securities, and (3) MRBs and miscellaneous MRS.

3.7.3.1 Single Class MBSs

[a] The calculation of cash flows for single class MBSs is based on the procedures outlined earlier in section 3.6, Whole Loan Cash Flows, of this Appendix. The collateral (i.e., the mortgage pool) underlying each MBS is treated as one single family Loan Group with characteristics equal to the weighted average characteristics of the underlying loans.

[b] For each MBS, compute the scheduled cash flows specified in Table 3–33, as directed in section 3.6.3.3.3, Mortgage Amortization Schedule Procedures of this Appendix, with the following exceptions and clarifications:

1. The Net Yield Rate (NYR) is not used in the MBS calculation. Instead, the Pass-Through Rate (for Fixed-Rate MBSs) and INDEX + Net Margin (for Adjustable-Rate MBSs) are used.
2. PMT is not a direct input for MBSs. (That is, it is not specified in the RBC Report.) Instead, compute PMT from UPB, MIR and remaining amortizing term AT–A₀, using the standard mortgage payment formula (and update it as appropriate for ARMs, as described in the Whole Loan calculation).
3. For ARM MBS, interest rate and monthly payment adjustments for the underlying loans are calculated in the same manner as they are for ARM Loan Groups.
4. MBSs backed by Biweekly mortgages, GPMs, TPMs, GEMs, and Step mortgages are mapped into mortgage types as described in section 3.6, Whole Loan Cash Flows, of this Appendix.

[c] Use the Loan Group characteristics to generate Default and Prepayment rates as described in section 3.6.3.4.3, Single Family Default and Prepayment Procedures, of this Appendix. For the following explanatory variables that are not specified for MBSs, proceed as follows:

1. For fixed rate Ginnie Mae certificates and the small number of multifamily MBS held by the Enterprises, use the model coefficients for Government Loans. For loans underlying Ginnie Mae ARM certificates, use the conventional ARM model coefficients.
2. Set Investor Fraction (IF) = 7.56%
3. Set Relative Loan Size (RLS) = 1.0. For Ginnie Mae certificates, use RLS = 0.75.
4. For LTV_{ORIG} of the underlying loans: Divide the MBS’s single weighted average Loan Group into several otherwise identical Loan Groups (“LTV subgroups”), one for each Original LTV range specified in Table 3–59. UPB₀ for each of these LTV subgroups is the specified percentage of the aggregate UPB₀. AOLTV₀ for each subgroup is also specified in Table 3–59. For Ginnie Mae certificates, use only the 95 < LTV ≤ 100 LTV category and its associated weighted average LTV.

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5. For each LTV subgroup, compute LTV_0 as follows:

$$LTV_0 = AOLTV_0 \times \left(\frac{HPI_{ORIG}}{HPI_{AQ'_0}} \right)^{\frac{AQ_0}{AQ'_0}}$$

Where:

HPI = the national average HPI figures in Table 3-60 (updated as necessary from subsequent releases of the OFHEO HPI).

A_0 = weighted average age in months of the underlying loans immediately prior to the start of the Stress Test.

AQ_0 = weighted average age in quarters of the underlying loans immediately prior to the start of the Stress Test. $AQ_0 = int(A_0/3)$.

AQ'_0 = AQ_0 minus the number of whole quarters between the most recently available HPI at the start of the Stress Test and time zero.

If $AQ'_0 \leq 0$, then $LTV_0 = AOLTV_0$.

TABLE 3-60—HISTORICAL NATIONAL AVERAGE HPI ¹

Quarter ²	HPI	Quarter	HPI	Quarter	HPI
1975Q1	62.45	1983Q4	116.63	1992Q3	177.94
1975Q2	63.50	1984Q1	118.31	1992Q4	178.71
1975Q3	62.85	1984Q2	120.40	1993Q1	178.48
1975Q4	63.92	1984Q3	121.68	1993Q2	179.89
1976Q1	65.45	1984Q4	122.94	1993Q3	180.98
1976Q2	66.73	1985Q1	124.81	1993Q4	182.38
1976Q3	67.73	1985Q2	126.91	1994Q1	183.35
1976Q4	68.75	1985Q3	129.38	1994Q2	183.95
1977Q1	70.70	1985Q4	131.20	1994Q3	184.43
1977Q2	73.34	1986Q1	133.77	1994Q4	184.08
1977Q3	75.35	1986Q2	136.72	1995Q1	184.85
1977Q4	77.71	1986Q3	139.37	1995Q2	187.98
1978Q1	79.96	1986Q4	141.99	1995Q3	190.81
1978Q2	82.75	1987Q1	145.07	1995Q4	192.42
1978Q3	85.39	1987Q2	147.88	1996Q1	194.80
1978Q4	87.88	1987Q3	150.21	1996Q2	195.00
1979Q1	91.65	1987Q4	151.57	1996Q3	195.78
1979Q2	94.26	1988Q1	154.26	1996Q4	197.48
1979Q3	96.24	1988Q2	157.60	1997Q1	199.39
1979Q4	98.20	1988Q3	159.25	1997Q2	201.00
1980Q1	100.00	1988Q4	160.96	1997Q3	203.94
1980Q2	100.86	1989Q1	163.10	1997Q4	206.97
1980Q3	104.27	1989Q2	165.33	1998Q1	210.09
1980Q4	104.90	1989Q3	169.09	1998Q2	212.37
1981Q1	105.69	1989Q4	170.74	1998Q3	215.53

TABLE 3–60—HISTORICAL NATIONAL AVERAGE HPI ¹—Continued

Quarter ²	HPI	Quarter	HPI	Quarter	HPI
1981Q2	107.85	1990Q1	171.42	1998Q4	218.09
1981Q3	109.21	1990Q2	171.31	1999Q1	220.80
1981Q4	109.38	1990Q3	171.85	1999Q2	224.32
1982Q1	111.02	1990Q4	171.03	1999Q3	228.46
1982Q2	111.45	1991Q1	172.41	1999Q4	232.41
1982Q3	110.91	1991Q2	173.14	2000Q1	235.91
1982Q4	111.96	1991Q3	173.14	2000Q2	240.81
1983Q1	114.12	1991Q4	175.46	2000Q3	245.15
1983Q2	115.33	1992Q1	176.62		
1983Q3	116.15	1992Q2	176.26		

¹ These numbers are updated as necessary from subsequent releases of the HPI after 2000Q3.

² Note: If the underlying loans were originated before 1975, use the HPI from 1975Q1 as HPI_{ORIG}.

6. For each quarter q of the Stress Test, use UPB_q and the house price growth rates from the Benchmark regional time period:

$$LTV_q = LTV_0 \times \frac{\left(\frac{UPB_{m=3q-3}}{UPB_0} \right)}{\exp \sum_{k=1}^q HPGR_k}$$

7. Generate Default, Prepayment and Performance vectors PRE_m, DEF_m and PERF_m for each LTV subgroup. When LTV_{ORIG} is used as a categorical variable, use the corresponding range defined for each LTV subgroup in Table 3-59. For LTV subgroup 95 < LTV < 100, use 90 < LTV_{ORIG} in Table 3-35.

[d] For each LTV subgroup, do not compute any Loss Severity or Credit Enhancement amounts. MBS investors receive the full UPB of defaulted loans.

[e] Compute Total Principal Received (TPR), Total Interest Received (TIR), and Amortization Expense (AE) for each LTV subgroup as directed in section 3.6.3.7.3, Stress Test Whole Loan Cash Flow Procedures and section 3.6.3.8.3, Whole Loan Accounting Flows Procedures, of this Appendix, with the following exception:

1. For Net Interest Received (NIR), do not use the Net Yield Rate (NYR_m). Instead, use the Pass-Through Rate (PTR_m) for Fixed Rate Loans, and INDEX_{m-1-LB} + Wt Avg Net Margin, subject to rate resets as described in section 3.6.3.3.3, Mortgage

Amortization Schedule Procedures, [a]1.b.3) of this Appendix, for ARMs.

2. Calculate Recovery Principal Received using a Loss Severity rate of zero (LS = 0).

[f] Sum over the LTV subgroups to obtain the original MBS's TPR, TIR and AE for m = 1...RM.

[g] Apply counterparty Haircuts in each month m as follows:

1. Compute:

$$HctFac_m = \frac{m'}{120} \times \text{MaxHct}(R)$$

Where:

m' = m, except for MBS credit rating below

BBB where m'=120

R = MBS credit rating

2. Compute:

$$HctAmt_m = (TPR_m + TIR_m) \times HctFac_m$$

[h] The resulting values, for each MBS, of TPR, TIR, AE, and HctAmt for months m = 1...RM are used in the section 3.10, Operations, Taxes, and Accounting, of this Appendix.

3.7.3.2 REMICs and Strips

[a] Cash flows for REMICs and Strips are generated according to standard securities industry procedures, as follows:

1. From the CUSIP number of the security, identify the characteristics of the underlying collateral. This is facilitated by using a securities data service.
2. Calculate the cash flows for the underlying collateral in the manner described for whole loans and MBS, based on Stress

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Test interest, Default, and Prepayment rates appropriate for the collateral.

3. Calculate cash flows for the Multiclass MBS using the allocation rules specified in the offering materials.
4. Determine the cash flows attributable to the specific securities held by an Enterprise, applying the Enterprise's ownership percentage.
5. For securities not issued by the Enterprise or Ginnie Mae, reduce cash flows by applying the Haircuts specified in section 3.5, Counterparty Defaults, of this Appendix, as appropriate.

[b] If a commercial information service is used for steps [a] 1 through 4 of this section, the information service may model mortgage product types beyond those described for Whole Loans in section 3.6, Whole Loan Cash Flows, and ARM indexes in addition to those listed in section 3.3, Interest Rates, of this Appendix. In such cases, the cash flows used are generated from the actual data used by the information service for the underlying security.

3.7.3.3 Mortgage Revenue Bonds and Miscellaneous MRS

[a] Cash flows for mortgage revenue bonds and miscellaneous MRS are computed as follows:

1. From the start of the Stress Test until the first principal payment date at the start of the Principal Payment Window, the security pays coupon interest at the Security Interest Rate, adjusted as necessary according to the Security Rate Index and Adjustment information in Table 3-58, but pays no principal.
2. During the Principal Payment Window, the security pays principal and interest equal to the aggregate cash flow from a level pay mortgage whose term is equal to the length of the Principal Payment Window and whose interest rate is the Security Interest Rate. If the Security Interest Rate is zero (as in the case of zero-coupon MRBs), then the security pays principal only in level monthly payment amounts equal to the Current Security Balance divided by the length of the Principal Payment Window.
3. For securities not issued by the Enterprise or Ginnie Mae, reduce cash flows by applying the Haircuts specified in section 3.5, Counterparty Defaults, of this Appendix, as appropriate.

3.7.3.4 Accounting

Deferred balances are amortized as described in section 3.6.3.8, Whole Loan Accounting Flows, of this Appendix, using the Pass-Through Rate (or Security Interest Rate for MRBs) rather than the Net Yield Rate. For principal-only strips and zero-coupon MRBs, assume Allocated Interest is zero.

If the conditions in section 3.6.3.8.3.1[a]3.a. of this Appendix, apply, do not realize the full amount in the first month. Instead, amortize the deferred balances using a straight line method over a period from the start of the Stress Test through the latest month with a non-zero cash flow.

3.7.4 Mortgage-Related Securities Outputs

[a] The outputs for MBS and MRS Cash Flows, found in Table 3-61, are analogous to those specified for Whole Loans in section 3.6.4, Final Whole Loan Cash Flow Outputs, of this Appendix, which are produced for each security for each month.

TABLE 3-61—OUTPUTS FOR MORTGAGE-RELATED SECURITIES

Variable	Description
TPR _m	Total Principal Received in month m = 1...RM
TIR _m	Total Interest Received in month m = 1...RM
HctAmt _m	Total Haircut amount in month m = 1...RM
AE _m	Amortization Expense for months m = 1...RM

[b] These outputs are used as inputs to the Operations, Taxes, and Accounting component of the Stress Test, which prepares pro forma financial statements. See section 3.10, Operations, Taxes, and Accounting, of this Appendix.

3.8 Nonmortgage Instrument Cash Flows

3.8.1 Nonmortgage Instrument Overview

[a] The Nonmortgage Instrument Cash Flows component of the Stress Test produces instrument level cash flows and accounting flows (accruals and amortization) for the 120 months of the Stress Test for:

1. Debt
2. Nonmortgage investments
3. Guaranteed Investment Contracts (GICs)
4. Preferred stock
5. Derivative contracts
 - a. Debt-linked derivative contracts
 - b. Investment-linked derivative contracts
 - c. Mortgage-linked derivative contracts
 - d. Derivative contracts that hedge forecasted transactions
 - e. Non-linked derivative contracts

[b] Although mortgage-linked derivative contracts are usually linked to mortgage assets rather than nonmortgage instruments, they are treated similarly to debt-linked and investment-linked derivative contracts and, therefore, are covered in this section.

[c] Debt, nonmortgage investments, and preferred stock cash flows include interest

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(or dividends for preferred stock) and principal payments or receipts, while debt-linked, investment-linked, and mortgage-linked derivative contract cash flows are composed of interest payments and receipts only. Debt, nonmortgage investments, and preferred stock are categorized in one of six classes² as shown in Table 3–62.

TABLE 3–62—DEBT, NON-MORTGAGE INVESTMENTS, AND PREFERRED STOCK CLASSIFICATIONS

Classification	Description
Fixed-Rate Bonds or Preferred Stock	Fixed-rate securities that pay periodic interest or dividends
Floating-Rate Bonds or Preferred Stock	Floating-rate securities that pay periodic interest or dividends
Fixed-Rate Asset-Backed Securities	Fixed-rate securities collateralized by nonmortgage assets
Floating-Rate Asset-Backed Securities	Floating-rate securities collateralized by nonmortgage assets
Short-Term Instruments	Fixed-rate, short-term securities that are not issued at a discount and which pay principal and interest only at maturity
Discount Instruments	Securities issued below face value that pay a contractually fixed amount at maturity

[d] Derivative contracts consist of interest rate caps, floors, and swaps. The primary difference between financial instruments and derivative contracts, in terms of calculating cash flows, is that interest payments on financial instruments are based on principal amounts that are eventually repaid to creditors, whereas interest payments on derivative contracts are based on notional amounts that never change hands. Debt- and investment-linked derivative contracts are categorized in one of seven classes³ as shown in Table 3–63:

²In addition to the items listed here, there are instruments that do not fit into these categories. Additional input information and calculation methodologies may be required for these instruments.

³*Ibid.*

TABLE 3–63—DEBT- AND INVESTMENT-LINKED DERIVATIVE CONTRACT CLASSIFICATION

Classification	Description of Contract
Basis Swap	Floating-rate interest payments are exchanged based on different interest rate indexes
Fixed-Pay Swap	Enterprise pays a fixed interest rate and receives a floating interest rate
Floating-Pay Swap	Enterprise pays a floating interest rate and receives a fixed interest rate
Long Cap	Enterprise receives a floating interest rate when the interest rate to which it is indexed exceeds a specified level (strike rate)
Short Cap	Enterprise pays a floating interest rate when the interest rate to which it is indexed exceeds the strike rate
Long Floor	Enterprise receives a floating interest rate when the interest rate to which it is indexed falls below the strike rate
Short Floor	Enterprise pays a floating interest rate when the interest rate to which it is indexed falls below the strike rate

[e] Mortgage-linked swaps are similar to debt-linked swaps except that the notional amount of a mortgage-linked swap amortizes based on the performance of certain MBS pools. Mortgage-linked derivative contracts are divided into two classes⁴ as shown in Table 3–64:

TABLE 3–64—MORTGAGE-LINKED DERIVATIVE CONTRACT CLASSIFICATION

Classification	Description of Contract
Fixed-Pay Amortizing Swaps	Enterprise pays a fixed interest rate and receives a floating interest rate, both of which are based on a declining notional balance
Floating-Pay Amortizing Swaps	Enterprise pays a floating interest rate and receives a fixed interest rate, both of which are based on a declining notional balance

⁴*Ibid.*

[f] In a currency swap, the Enterprise receives payments that are denominated in a foreign currency and it makes payments in U.S. dollars. The main difference between currency swaps and the type of swaps dis-

cussed above is that in a currency swap principal amounts are actually exchanged between the two counterparties. Currency swaps are divided into two classes, as shown in Table 3-65.⁵

TABLE 3-65—CURRENCY SWAP CONTRACT CLASSIFICATION

Classification	Description of Contract
Fixed-for-Fixed Currency Swap	Enterprise receives fixed interest payments denominated in a foreign currency and makes fixed, US dollar-denominated payments
Fixed-for Floating Currency Swap	Enterprise receives fixed interest payments denominated in a foreign currency and makes payments in US dollar based on a floating interest rate

3.8.2 Nonmortgage Instrument Inputs

[a] The Nonmortgage Instrument Cash Flows component of the Stress Test requires numerous inputs. Instrument level inputs provided by the Enterprises in the RBC Report are listed in Table 3-66. Many instrument classes require simulated Interest Rates because their interest payments adjust periodically based on rates tied to various indexes. These rates are generated as described in section 3.3, Interest Rates, of this Appendix.

TABLE 3-66—INPUT VARIABLES FOR NONMORTGAGE INSTRUMENT CASH FLOWS

Data Elements	Description
Amortization Methodology Code	Enterprise method of amortizing deferred balances (e.g., straight line)
Asset ID	CUSIP or Reference Pool Number identifying the asset underlying a derivative position
Asset Type Code	Code that identifies asset type used in the commercial information service (e.g., ABS, Fannie Mae pool, Freddie Mac pool)
Associated Instrument ID	Instrument ID of an instrument linked to another instrument
Coefficient	Indicates the extent to which the coupon is leveraged or de-leveraged
Compound Indicator	Indicates if interest is compounded
Compounding Frequency	Indicates how often interest is compounded

TABLE 3-66—INPUT VARIABLES FOR NONMORTGAGE INSTRUMENT CASH FLOWS—Continued

Data Elements	Description
Counterparty Credit Rating	NRSRO's rating for the counterparty
Counterparty Credit Rating Type	An indicator identifying the counterparty's credit rating as short-term ('S') or long-term ('L')
Counterparty ID	Enterprise counterparty tracking ID
Country Code	Standard country codes in compliance with Federal Information Processing Standards Publication 10-4
Credit Agency Code	Identifies NRSRO (e.g., Moody's)
Current Asset Face Amount	Current face amount of the asset underlying a swap
Current Coupon	Current coupon or dividend rate of the instrument
Current Unamortized Discount	Current unamortized premium or unaccreted discount of the instrument adjusted by the Unamortized Balance Scale Factor. If the proceeds from the issuance of debt or derivatives or the amount paid for an asset were greater than par, the value should be positive. If the proceeds or the amounts paid were less than par, the value should be negative

⁵ *Ibid.*

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TABLE 3–66—INPUT VARIABLES FOR NONMORTGAGE INSTRUMENT CASH FLOWS—Continued

TABLE 3–66—INPUT VARIABLES FOR NONMORTGAGE INSTRUMENT CASH FLOWS—Continued

Data Elements	Description
Current Unamortized Fees	Current unamortized fees associated with the instrument adjusted by the Unamortized Balance Scale Factor. Generally fees associated with the issuance of debt or derivatives should be negative numbers. Fees associated with the purchase of an asset should generally be reported as positive numbers
Current Unamortized Hedge	Current unamortized hedging gains (positive) or losses (negative) associated with the instrument adjusted by the Unamortized Balance Scale Factor
Current Unamortized Other	Any other unamortized items originally associated with the instrument adjusted by the Unamortized Balance Scale Factor. If the proceeds from the issuance of debt or derivatives or the amount paid for an asset was greater than par, the value should be positive. If the proceeds or the amounts paid were less than par, the value should be negative
CUSIP_ISIN	CUSIP or ISIN Number identifying the instrument
Day Count	Day count convention (e.g., 30/360)
End Date	The last index repricing date
EOP Principal Balance	End of Period face, principal or notional, amount of the instrument
Exact Representation	Indicates that an instrument is modeled according to its contractual terms
Exercise Convention	Indicates option exercise convention (e.g., American Option)
Exercise Price	Par = 1.0; Options
First Coupon Date	Date first coupon is received or paid
Index Cap	Indicates maximum index rate
Index Floor	Indicates minimum index rate

Data Elements	Description
Index Reset Frequency	Indicates how often the interest rate index resets on floating-rate instruments
Index Code	Indicates the interest rate index to which floating-rate instruments are tied (e.g., LIBOR)
Index Term	Point on yield curve, expressed in months, upon which the index is based
Instrument Credit Rating	NRSRO credit rating for the instrument
Instrument Credit Rating Type	An indicator identifying the instruments credit rating as short-term ('S') or long-term ('L')
Instrument ID	An integer used internally by the Enterprise that uniquely identifies the instrument
Interest Currency Code	Indicates currency in which interest payments are paid or received
Interest Type Code	Indicates the method of interest rate payments (e.g., fixed, floating, step, discount)
Issue Date	Indicates the date that the instrument was issued
Life Cap Rate	The maximum interest rate for the instrument throughout its life
Life Floor Rate	The minimum interest rate for the instrument throughout its life
Look-Back Period	Period from the index reset date, expressed in months, that the index value is derived
Maturity Date	Date that the instrument contractually matures
Notional Indicator	Identifies whether the face amount is notional
Instrument Type Code	Indicates the type of instrument to be modeled (e.g., ABS, Cap, Swap)
Option Indicator	Indicates if instrument contains an option
Option Type	Indicates option type (e.g., Call option)

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TABLE 3-66—INPUT VARIABLES FOR NONMORTGAGE INSTRUMENT CASH FLOWS—Continued

Data Elements	Description
Original Asset Face Amount	Original face amount of the asset underlying a swap
Original Discount	Original premium or discount associated with the purchase or sale of the instrument adjusted by the Unamortized Balance Scale Factor. If the proceeds from the issuance of debt or derivatives or the amount paid for an asset were greater than par, the value should be positive. If the proceeds or the amounts paid were less than par, the value should be negative
Original Face	Original face, principal or notional, amount of the instrument
Original Fees	Fees or commissions paid at the time of purchase or sale adjusted by the Unamortized Balance Scale Factor. Generally fees associated with the issuance of debt or derivatives should be negative numbers. Fees associated with the purchase of an asset should generally be reported as positive numbers
Original Hedge	Gains (positive) or losses (negative) from closing out a hedge associated with the instrument at settlement, adjusted by the Unamortized Balance Scale Factor
Original Other	Any other amounts originally associated with the instrument to be amortized or accreted adjusted by the Unamortized Balance Scale Factor. If the proceeds from the issuance of debt or derivatives or the amount paid for an asset were greater than par, the value should be positive. If the proceeds or the amounts paid were less than par, the value should be negative
Parent Entity ID	Enterprise internal tracking ID for parent entity

TABLE 3-66—INPUT VARIABLES FOR NONMORTGAGE INSTRUMENT CASH FLOWS—Continued

Data Elements	Description
Payment Amount	Interest payment amount associated with the instrument (reserved for complex instruments where interest payments are not modeled)
Payment Frequency	Indicates how often interest payments are made or received
Performance Date	“As of” date on which the data is submitted
Periodic Adjustment	The maximum amount that the interest rate for the instrument can change per reset
Position Code	Indicates whether the Enterprise pays or receives interest on the instrument
Principal Currency Code	Indicates currency in which principal payments are paid or received
Principal Factor Amount	EOP Principal Balance expressed as a percentage of Original Face
Principal Payment Date	A valid date identifying the date that principal is paid
Settlement Date	A valid date identifying the date the settlement occurred
Spread	An amount added to an index to determine an instrument’s interest rate
Start Date	The date, spot or forward, when some feature of a financial contract becomes effective (e.g., Call Date), or when interest payments or receipts begin to be calculated
Strike Rate	The price or rate at which an option begins to have a settlement value at expiration, or, for interest-rate caps and floors, the rate that triggers interest payments
Submitting Entity	Indicates which Enterprise is submitting information
Trade ID	Unique code identifying the trade of an instrument

TABLE 3–66—INPUT VARIABLES FOR NONMORTGAGE INSTRUMENT CASH FLOWS—Continued

Data Elements	Description
Transaction Code	Indicates the transaction that an Enterprise is initiating with the instrument (e.g., buy, issue re-open)
Transaction Date	A valid date identifying the date the transaction occurred
UPB Scale Factor	Factor applied to UPB to adjust for timing differences
Unamortized Balances Scale Factor	Factor applied to Unamortized Balances to adjust for timing differences

[b] In addition to the inputs in Table 3-66, other inputs may be required depending on the characteristics of the instrument modeled. For example, the mortgage-linked derivative contract cash flows require inputs describing the performance of the mortgage assets to which they are linked, including Single Family Default and Prepayment rates (See section 3.6.3.4, Single Family Default and Prepayment Rates, of this Appendix). Mortgage-linked derivative contract identification numbers (Asset IDs) are used to link the derivative contract to the required pool information that will be used to calculate the cash flows of the corresponding swap.

3.8.3 Nonmortgage Instrument Procedures

In general, non mortgage instruments are modeled according to their terms. The general methodology for calculating cash flows for principal and interest payments is described in this section and is not intended to serve as definitive text for calculating all possible present and future complex instruments. As mentioned in section 3.8.2, Nonmortgage Instrument Inputs, of this Appendix, there are some instruments that may require additional input information and calculation methodologies. Simplifying assumptions are made for some instrument terms until they can be modeled more precisely.

3.8.3.1 Apply Specific Calculation Simplifications

[a] In order to produce cash flows, accruals, or amortization of deferred balances, the following simplifications are used for all instruments to which they apply. Should the language in any other portion of section 3.8, Nonmortgage Instrument Cash Flows, of this Appendix, seem to conflict with a statement in this section, the language in section 3.8.3.1 takes precedence.

1. For day count methodology, use one of three methodologies 30/360, Actual/360, and Actual/365. All special day counts

(i.e. Actual/366 B, Actual/366 S, Actual/366 E, and Actual/Actual) are treated as Actual/365.

2. Set the first index reset date to the First Coupon Date. If the Issue Date is later than the start of the Stress Test, use the Current Coupon Rate to determine the interest paid from Issue Date to First Coupon Date. When a calculation requires a rate that occurs before the start of the Stress Test, use the Current Coupon Rate. This applies to interest accrued but not paid for the start of the Stress test and to rate indexes where applying a Look Back Period requires data prior to the start of the Stress Test.
 - a. If periodic caps are zero, change them to 999.99; If periodic floors are greater than 1, change them to zero.
 - b. For instruments which have principal balance changes other than those caused by compounding interest, perform calculations as if the principal changes occur only on coupon dates (coupon dates on the fixed-rate leg for swaps) on or later than the first principal change date.
 - c. When using a rate index for a specified term in an option exercise rule or as an index, assume that rate is appropriate for the calculation. Do not convert from bond equivalent yield to another yield form for a discount, monthly pay, quarterly pay, semi-annual pay or annual pay instrument.
3. When applying the option exercise rule:
 - a. For zero coupon and discount securities, instruments with European options, and zero coupon swaps, evaluate option exercise only on dates listed in the instrument's option exercise schedule. For Bermudan options, evaluate option exercise on the first option date in the instrument's option exercise schedule and subsequent coupon dates (coupon dates on the fixed-rate leg for swaps). For American options, evaluate option exercise on the first option date in the instrument's option exercise schedule and subsequent monthly anniversaries of the instrument's first coupon date.
 - b. Assume all call/put premiums/discounts are zero except for zero coupon instruments (including zero coupon swaps and discount notes). For these exceptions, when calculating a rate to compare with the Enterprise Cost of Funds, use the yield to maturity calculated by equating the face or notional amount plus the unamortized discount at the start of the Stress Test to the present value of the face or notional amount at maturity.
 - c. Assume basis swaps and floating rate securities have no cancel, put, or call options.

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d. If the remaining maturity is greater than 360 months, use the equivalent-maturity Enterprise Cost of Funds as if the remaining maturity is 360 months.

e. In the Stress Test, no preferred stock issued by the Enterprise will be called.

3.8.3.2 Determine the Timing of Cash Flows

Project payment dates from the payment date immediately prior to the start of the stress test according to the Payment Frequency, First Coupon Date, and Maturity Date.

3.8.3.3 Obtain the Principal Factor Amount at Each Payment Date

[a] Where there is no amortization or prepayment of principal, the Principal Factor Amount is 1.0 for each payment date until the stated Maturity Date, when it becomes zero.

[b] For debt and debt-linked derivative contracts that amortize, either a principal or a notional amortization schedule must be provided. If amortization information is unavailable, then the Principal Factor Amount is 1.0 for each payment date until the stated Maturity Date, when it becomes zero.

[c] Monthly prepayment rates are 3.5 percent for fixed-rate and 2.0 percent for floating-rate asset-backed securities. Furthermore, asset-backed securities are modeled through a commercial information service where possible. Instruments that cannot be modeled through the commercial information service are treated in accordance with section 3.9, Alternative Modeling Treatments, of this Appendix.

[d] In the case of mortgage-linked derivative contracts, notional amounts are amortized based on the characteristics of the underlying pool in the manner described for principal balances of mortgage-backed securities held by an Enterprise in section 3.7, Mortgage-Related Securities Cash Flows, of this Appendix.

3.8.3.4 Calculate the Coupon Factor

The Coupon Factor applicable to a given period, which applies to dividends also, depends on day count conventions used to calculate the interest payments for the instrument. For example, the Coupon Factor for a bond that pays interest quarterly based on a non-compounded 30/360 convention would be 3 (representing the number of months in a quarter) times 30 days divided by 360 days, or 0.25. Table 3-67 lists the most common day count conventions.

TABLE 3-67—DAY COUNT CONVENTIONS

Convention	Coupon Factor Calculation
30/360	Number of days between two payment dates assuming 30 days per month/360
Actual/360	Number of days between two payment dates/360
Actual/365	Number of days between two payment dates/365
Actual/Actual	Number of days between two payment dates/Number of days in the year

3.8.3.5 Project Principal Cash Flows or Changes in the Notional Amount

For all financial instruments, principal outstanding for the current period is determined by multiplying the Original Face by the Principal Factor Amount for the current period. The principal payment equals the amount of principal outstanding at the end of the previous period less the principal outstanding at the end of the current period, or zero if the instrument has a notional amount.

3.8.3.6 Project Interest and Dividend Cash Flows

3.8.3.6.1 Non-Complex Financial Instruments

[a] *Fixed-Rate Instruments.* The current period principal outstanding is multiplied by the product of the Current Coupon and current period Coupon Factor and rounded to even 100ths of a dollar.

[b] *Zero-Coupon Bonds.* Interest payments equal zero.

[c] *Discount Notes.* Interest payments equal zero.

[d] *Floating-Rate Instruments.* Interest payments are calculated as principal outstanding multiplied by the coupon for the current period. The current period coupon is calculated by adding a spread to the appropriate interest rate index and multiplying by the Coupon Factor. The coupon for the current period is set to this amount as long as the rate lies between the periodic and lifetime maximum and minimum rates. Otherwise the coupon is set to the maximum or minimum rate.

[e] *Interest Rate Caps and Floors.* These derivative instruments pay or receive interest only if the underlying index is above a Strike Rate (for caps) or below it (for floors). Interest payments are based on notional amounts instead of principal amounts.

1. The interest payment on a long cap is the Original Face multiplied by the amount,

if any, by which the index exceeds the Strike Rate, as defined by the equation in Table 3-68. The interest payment on a long floor is the Original Face multiplied by the amount, if any, by which the index is below the Strike Rate. Otherwise interest payments are zero for caps and floors. Interest payments are either paid or received depending on whether the Enterprise is in a long or short position in a cap or a floor.

2. Monthly cash flows for long caps and floors are calculated as illustrated in Table 3-68:

TABLE 3-68—CALCULATION OF MONTHLY CASH FLOWS FOR LONG CAPS AND FLOORS

Instrument	Cash Flows
Cap	$(1-K) \times N \times D$ if $I > K$; 0 if $I \leq K$
Floor	$(K-I) \times N \times D$ if $I < K$; 0 if $I \geq K$

Where:

N = Original Face

K = Strike Rate

I = interest rate index

D = Coupon Factor

[f] *Swaps*. A derivative contract in which counterparties exchange periodic interest payments. Each swap leg (pay side or receive side) is modeled as a separate instrument, with interest payments based on the same notional amount but different interest rates.

1. For debt- and investment-linked swaps, each leg's interest payment is determined in the same manner as payments for fixed-rate, floating-rate or zero coupon instruments as described in paragraph [a], [b] and [d] of this section.
2. For mortgage-linked swaps, calculate the reduction in the notional amount due to scheduled monthly principal payments (taking into account both lifetime and reset period caps and floors), Prepayments, and Defaults of the reference MBS or index pool. Reduce the notional amount of the swap for the previous period by this amount to determine the notional amount for the current period. Calculate interest payments or receipts for a given period as the product of the notional amount of the swap in that period, the coupon, and the Coupon Factor applicable for that period.

3.8.3.6.2 Complex Financial Instruments

[a] Some instruments have more complex or non-standard features than those described in section 3.8.3.6.1, Non-Complex Financial Instruments, of this Appendix. These complexities can include more sophisticated variants of characteristics such as principal or notional amortization schedules, interest

accrual methodologies, coupon reset formulas, and option features. In these instances, additional information may be required to completely specify the contractual cash flows or a proxy treatment for these instruments.

[b] An example of an instrument with complex features is an indexed amortizing swap. This instrument is non-standard because its notional amount declines in a way that is related to the level of interest rates. Its amortization table contains a notional amount reduction factor for a given range of interest rates. To compute cash flows for this instrument, reduce the notional amount on each payment date as specified in the amortization table. (The notional amount at the beginning of the Stress Period is given as an input to the calculation.)

[c] Special treatment is also required for foreign-currency-linked notes, the redemption value of which is tied to a specific foreign exchange rate. These require special treatment because the Stress Test does not forecast foreign currency rates. If these instruments are currency-hedged, then the note plus the hedge comprise a synthetic debt instrument for which only the pay side of the swap is modeled. If these instruments are not currency-hedged, the following treatment applies:

1. In the up-rate scenario, the U.S. dollar per unit of foreign currency ratio is increased in proportion to the increase in the ten-year CMT; therefore, the amount of an interest or principal payment is increased accordingly. For example, if the ten-year CMT shifts up by 50 percent, then the U.S. dollar per unit of foreign currency ratio shifts up by 50 percent. In the Stress Test, the payment would be multiplied by 1.5.
2. In the down-rate scenario, the foreign currency per U.S. dollar ratio is decreased in proportion to the decrease in the ten-year CMT.

[d] Futures and Options on Futures also require special treatment:

1. Settle positions on their expiration dates. Exercise only in-the-money options (settlement value greater than zero).
2. Settle all contracts for cash
3. Calculate the cash settlement amount—the change in price of a contract from the contract trade date to its expiration date. Calculate the price on the expiration date based on stress test interest rates (or, as necessary, forward rates extrapolated from these rates).
4. Amortize amounts received or paid at the expiration date into income or expense on a straight-line basis over the life of the underlying instrument (in the case of an option on a futures contract, the life of the instrument underlying the futures contract).

5. Amortize an option premium on a straight-line basis over the life of the option. (Amortize any remaining balances upon option exercise.)

[e] Swaptions also require special treatment:

1. Assume swap settlement (i.e., initiation of the underlying swap) when a swap option is exercised.
2. Calculate a “normalized” fixed-pay coupon by subtracting the spread over the index, if any, from the coupon on the fixed-rate swap leg.
3. For all exercise types (American, Bermudan, and European), consistent with RBC Rule section 3.8.3.7, assume exercise by the party holding the swap option if the equivalent maturity Enterprise Cost of Funds is more than
 - a. 50 basis points above the normalized fixed-pay coupon, for a pay-fixed swaption (a call or ‘payor’ swaption), or
 - b. 50 basis points below the normalized fixed pay coupon for a receive-fixed swaption (a put or ‘receiver’ swaption).
4. Amortize option premiums on a straight-line basis over the option term. (Amortize any remaining balances upon option exercise).

[f] CPI-Linked Instruments also require special treatment. The stress test lacks the ability to accommodate floating-rate instruments that reset in response to changes in the consumer price index (CPI) as published by the Bureau of Labor Statistics. Enterprise issuance of CPI-linked instruments is tied to swap market transactions intended to create desired synthetic debt structure and terms. In such cases, the true economic position nets to the payment terms of the related derivative contract. Accordingly, in order to accommodate and address the existence of CPI-linked instruments in the Enterprises’ portfolios, the net synthetic position shall be evaluated in the stress test. That is, for CPI-linked instruments tied to swap transactions that are formally linked in a hedge accounting relationship, the Enterprise should substitute the CPI-linked instrument’s coupon payment terms with those of the related swap contract.

[g] Pre-refunded municipal bonds also require special treatments. Pre-refunded municipal bonds are collateralized by securities that are structured to fund all the cash flows of the refunded municipal bonds until the bonds are callable. Since the call date for the bonds, also referred to as the pre-refunded date, is a more accurate representation of the payoff date than the contractual maturity date of the bonds, the stress test models the bonds to mature on the call date.

[h] If a financial instrument’s inputs are described in section 3.1, Data, of this Appendix, then model the instrument according to its terms; however, the Director reserves the authority to determine a more appropriate

treatment if modeling the instrument according to its terms does not capture the instrument’s impact on Enterprise risk. If the financial instrument’s inputs are not described in section 3.1, then treat it as described in section 3.9, Alternative Modeling Treatments, of this Appendix.

3.8.3.7 Apply Call, Put, or Cancellation Features, if Applicable

[a] In some cases, principal and interest cash flows may be altered due to options imbedded in individual financial instruments. Securities can be called or put and contracts can be cancelled at the option of the Enterprise or the counterparty. The Option Type, Exercise Convention Type, and the Start Date determine when an option may be exercised. There are three standard Exercise Convention Types, all of which are accommodated in the Stress Test:

- American—Exercise can occur at any time after the Start Date of the option.
- European—Exercise can occur only on the Start Date of the option.
- Bermudan—Exercise can occur only on specified dates, usually on coupon payment dates between the Start Date of the option and maturity.

[b] The options are treated in the following manner for each date on which the option can be exercised:

1. Project cash flows for the instrument with the imbedded option assuming that the option is not exercised. If the instrument is tied to an index, assume that the index remains constant at its value on that date.
2. Determine the discount rate that equates the outstanding balance of the security plus option premium and accrued interest to the sum of the discounted values of the projected cash flows. This discount rate is called the yield-to-maturity.
3. Convert the yield-to-maturity to a bond-equivalent yield and compare the bond-equivalent yield with the projected Enterprise Cost of Funds for debt with an equivalent maturity. Interpolate linearly if the maturity is not equal to one of the maturities specified in section 3.3, Interest Rates, of this Appendix.
4. If the equivalent-maturity Enterprise Cost of Funds is lower (higher) than 50 basis points below (above) the bond-equivalent yield of the callable (puttable) instrument, then the option is exercised. Otherwise, the option is not exercised, and it is evaluated at the next period when the option can be exercised.

[c] Some swap derivative contracts have cancellation features that allow either counterparty to terminate the contracts on certain dates. The cancellation feature is evaluated by comparing the fixed-rate leg of the swap to the Enterprise Cost of Funds. If either leg of the swap is cancelled, then the

other leg is cancelled concurrently. Cancellable swaps are treated in the following manner:

1. For each period when an option can be exercised, compare the swap's fixed-leg coupon rate to the Enterprise Cost of Funds with a maturity equivalent to the maturity date of the swap.
2. If the option is a Call, it is deemed to be exercisable at the discretion of the Enterprise. If the option is a Put, it is deemed to be exercisable at the discretion of the Counterparty. If the option is a PutCall, it is deemed to be exercisable at the discretion of either party to the swap. Exercise the option when the swap is out of the money for the party who holds the option. A swap is considered out of the money when the rate on its fixed leg is at least 50 basis point higher or lower, depending upon whether the fixed rate is paid or received, than the like-maturity Enterprise Cost of Funds. For zero coupon swaps in all option exercise periods, use the yield to maturity calculated by equating the notional amount plus the unamortized discount at the start of the Stress Test to the present value of the notional amount at maturity.
 - a. For example, if the Enterprise holds a call option for a fixed-pay swap and the coupon rate on the fixed-pay leg is at least 50 basis points above the Enterprise cost of funds for a maturity equivalent to that of the swap, then cancel the swap. Otherwise, the swap is not cancelled and it is evaluated the next time that the swap can be cancelled.

3.8.3.8 Calculate Monthly Interest Accruals for the Life of the Instrument

[a] Monthly interest accruals are calculated by prorating the interest cash flows on an actual-day basis. In this section, the term "from" means from and including, "to" means up to and not including, and "through" means up to and including. As an example, from the first to the third of a month is two days from the first through the third is three days. This convention is used to facilitate the day count and does not imply on which day's payments or accruals are actually made. Use one of the three following methodologies with the exception that interest cash flow dates occurring on or after the 30th of a month are considered as occurring on the last day of the month:

1. If the final interest cash flow occurs within the month, the interest accrual for

that month is calculated by multiplying the final interest cash flow amount (as calculated in section 3.8.3.6 of this Appendix) times the number of days from the beginning of the month through the final maturity date divided by the number of days from the previous interest cash flow date to the maturity date.

2. If an interest cash flow other than the final interest cash flow occurs within a month, the interest accrual for that month is determined by multiplying the interest cash flow amount for the current month times the number of days from the beginning of the month through the interest cash flow date, divided by the number of days from the previous interest cash flow date (or issue date) to this interest cash flow date. To this add the interest cash flow amount for the next interest cash flow date times the number of days from the current month's interest cash flow date to the end of the month, divided by the number of days from the current month's interest cash flow date to the following next interest cash flow date.
3. If no interest cash flows occur during a month other than the issue month, the monthly interest accrual is calculated by multiplying the next interest cash flow amount times the number of days in the month divided by the number of days from the previous interest cash flow date to the next interest cash flow date.
4. If the issue month occurs after the start of the Stress Test, the monthly interest accrual is calculated by multiplying the next interest cash flow amount by the number of days in the month minus the day of issue, divided by the number of days from the issue date to the next interest cash flow date.

3.8.3.9 Calculate Monthly Amortization (Accretion) of Premiums (Discounts) and Fees

[a] Adjust monthly interest accruals (*see* section 3.10.3.6.1[a]3., of this Appendix) to reflect the value over time of discounts, premiums, fees and hedging gains and losses incurred (Deferred Balances). Amortize Deferred Balances that exist at the beginning of the Stress Test until the instrument's Maturity Date. If there are any put, call, or cancel options that are executed, amortize any remaining Deferred Balances in the execution month.

TABLE 3-69—INPUTS FOR NONMORTGAGE INSTRUMENT ACCOUNTING FLOWS

Variable	Description	Source
MD	Maturity Date	Table 3-66, Input Variables for Non-mortgage Instrument Cash Flows
UDB ₀	The sum of Current Unamortized Discount, Current Unamortized Hedge, and Current Unamortized Other (Deferred Balances) for the instrument at the start of the Stress Test	Table 3-66, Input Variables for Non-mortgage Instrument Cash Flows
MACRU _m	Monthly Interest Accruals	section 3.8.3.8, Calculate Monthly Interest Accruals for the Life of the Instrument
EOMPBAO _m	Principal Balance at the end of the month for months m = 0...RM after modeling all options execution	section 3.8.3.6, Project Interest and Dividend Cash Flows
EOMP _m	Principal Balance at the end of the month for months m = 0...RM before modeling any options execution	section 3.8.3.6, Project Interest and Dividend Cash Flows

1. Compute Remaining Term (RM) as follows:

$$RM = 12 \times (\text{year (MD)} - \text{year (STDT)}) + \text{month (MD)} - \text{month (STDT)} + 1$$

Where:

STDT is the Starting Date of the Stress Test

2. For nonmortgage instruments with notional principal, calculate the monthly Amortization Amount (AA_m) for each month m = 1...RM:

$$AA_m = -\frac{UDB_0}{RM} \text{ if } EOMPBAO_m > 0$$

$$AA_m = -UDB_{m-1} \text{ if } EOMPBAO_m = 0$$

$$UDB_m = UDB_{m-1} + AA_m$$

3. For nonmortgage instruments with principal and interest payments,

a. Compute Allocated Interest for all months m (AI_m) as follows:

$$AI_m = \left[\frac{EOMP_{m-1}}{\sum_{k=0}^{RM} EOMP_k} \right] \times \sum_{k=1}^{RM} MACRU_k$$

b. Calculate the monthly Internal Rate of Return (IRR) that equates the adjusted cash flows (actual principal plus allocated interest) to the Initial Book Value (BV₀) of the instrument. Solve for IRR such that:

$$BV_0 = \sum_{m=1}^{RM} \frac{ACF_m}{(1 + IRR)^m}$$

Where:

$$BV_0 = EOMP_{B0} + UPD_0$$

$$ACF_m = EOMP_{B_{m-1}} - EOMP_{B_m} + AI_m$$

c. Calculate the monthly Amortization Amount (AA_m) for each month m = 1...RM:

$$AA_m = (BV_{m-1} \times IRR) - AI_m \text{ if } EOMPBAO_m > 0$$

$$AA_m = -UDB_{m-1} \text{ if } EOMPBAO_m = 0$$

$$UDB_m = UDB_{m-1} + AA_m$$

$$BV_m = EOMPBAO_m + UDB_m$$

4. For discount notes,

a. Calculate Remaining Maturity in Actual Days (RMD):

$$RMD = MD - STDT + 1$$

b. Calculate the month Amortization Amount (AA_m) for each month m = 1...RM:

$$AA_m = -UDB_0 \times \frac{ADAYS_m}{RDM}$$

if EOMPBAO_m > 0

$$AA_m = -UDB_{m-1} \text{ if EOMPBAO}_m = 0$$

$$UDB_m = UDB_{m-1} + AA_m$$

Where:

ADAYS_m = actual number of days in month m (days from the first of the month through maturity in month RM)

5. For zero coupon bonds,
a. Calculate Remaining Maturity in Actual Days (RMD):

$$RMD = MD - STDT + 1$$

- b. Calculate Yield Factor (YF):

$$YF = \left(\frac{EOMPBO}{EOMPBO + UDB_0} \right)^{\frac{1}{RMD}}$$

- c. Calculate the monthly Amortization Factor (AF_m) for each month m = 1...RM:

$$AF_m = 1 \text{ if } m = 0$$

$$AF_m = AF_{m-1} \times YF^{ADAYS_m}$$

Where:

ADAYS_m = actual number of days in month m (days from the first of the month through maturity in month RM):

- d. Calculate the monthly Amortization Amount (AA_m) for each month m = 1...RM

$$AA_m = (EOMPBO + UDB_0) \times (AF_m - AF_{m-1})$$

if EOMPBAO_m > 0

$$AA_m = -UDB_{m-1} \text{ if EOMPBAO}_m = 0$$

$$UDB_m = UDB_{m-1} + AA_m$$

3.8.3.10 Apply Counterparty Haircuts

[a] Finally, the interest and principal cash flows received by the Enterprises for non-mortgage instruments other than swaps and foreign currency-related instruments are

Haircut (i.e., reduced) by a percentage to account for the risk of counterparty insolvency, if a counterparty obligation exists. The amount of the Haircut is calculated based on the public rating of the counterparty and time during the stress period in which the cash flow occurs, as specified in section 3.5, Counterparty Defaults, of this Appendix.

[b] An Enterprise may issue debt denominated in, or indexed to, foreign currencies, and eliminate the resulting foreign currency exposure by entering into currency swap agreements. The combination of the debt and the swap creates synthetic debt with principal and interest payments denominated in U.S. dollars. The Haircuts for currency swaps are applied to the pay (dollar-denominated) side of the currency swaps, or to the cash outflows of the synthetic debt instrument. Therefore, the payments made by the Enterprise on a foreign currency contract are increased by the haircut amount. The Haircuts and the Phase-in periods for currency swaps are detailed in Table 3-31, under Derivative Contracts.

[c] Haircuts for swaps that are not foreign currency related are applied to the Monthly Interest Accruals (as calculated in section 3.8.3.8, of this Appendix) on the receive leg minus the Monthly Interest Accruals on the pay leg when this difference is positive. Use the maximum haircut from Table 3-31 for periods before and after the implementation of netting, as appropriate. After the implementation of netting, net the swap proceeds for each counterparty before applying the haircuts. The following example applies to an Enterprise having two swaps with the same counterparty. On the first swap, the Enterprise pays fixed and receives floating and on the second swap it pays floating and receives fixed. If the counterparty is a net payer to the Enterprise, the haircuts will be applied to the sum of the two receive legs net of the sum of the two pay legs.

3.8.4 Nonmortgage Instrument Outputs

[a] Outputs consist of cash flows and accounting information for debt, nonmortgage investments, preferred stock, and derivative contracts. Cash flows and accounting information outputs are inputs to section 3.10, Operations, Taxes, and Accounting, of this Appendix.

[b] Cash flows include the following monthly amounts:

1. Interest and principal payments for debt and nonmortgage investments,
2. Dividends and redemptions for preferred stock, and
3. Interest payments for debt-linked, investment-linked, and mortgage-linked derivative contracts.

[c] Accounting information includes the following monthly amounts:

1. Accrued interest and

- 2. Amortization of discounts, premiums, fees and other deferred items.

3.9 Alternative Modeling Treatments

3.9.1 Alternative Modeling Treatments Overview

[a] This section provides treatment for items that cannot be modeled in one of the ways specified in paragraph [b] of this section, but must be included in order to run the Stress Test. Because the rule provides treatments for a wide variety of instruments and activities that can be applied to accommodate unusual instruments, OFHEO expects few items to fall into this category.

[b] An Alternative Modeling Treatment (AMT) applies to any on- or off-balance-sheet item that is missing data elements required to calculate appropriate cash flows, or any instrument with unusual features for which this Appendix does *not*:

1. Provide an explicit computational procedure and set of inputs (i.e., the Appendix specifies exact data inputs and procedures for a class of instruments to which the item belongs); or,
2. Provide an implicit procedure (used for a general class of instruments), and explicit inputs that allow the item to be fully characterized for computational purposes (i.e., the Appendix specifies procedures and data inputs for a class of instruments to which the item does not belong that can be applied to the item to accurately compute its cash flows); or
3. Provide an implicit procedure by exact substitution, i.e., by representing the item as a computationally equivalent combination of other items that are

specified in paragraphs (1) or (2) in this section (i.e., the Appendix specifies treatments for two or more instruments, which, in combination, exactly produce the item's cash flows); or

4. Permit the approximation of one or more computational characteristics by other similar values that are explicitly specified in this Appendix, or in the RBC Report instructions (i.e., the Appendix specifies a treatment, or combination of treatments, that can be used as a reasonable proxy for the computational characteristics of the item). Such proxy treatments must be approved by OFHEO. OFHEO may, in its discretion, approve a proposed proxy treatment, adopt a different proxy treatment, or treat items for which a proxy treatment has been proposed by the Enterprises according to the remaining provisions of section 3.9, Alternative Modeling Treatments, of this Appendix.

[c] For a given on- or off-balance sheet item, the appropriate AMT is determined according to the categories specified in section 3.9.3, Alternative Modeling Treatments Procedures, of this Appendix, based on the information available for that item. The output for each such item is a set of cash and accounting flows, or specific amounts to be applied in section 3.12, Calculation of the Risk-Based Capital Requirement, of this Appendix.

3.9.2 Alternative Modeling Treatments Inputs

Table 3-70 identifies the minimal inputs that are used to determine an AMT. (*See also* section 3.1, Data, of this Appendix)

TABLE 3-70—ALTERNATIVE MODELING TREATMENT INPUTS

Variable	Description
TYPE	Type of item (asset, liability or off-balance sheet item)
BOOK	Book Value of item (amount outstanding adjusted for deferred items)
FACE	Face Value or notional balance of item for off-balance sheet items
REMATUR	Remaining Contractual Maturity of item in whole months. Any fraction of a month equals one whole month.
RATE	Interest Rate
INDEX	Index used to calculate Interest Rate
FAS115	Designation that the item is recorded at fair value, according to FAS 115
RATING	Instrument or counterparty rating
FHA	In the case of off-balance sheet guarantees, a designation indicating 100% of collateral is guaranteed by FHA
MARGIN	Margin over an Index

3.9.3 Alternative Modeling Treatments Procedures

For each item, one of the following alternatives will be applied:

3.9.3.1 Off-Balance Sheet Items

[a] If the item is a guarantee of a tax-exempt multifamily housing bond, or a single family or multifamily whole-loan REMIC class rated triple-A, or other similar transaction guaranteed by the Enterprises, multiply the face value of the guaranteed instruments by 0.45 percent. This amount is added to the amount of capital required to maintain positive total capital throughout the ten-year Stress Period. Any instruments or obligations with 100 percent of collateral guaranteed by the Federal Housing Administration (FHA) are excluded from this calculation.

[b] Otherwise, add to the amount of capital required to maintain positive total capital throughout the ten-year Stress Period an amount equal to the face or notional value of the item at the beginning of the Stress Period times three percent.

3.9.3.2 Reconciling Items

Reconciling items falling into this category will be treated according to the specifications in section 3.10, Operations, Taxes, and Accounting, of this Appendix.

3.9.3.3 Balance Sheet Items

[a] If the item is a trading security recorded at fair value according to FAS 115, then the book value (the face value adjusted for deferred balances) will be converted to cash in the first month of the Stress Test.

[b] Otherwise, if the item is an earning asset, then it is treated as a held-to-maturity asset, based on book value, as follows:

1. In the up-rate scenario, it will be treated as a held-to-maturity bond paying compound interest on a 30/360 basis at maturity, with the item's contractual maturity and rate. The item will be Haircut according to its rating. If no maturity is provided, maturity will be set at 120 months. If no rate is provided, a rate will be assigned at the Initial Enterprise Cost of Funds whose term is equal to the remaining maturity, less 200 basis points (but not less than zero). If no rating is provided, the asset will be classified as unrated.
2. In the down-rate scenario, it will be treated as a held-to-maturity bond paying compound interest on a 30/360 basis at maturity, with the item's contractual maturity and rate. The item will be Haircut according to its rating. If no maturity is provided, maturity will be set at 120 months. If no rate is provided, a rate will be assigned at the floating one-month Enterprise Cost of Funds less 200

basis points (but not less than zero). If no rating is provided, the asset will be classified as unrated.

[c] If the item is a non-earning asset it will remain on the books and earn no interest throughout the Stress Period.

[d] Otherwise, if the item is a liability, then it is treated as follows, based on book value:

1. In the up-rate scenario, it will be treated as non-callable and monthly coupon-paying to maturity on a 30/360 basis. If the coupon rate is not specified, the liability will be given a floating rate at the one-month Enterprise Cost of Funds plus 200 basis points. If no maturity is provided, maturity will be set at 120 months.
2. In the down-rate scenario, it will be treated as non-callable and monthly coupon paying to maturity. If no coupon is provided, the liability will be given a fixed rate at the Initial Enterprise Cost of Funds plus 200 basis points. If no maturity is provided, maturity will be set at ten years.

[e] Unamortized Balances should be amortized on a straight-line basis over the designated remaining maturity of the instrument.

[f] All items in this section are treated as if they had no options or cancellation features. The face value will be held constant until maturity. If an item has an adjustable rate, it is assumed that the interest rate will adjust monthly with no caps and a lifetime floor of zero percent.

3.9.4 Alternative Modeling Treatments Outputs

For each AMT item, the output is a set of cash and accounting flows appropriate to its respective treatment as specified in section 3.9.3, Alternative Modeling Treatments Procedures, or specific amounts to be applied in section 3.12, Calculation of the Risk-Based Capital Requirement, of this Appendix.

3.10 Operations, Taxes, and Accounting

3.10.1 Operations, Taxes, and Accounting Overview

This section describes the procedures for determining new debt issuance and investments, computing capital distributions, calculating operating expenses and taxes, and creating pro forma balance sheets and income statements. Input data include an Enterprise's balance sheet at the beginning of the Stress Period, interest rates from the Interest Rates component of the Stress Test, and the outputs from cash flow components of the Stress Test. The outputs of the procedures discussed in this section—monthly pro forma balance sheets, cash flow and income statements for each month of the Stress Test—are the basis for the capital calculation described in section 3.12, Calculation of

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the Risk-Based Capital Requirement, of this Appendix.

3.10.2 Operations, Taxes, and Accounting Inputs

[a] Data described in section 3.1, Data, section 3.3.4, Interest Rates Outputs, section 3.6.4, Final Whole Loan Cash Flow Outputs,

section 3.7.4, Mortgage-Related Securities Outputs, and section 3.8.4, Nonmortgage Instrument Outputs, of this Appendix, is used to produce monthly pro forma balance sheets and income statements for the Enterprises. In addition to the starting position data, described in the cash flow components, the Enterprises provide the starting position dollar values for the items in Table 3-71.

TABLE 3-71—OPERATIONS, TAXES, AND ACCOUNTING INPUTS

Input	Description
FAS 115 and 125 fair value adjustment on retained mortgage portfolio	
FAS 133 fair value adjustment on retained mortgage portfolio	
Reserve for losses on retained mortgage portfolio	
FAS 115 and 125 fair value adjustments on non-mortgage investments	
FAS 133 fair value adjustments on non-mortgage investments	
Total cash	
Accrued interest receivable on mortgages	
Accrued interest receivable on non-mortgage investment securities	
Accrued interest receivable on non-mortgage investment securities denominated in foreign currency—hedged	
Accrued interest receivable on non-mortgage investment securities denominated in foreign currency—unhedged	
Accrued interest receivable on mortgage-linked derivatives, gross	
Accrued interest receivable on investment-linked derivatives, gross	
Accrued interest receivable on debt-linked derivatives, gross	
Other accrued interest receivable	
Accrued interest receivable on hedged debt-linked foreign currency swaps	Underlying instrument is GSE issued debt
Accrued interest receivable on unhedged debt-linked foreign currency swaps	
Accrued interest receivable on hedged asset-linked foreign currency swaps	Underlying instrument is an asset
Accrued interest receivable on unhedged asset-linked foreign currency swaps	

TABLE 3–71—OPERATIONS, TAXES, AND ACCOUNTING INPUTS—Continued

Input	Description
Currency transaction adjustments—hedged assets	Cumulative gain or loss due to changes in foreign exchange rates relative to on-balance sheet assets originally denominated in foreign currency
Currency transaction adjustments—unhedged assets	Cumulative gain or loss due to changes in foreign exchange rates relative to unhedged assets and off-balance sheet items originally denominated in foreign currency
Federal income tax refundable	
Accounts receivable	
Fees receivable	
Low income housing tax credit investments	
Fixed assets, net	
Clearing accounts	Net book value of all clearing accounts
Other assets	
Foreclosed property, net	Real estate owned including property acquired through foreclosure proceedings
FAS 133 fair value adjustment on debt securities	
Accrued interest payable on existing fixed-rate debt securities	
Accrued interest payable on existing floating-rate debt securities	
Accrued interest payable on existing debt issued in foreign currency—hedged	
Accrued interest payable on existing debt issued in foreign currency—unhedged	
Accrued interest payable on mortgage-linked derivatives, gross	
Accrued interest payable on investment-linked derivatives, gross	
Accrued interest payable on debt-linked derivatives, gross	
Other accrued interest payable	
Accrued interest payable debt-linked foreign currency swaps—hedged	
Accrued interest payable debt-linked foreign currency swaps—unhedged	
Accrued interest payable asset-linked foreign currency swaps—hedged	
Accrued interest payable asset-linked foreign currency swaps—unhedged	

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TABLE 3-71—OPERATIONS, TAXES, AND ACCOUNTING INPUTS—Continued

Input	Description
Principal and interest due to mortgage security investors	Cash received on sold mortgages for onward submission to mortgage security investors
Currency transaction adjustments—hedged debt	Cumulative gain or loss due to changes in foreign exchange rates relative to on-balance sheet debt originally denominated in foreign currency
Currency transaction adjustments—unhedged debt	Cumulative gain or loss due to changes in foreign exchange rates relative to unhedged liabilities and off-balance sheet items originally denominated in foreign currency
Escrow deposits	Cash balances held in relation to servicing of multi-family loans
Federal income taxes payable	
Preferred dividends payable	
Accounts payable	
Other liabilities	
Common dividends payable	
Reserve for losses on sold mortgages	
Common stock	
Preferred stock, non-cumulative	
Additional paid-in capital	
Retained earnings	
Treasury stock	
Unrealized gains and losses on available-for-sale securities, net of tax, in accordance with FAS 115 and 125	
Unrealized gains and losses due to mark to market adjustments, FAS 115 and 125	
Unrealized gains and losses due to deferred balances related to pre-FAS 115 and 125 adjustments	
Unrealized gains and losses due to other realized gains, FAS 115	
Other comprehensive income, net of tax, in accordance with FAS 133	
OCI due to mark to market adjustments, FAS 133	
OCI due to deferred balances related to pre-FAS 133 adjustments	
OCI due to other realized gains, FAS 133	
Operating expenses	Average of prior three months

TABLE 3–71—OPERATIONS, TAXES, AND ACCOUNTING INPUTS—Continued

Input	Description
Common dividend payout ratio (average of prior 4 quarters)	Sum dollar amount of common dividends paid over prior 4 quarters and divided by the sum of total of after tax income less preferred dividends paid over prior 4 quarters
Common dividends per share paid 1 quarter prior to the beginning of the stress period	
Common shares outstanding	
Common Share Market Price	
Dividends paid on common stock 1 quarter prior to the beginning of the stress period	
Share Repurchases (average of prior 4 quarters)	Sum dollar amount of repurchased shares, net of newly issued shares, over prior 4 quarters and divided by 4
Off-balance-sheet Guarantees	Guaranteed instruments not reported on the balance sheet, such as whole loan REMICs and multifamily credit enhancements, and not 100% guaranteed by the FHA
Other Off-Balance Sheet Guarantees	All other off-balance sheet guaranteed instruments not included in another category, and not 100% guaranteed by the FHA
YTD provision for income taxes	Provision for income taxes for the period beginning January 1 and ending as of the report date
Tax loss carryforward	Net losses available to write off against future years' net income
Tax liability for the year prior to the beginning of the Stress Test	
Tax liability for the year 2 years prior to the beginning of the Stress Test (net of carrybacks)	
Taxable income for the year prior to the beginning of the Stress Test	
Taxable income for the year 2 years prior to the beginning of the Stress Test (net of carrybacks)	
Net after tax income for the quarter preceding the start of the stress test	
YTD taxable income	Total amount of taxable income for the period beginning January 1 and ending as of the report date
Minimum capital requirement at the beginning of the Stress Period	
Specific allowance for loan losses	Loss allowances calculated in accordance with FAS 114
Zero coupon swap receivable	
Unamortized discount on zero coupon receivable	

[b] Amounts required to reconcile starting position balances from cash flow components of the Stress Test with an Enterprise's balance sheet will be reported in the RBC Report with the related instrument. The corresponding balance for the related instrument will be adjusted accordingly.

3.10.3 Operations, Taxes, and Accounting Procedures

The Stress Test calculates new debt and investments, dividends, allowances for loan losses, operating expenses, and income taxes. These calculations are determined by, and also affect, the pro forma balance sheets and income statements during the Stress Period.

3.10.3.1 New Debt and Investments

[a] For each month of the Stress Test, cash deficits and surpluses are eliminated by issuing new debt or purchasing new investments. The Stress Test calculates cash received and cash disbursed each month in order to determine the net availability of cash. Depending on the calculated net cash position at month end, new short term investments are purchased at mid-month or a mix of long and short term debt is issued at mid-month so that the recalculated net cash position at month end is zero.

[b] For each month of the Stress Test, the following calculations are performed to determine the amount and type of new debt and investments. The short-term investments and appropriate mix of long-term and short-term debt are reflected in the pro forma balance sheets. Interest income or interest expense for the new investments or debt are reflected in the pro forma income statements.

1. In any month in which the cash position is positive at the end of the month, the Stress Test invests the Enterprise's excess cash on the 15th day of that month in one-month Treasury bills that yield the six-month Treasury rate for that month as specified in section 3.3, Interest Rates, of this Appendix.
2. In any month in which the cash position is negative at the end of the month, the Stress Test issues a mix of new short-term and long-term debt on the 15th day of that month. New short-term debt issued is six-month discount notes with a discount rate at the six-month Enterprise Cost of Funds as specified in section 3.3, Interest Rates, of this Appendix, with interest accruing on a 30/360 basis. New long-term debt issued is five-year bonds not callable for the first year ("five-year-no call-one") with an American call at par after the end of the first year, semiannual coupons on a 30/360 basis with principal paid at maturity or call, and a coupon rate set at the five year Enterprise Cost of Funds as speci-

fied in section 3.3, Interest Rates, of this Appendix, plus a 50 basis point premium for the call option. During the Stress Test, the call option for new long-term debt issued is not executed in the up-rate scenario and in the down-rate scenario follows the same call exercise rule as other debt. An issuance cost of 2.5 basis points is assessed on new short-term debt at issue and an issuance cost of 20 basis points is assessed on new long-term debt at issue. New long-term debt is issued to target a total debt mix of short- to long-term debt that is the same as the short- to long-term debt mix at the beginning of the Stress Test. Issuance fees for new debt are amortized on a straight line basis to the maturity of the appropriate instrument.

3. Given the Net Cash Deficit (NCD_m) in month m, use the following constants and method to calculate the amount of short-term and long-term debt to issue in month m:
 - a. Set the Issuance Cost on new short-term debt at issue (ISCOST):
ISCOST = 0.00025
 - b. Set the Issuance Cost on new long-term debt at issue (ILCOST):
ILCOST = 0.002
 - c. Calculate Net Short-term Debt Outstanding (NSDO_m) and Total Debt Outstanding (TDO_m) at the start of the Stress Test (m = 0) using the following methodology:
 - 1) For each month m and each debt and swap instrument i (each swap leg is considered a separate instrument), determine the Month of Next Repricing (MNR_{m,i}) defined as the first month greater than m in which the instrument matures or repricing can occur whether or not the coupon rate actually changes. Set the Principal Balance (PB_{m,i}) to be:
 - a) The principal (or notional principal) outstanding if the instrument cash flows are paid by the Enterprise,
 - b) Minus the principal (or notional principal) outstanding if the instrument cash flows are received by the Enterprise.
 - c) Zero if m is less than or equal to the issue month or the month in which an option exercised during the stress test would begin accruing cash flows to or from the Enterprise.
 - d) Zero if m is greater than or equal to the maturity month or the month in which an option exercised during the stress test would cease further cash flows to or from the Enterprise.
 - 2) Calculate NSDO_m by summing PB_{m,i} for all instruments where MNR_{m,i} is less than or equal to m plus 12.
 - 3) Calculate TDO_m by summing PB_{m,i} for instruments where MNR_{m,i} is greater than m.

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- d. Set the Maximum Proportion of Total Debt (MPD):

$$MPD = \frac{TDO_0 - NSDO_0}{TDO_0}$$

- e. Calculate Discount Rate Factor (DRF_m):

$$DRF_m = \left(1 + \frac{CF_m}{12}\right)^6$$

Where: CF_m = six month Enterprise Cost of Funds for month m

- f. Calculate the Adjustment Factor for Short-Term Debt Issuance Fees (AFSIF_m):

$$AFSIF_m = \frac{DRF_m}{1 - ISCOST \times DRF_m}$$

- g. Calculate the Adjustment Factor for Long-Term Debt Issuance Fees (AFLIF_m):

$$AFLIF_m = \frac{1}{1 - ILCOST}$$

- h. Calculate the Maximum Long-Term Issuance (MLTI_m):

$$MLTI_m = NCD_m \times AFLIF_m$$

- i. Calculate Net Short-Term Debt Outstanding (NSDO_m) and Total Debt Outstanding (TDO_m) for month m using the methodology described in paragraph 3.10.3.1.[b]3.c. of this appendix. *Note:* This calculation must reflect all new issuances, option exercises, and maturities between the beginning of the Stress Test and month m.

- j. Calculate Interim Face Amount of Long-Term Debt to be issued this month (IFALD_m):

$$IFALD_m = \frac{((MPD - 1) \times TDO_m) + NSDO_m + (MPD \times AFSIF_m \times NCD_m)}{1 - MPD + \left(AFSIF_m \times \frac{MPD}{AFLIF_m}\right)}$$

- k. Calculate Face Amount of Long-Term Debt to be issued (FALD_m):

$$FALD_m = \min(MLTI_m, \max(0, IFALD_m))$$

- l. Calculate Face Amount of Short-Term Debt to be issued (FASD_m):

$$FASD_m = AFSIF_m \times \max\left(0, NCD_m - \frac{FALD_m}{AFLIF_m}\right)$$

3.10.3.2 Dividends and Share Repurchases

[a] The Stress Test determines quarterly whether to pay dividends and make share repurchases. Dividends are decided upon and paid during the first month after the end of the quarter for which they are declared. If any dividends are paid, the dividend payout cannot exceed an amount equal to core capital less the estimated minimum capital requirement at the end of the quarter. Share repurchases are made during the middle month of the quarter.

- Preferred Stock.* An Enterprise will pay dividends on preferred stock as long as that Enterprise meets the estimated minimum capital requirement before and after the payment of these dividends.

Preferred stock dividends are based on the coupon rates of the issues outstanding. The coupon rates for any issues of variable rate preferred stock are calculated using projections of the appropriate index rate. Preferred stock dividends may not exceed core capital less the estimated minimum capital requirement at the end of the preceding quarter.

- Common Stock.* In the first year of the Stress Test, dividends are paid on common stock in each of the four quarters after preferred dividends, if any, are paid unless the Enterprise's capital is, or after the payment, would be, below the estimated minimum capital requirement.
 - First Quarter.* In the first quarter, the dividend is the dividend per share ratio

for common stock from the quarter preceding the Stress Test times the current number of shares of common stock outstanding.

b. *Subsequent Quarters.*

- 1) In the three subsequent quarters, if the preceding quarter's after tax income is greater than after tax income in the quarter preceding the Stress Test, (adjusted by the ratio of the Enterprise's retained earnings and retained earnings after adjustments are made that revert investment securities and derivatives to amortized cost), pay the larger of (1) the dividend per share ratio for common stock from the quarter preceding the Stress Test times the current number of shares of common stock outstanding or (2) the average dividend payout ratio for common stock for the four quarters preceding the start of the Stress Test times the preceding quarter's after tax income (adjusted by the reciprocal of the ratio of the Enterprise's retained earnings and retained earnings after adjustments are made that revert investment securities and derivatives to amortized cost) less preferred dividends paid in the current quarter. In no case may the dividend payment exceed an amount equal to core capital less the estimated minimum capital requirement at the end of the preceding quarter.
 - (2) If the previous quarter's after tax income is less than or equal to after tax income in the quarter preceding the Stress Test (adjusted by the ratio of the Enterprise's retained earnings and retained earnings after adjustments are made that revert investment securities and derivatives to amortized cost), pay the lesser of (1) the dividend per share ratio for common stock for the quarter preceding the Stress Test times the current number of shares of common stock outstanding or (2) an amount equal to core capital less the estimated minimum capital requirement at the end of the preceding quarter, but not less than zero.
3. *Share Repurchases.* In the first two quarters of the Stress Test, the capital of the Enterprises will be reduced to reflect the repurchase of shares. The amount of the capital reduction in each of those two quarters will be equal to the average net stock repurchases by the Enterprise during the four quarters preceding the start of the Stress Period. Net stock repurchases equal repurchases less receipts from new stock issued, but not less than zero. Repurchases in each of the first two quarters may occur only up to the point that the amount of core capital exceeds the estimated minimum capital requirement at the end of the first month of the quarter.

4. *Minimum Capital Requirements.* For the purposes of the Stress Test, the Enterprise's minimum capital requirement is computed by applying leverage ratios to all assets (2.50 percent) and off-balance sheet obligations (0.45 percent), and summing the results. Repurchases of an Enterprise's own previously-issued MBSs are excluded from the minimum capital calculation used in section 3.10.3.2, Dividends and Share Repurchases, of this Appendix.

3.10.3.3 Allowances for Loan Losses and Other Charge-Offs

[a] The Stress Test calculates a tentative allowance for loan losses monthly by multiplying current-month Credit Losses (CL in Table 3-52) by twelve, thus annualizing current month Credit Losses. This is a proxy for a loss contingency where it is probable that a loss has been incurred and the amount can be reasonably estimated. For both the retained and sold portfolios, these credit losses include lost principal (net of recoveries from credit enhancements and disposition of the real estate collateral), and foreclosure, holding, and disposition costs. If the tentative allowance for loan losses for the current period is greater than the balance from the prior month less charge-offs (i.e., credit losses) for the current month, a provision (i.e., expense) is recorded. Otherwise, no provision is made and the allowance for loan losses is equal to the prior period amount less current month charge-offs.

[b] Other charge-offs result from Haircuts related to mortgage revenue bonds, private-issue MBS, and non mortgage investments, described in their respective cash flow components.

1. In the case of Enterprise investments in securities, these Haircuts result in the receipt of less principal and interest than is contractually due. Lost principal is recorded as Other Losses when due and not received, while lost interest is recorded as a reduction of Interest Income.
2. In the case of interest rate derivative instruments, these Haircuts result in the receipt of less net interest than is contractually due from, or the payment of more interest than is contractually due to, an Enterprise counterparty. For those swaps that are linked to Enterprise investments, the increase or decrease of net swap interest due is recorded as an adjustment of Interest Income. For those swaps that are linked to Enterprise debt obligations, the increase or decrease of net swap interest due is recorded as an adjustment of Interest Expense.

3.10.3.4 Operating Expenses

[a] The Stress Test calculates operating expenses, which include non-interest costs

such as those related to an Enterprise's salaries and benefits, professional services, property, equipment and office space. Over the Stress Period, operating expenses are equal to the sum of two components. The first component in each month is equal to one-third ($\frac{1}{3}$) of the average monthly operating expenses of the Enterprise in the quarter immediately preceding the start of the Stress Test. The second component changes in proportion to the change in the size of the Enterprise's mortgage portfolio (i.e., the sum of outstanding principal balances of its retained and sold mortgage portfolios). The Stress Test calculates the Enterprise's mortgage portfolio at the end of each month of the Stress Period as a percentage of the portfolio at the start of the Stress Test, and then multiplies the percentage of assets remaining by two-thirds ($\frac{2}{3}$) of the average monthly operating expenses of the Enterprise in the quarter immediately preceding the start of the Stress Test.

[b] The sum of the two components in paragraph [a], of this section, is multiplied by a factor which equals

$$\left(1 - \frac{m}{36}\right)$$

for the first 12 months of the Stress Test and then equals two-thirds for months 13 and beyond. This product is the Enterprise's operating expense for a given month in the Stress Period.

3.10.3.5 Income Taxes

[a] Both Enterprises are subject to Federal income taxes, but neither is subject to state or local income taxes.

[b] The Stress Test applies an effective Federal income tax rate of 30 percent when calculating the monthly provision for income taxes (e.g., income tax expense). OFHEO may change the 30 percent income tax rate if there are significant changes in Enterprise experience or changes in the statutory income tax.

[c] The Stress Test sets income tax expense for tax purposes equal to the provision for income taxes. The effects of timing differences between taxable income and Generally Accepted Accounting Principles (GAAP) income before income taxes are ignored. Income before taxes is adjusted by the ratio of Enterprise retained earnings and retained earnings after adjustments are made that revert investment securities and derivatives to amortized cost. Therefore, Net Operating Loss (NOL) occurs only when the net income, before the provision for income taxes, is negative.

[d] Payments for estimated income taxes are made quarterly, in the month after the end of the quarter. At the end of each year, the annual estimated tax amount is com-

pared to the annual actual tax amount. In March of the next year, a payment of remaining taxes is made or a refund for overpayment of income taxes is received.

[e] The NOL for the current year is "carried back" to offset taxes in any or all of the preceding two calendar years. (The Enterprises' tax year is the same as the calendar year.) This offset of the prior years' taxes results in a negative provision for income taxes (e.g., income) for the current year. Use of a carry back reduces available carry backs in subsequent years. Any NOL remaining after carry backs are exhausted becomes a carry forward.

[f] Carry forwards represent NOLs that cannot be carried back to offset previous years' taxes, but can be used to offset taxes in any or all of the subsequent 20 years. Carry forwards accumulate until used, or until they expire 20 years after they are generated.

[g] A valuation adjustment is used to eliminate any deferred tax asset.

3.10.3.6 Accounting

[a] The 1992 Act specifies that total capital includes core capital and a general allowance for foreclosure losses. For the Enterprises, this general allowance is represented by general allowances for loan losses on their retained and sold mortgage portfolios. As defined at 12 CFR 1750.2, core capital includes the sum of the following components of equity:

1. The par or stated value of outstanding common stock,
2. The par or stated value of outstanding perpetual, noncumulative preferred stock,
3. Paid-in capital, and
4. Retained earnings.

[b] In order to determine the amount of total capital an Enterprise must hold to maintain positive total capital throughout the ten-year Stress Period, the Stress Test projects the four components of equity listed in paragraph [a] of this section plus general loss allowances as part of the monthly pro forma balance sheets.

[c] Details of an Enterprise's actual balance sheet at the beginning of the Stress Test are recorded from a combination of starting position balances for all instruments for which other components of the Stress Test calculate cash flows and other starting position balances for assets, liabilities, and equity accounts needed to complete an Enterprise's balance sheet.

[d] After recording an Enterprise's balance sheet at the beginning of the Stress Period, the Stress Test creates monthly pro forma balance sheets and income statements by recording output from the cash flow components of the Stress Test; recording new debt and investments (and related interest), dividends, loss allowances, operating expenses, and taxes; and applying accounting rules

pertaining to pro forma balance sheets and income statements.

3.10.3.6.1 Accounting for Cash Flows and Accounting Flows

[a] Balances at the beginning of the Stress Test are obtained from the RBC Report. Subsequent changes to related pro forma balance sheet and income statement accounts are obtained from data generated by cash flow components of the Stress Test as follows:

1. *Retained Loans.* For Retained Loans, interest cash flows in the first month of the Stress Period reduce accrued interest receivable at the beginning of the Stress Test. Subsequent months interest cash flows are recorded as accrued interest receivable and interest income in the month prior to receipt. When the interest cash flows are received, accrued interest receivable is reduced. Monthly principal cash flows (including Prepayments and defaulted principal) are recorded as reductions in the outstanding balance of the loan group. Net losses on Defaults are charged off against the allowance for loan losses. Amortization of deferred discounts increases interest income; amortization of deferred premiums decreases interest income.
2. *Mortgage Revenue Bonds.* For mortgage revenue bonds, interest cash flows in the first month of the Stress Period reduce accrued interest receivable at the beginning of the Stress Test. Subsequent months' interest cash flows are recorded as accrued interest receivable and interest income in the month prior to receipt. When the interest cash flows are received, accrued interest receivable is reduced. Monthly principal cash flows (including Prepayments) are recorded in the month received as a reduction in the outstanding balance of mortgage assets. Defaulted principal is charged off when due and is not received. Amortization of deferred discounts increases interest income; amortization of deferred premiums decreases interest income.
3. *Nonmortgage Instruments.* Principal repayments of nonmortgage instruments reduce the nonmortgage instrument and increases or decreases cash. When the interest cash flows are received or paid, accrued interest receivable or payable is reduced. Accrued interest includes both amounts at the beginning of the Stress Period and subsequent monthly accruals (also recorded as interest income or interest expense). Amortization of deferred discounts and premiums increases or decreases interest income or interest expense. Defaulted principal is charged off when due and not received.
4. *Sold Portfolio.* Sold portfolio cash flows include monthly guarantee fees, float, and principal and interest due MBS invest-

tors. Guarantee fees are recorded as income in the month received. Principal and interest due mortgage security investors does not affect the balance sheet; however, interest earned on these amounts (float) is recorded as income in the month the underlying principal and interest payments are received. Principal payments received and defaulted loan balances reduce the outstanding balance of the sold portfolio. Losses (net of recoveries) are charged off against the allowance for losses on the sold portfolio (a liability on the pro forma balance sheets) and reduce cash. Amortization of deferred premiums and discounts increases or decreases guarantee fees.

3.10.3.6.2 Accounting for Non-Cash Items

[a] Changes in the pro forma balances for other parts of the Enterprise's balance sheet not resulting from cash flows are recorded as described in the following nine steps:

1. *Unrealized Gains and Losses.*
 - a. The valuation impact of any Applicable Fair Value Standards (AFVS), cumulative from their time of implementation, will be reversed out of the starting position data, by debiting any accumulated credits, and crediting any accumulated debits.
 - (1) AFVS are defined as GAAP pronouncements that require or allow fair value measurements, e.g., EITF 99-20, FAS 65, FAS 87, FAS 115, FAS 133, FAS 140, FAS 149 and FIN 45. Valuation impacts of AVFS pertain only to amounts that are measured at fair value and not to other amounts that are included in AFVS but are not measured at fair value.
 - (2) The GAAP pronouncements covered by this treatment are subject to OFHEO review. The Enterprises will submit a list of standards and pronouncements that are being reversed in their RBC Reports.
 - b. After reversing the valuation impact of AFVS, any affected items are presented as follows:
 - (1) If absent the adoption of the AFVS, the affected transactions measured at fair value would have been accounted for on an amortized cost basis, they are presented as if they had always been accounted for on an amortized cost basis. Amounts not measured at fair value are represented as specified by GAAP and are presented using current GAAP rules.
 - (2) To the extent that transactions would not have been accounted for on an amortized cost basis, they are accounted for as if they were income and expense items.
2. *Low Income Housing Tax Credit Investments.* Low income housing tax credit investments at the beginning of the Stress Test are converted to cash on a straight line

- basis over the first six months of the Stress Period.
3. *Other Assets.* The following other assets at the beginning of the Stress Test are converted to cash as follows:
 - a. Clearing accounts and other miscellaneous receivables (e.g., fees receivable, accounts receivable, and other miscellaneous assets) in the first month of the Stress Test.
 - b. Earning assets (*see* section 3.9, Alternative Modeling Treatments, of this Appendix)
 - c. Items not covered by a. and b. of this section on a straight-line basis over the first five-years of the Stress Test.
 4. *Real Estate Owned (REO).* Real estate owned at the beginning of the Stress Test is converted to cash on a straight-line basis over the first six months of the Stress Test.
 5. *Fixed Assets.* 25 percent of fixed assets (net of accumulated depreciation) as of the beginning of the Stress Test remain constant over the Stress Test. The remaining 75 percent is converted to cash on a straight line basis over the ten-year Stress Period. Depreciation is included in the base on which operating expenses are calculated for each month during the Stress Period.
 6. *Principal and Interest Payable.* Principal and interest payable to an Enterprise's mortgage security investors at the beginning of the Stress Test are paid during the first two months of the Stress Test (one-half in month one and one-half in month two).
 7. *Other Liabilities.* The following liabilities at the beginning of the Stress Test are paid in the first month of the Stress Test, reducing cash:
 - a. Escrow deposits
 - b. Other miscellaneous liabilities
 8. *Commitments.* No gains or losses are recorded when commitments are added to the Enterprise's sold portfolio. *See* section 3.2.1, of this Appendix.
 9. *Fully-Hedged Foreign Currency-Denominated Liabilities.* Amounts that relate to currency swaps and foreign currency-denominated liabilities will be treated as follows:
 - a. Recorded balances that correspond to converted foreign currency-denominated liabilities will be amortized in a manner that is consistent with scheduled pay leg exchanges of notional amounts as set forth in corresponding currency swaps. The unamortized premiums, discounts and/or fees that are associated with these liabilities will be amortized as described in section 3.8, of this Appendix, as if they were associated with the pay legs of the corresponding currency swap. Any differences will be reflected as an increase or decrease in Retained Earnings.

- b. Interest payable amounts associated with currency swaps will be settled in a manner that is consistent with the contractual terms for these instruments.
- c. Receivable amounts associated with currency swaps and interest payable amounts associated with foreign currency-denominated debt will be reversed against Retained Earnings.
- d. The adjustments in a., b. and c., of this section, will take place at the start of the Stress Test. These treatments are not applied to instruments that are modeled under AMT (*see* section 3.9, Alternative Modeling Treatments, of this Appendix) or foreign currency-denominated instruments that are not fully hedged.

3.10.3.6.3 Other Accounting Principles

The following additional accounting principles apply to the pro forma balance sheets and income statements:

1. All investment securities are treated as held to maturity. As such, they are recorded as assets at amortized cost, not at fair value.
2. All non-securitized mortgage loans will be classified as "held-to-maturity" and will be accounted for on an amortized cost basis.
3. Effective control over the collateral for collateral financings is with the party that originally delivered such collateral.
4. Enterprise Real Estate Investment Trust (REIT) subsidiaries are consolidated. Specifically, REIT assets are treated as Enterprise assets. Preferred stock of the REIT is reflected as Enterprise debt. Dividends paid on the preferred stock are reported as interest expense.
5. Treasury stock is reflected as a reduction in retained earnings.

3.10.4 Operations, Taxes, and Accounting Outputs

For each month of the Stress Period, the Stress Test produces a pro forma balance sheet and income statement. The Operations, Taxes and Accounting component outputs 121 monthly and 11 annual balance sheets, 120 monthly and 10 annual income statements, and 120 monthly and 10 annual cash flow statements, including part-year statements for the first and last calendar years of the Stress Test when necessary. These pro forma financial statements are the inputs for calculation of the risk-based capital requirement (*see* section 3.12, Calculation of the Risk-Based Capital Requirement, of this Appendix).

3.11 Treatment of New Enterprise Activities

3.11.1 New Enterprise Activities Overview

[a] Given rapid innovation in the financial services industry, OFHEO anticipates the

Enterprises will become involved with new mortgage products, investments, debt and derivative instruments, and business activities, which must be accommodated in the Stress Test in order to capture all of the risk in the Enterprises' businesses. New accounting entries resulting from these innovations and changes in accounting must also be accommodated. The regulation is sufficiently flexible and complete to address new Enterprise activities as they emerge, using the procedures outlined in this section. However, OFHEO will monitor the Enterprises' activities and, when appropriate, propose amendments to this regulation addressing the treatment of new instruments, activities, or accounting treatments.

[b] For the purpose of this section of the Appendix, the term New Activity means any type of asset, liability, off-balance-sheet item, accounting entry, or activity to which a Stress Test treatment has not previously been applied. In addition, the Director has the discretion to treat as a New Activity: (1) any activity or instrument with characteristics or unusual features that create risks or hedges for the Enterprise that are not reflected adequately in the specified treatments for similar activities or instruments; and (2) any activity or instrument for which the specified treatment no longer adequately reflects the risk/benefit to the Enterprise, either because of increased volume or because new information concerning those risks/hedges has become available.

3.11.2 New Enterprise Activities Inputs

[a] Complete data and full explanations of the operation of the New Activity sufficient to understand the risk profile of the New Activity must be provided by the Enterprise. The Enterprises are required to notify OFHEO, pursuant to §1750.12(c), of proposals related to New Activities as soon as possible, but in any event no later than five calendar days after the date on which the transaction closes or is settled. The Enterprises are encouraged to suggest an appropriate capital treatment that will fully capture the credit and interest rate risk in the New Activity. Information on New Activities must also be submitted and appropriately identified as such in the RBC Report.

[b] The Stress Test will not give an Enterprise the capital benefit associated with a New Activity where OFHEO determines that the impact of that activity on the risk-based capital level of the Enterprise is not commensurate with the economic benefit to the Enterprise.

3.11.3 New Enterprise Activities Procedures

[a] OFHEO will analyze the risk characteristics and determine whether an existing approach specified in the Appendix appropriately captures the risk of the New Activ-

ity or whether some combination or adaptation of existing approaches specified in the Appendix is appropriate. For example, the Stress Test might employ its mortgage performance components and adapt its cash flow components to simulate accurately the loss mitigating effects and counterparty credit risk of credit derivatives.

[b] Where there is no reasonable approach using existing combinations or adaptations of treatments specified in this Appendix that could be applied within the timeframe for computing a quarterly capital calculation, the Stress Test will employ an appropriately conservative treatment, consistent with OFHEO's role as a safety and soundness regulator. Such treatment may include an alternative modeling treatment specified in section 3.9, Alternative Modeling Treatments, of this Appendix, or some other conservative treatment that OFHEO deems more appropriate.

[c] OFHEO will provide the Enterprise with its estimate of the capital treatment as soon as possible after receiving notice of the New Activity. In any event, the Enterprise will be notified of the capital treatment in accordance with the notice of proposed capital classification provided for in §1777.21 of this chapter.

[d] After a treatment has been incorporated into a final capital classification, OFHEO will provide notice of such treatment to the public, including the other Enterprise. OFHEO will consider any comments it receives from the public regarding the treatment during subsequent quarters. OFHEO may change the treatment as a result of such input or otherwise, if OFHEO determines that the risks of the New Activity are not appropriately reflected in a treatment previously adopted.

3.11.4 New Enterprise Activities Outputs

The Stress Test will generate a set of cash and/or accounting flows reflecting the treatment applied to the New Activity.

3.12 Calculation of the Risk-Based Capital Requirement

3.12.1 Risk-Based Capital Requirement Overview

The risk-based capital requirement is the sum of (1) the minimum amount of total capital that an Enterprise must hold at the start of the Stress Test in order to maintain positive total capital throughout the ten-year Stress Period, for all financial instruments explicitly modeled in the Stress Test (Stress Test capital subtotal) and (2) certain additional amounts relating to off-balance-sheet items addressed in section 3.9, Alternative Modeling Treatments, of this Appendix, and (3) 30 percent of that sum for management and operations risk. The Stress Test capital subtotal is determined based on

monthly total capital figures from the pro forma financial statements, the additional amounts related to off-balance-sheet items, and Enterprise short term borrowing and investment rates.

3.12.2 Risk-Based Capital Requirement Inputs

[a] Inputs to the capital calculation are outputs from section 3.3, Interest Rates, section 3.9, Alternative Modeling Treatments, and section 3.10, Operations, Taxes, and Accounting, of this Appendix.

[b] For each month of the Stress Test, the following inputs are from, or used in the creation of, pro forma financial statements projected in section 3.10, Operations, Taxes, and Accounting, of this Appendix:

1. Total capital
 - a. The par or stated value of outstanding common stock,
 - b. The par or stated value of outstanding perpetual, noncumulative preferred stock,
 - c. Paid-in capital,
 - d. retained earnings, and
 - e. allowance for losses on retained and sold mortgages less specific losses calculated in accordance with FAS 114,
2. Provision for income taxes (income tax expense),
3. Valuation adjustment that reduces benefits recorded from net operating losses when no net operating loss tax carrybacks are available, and
4. An Enterprise’s cash position prior to the decision to issue new debt or purchase new investments to balance the balance sheet (see section 3.10.3.1, New Debt and Investments, of this Appendix).

[c] For present-value calculations, the Stress Test uses the six-month Enterprise Cost of Funds or the six-month CMT yield as described in section 3.3, Interest Rates, of this Appendix.

[d] The amount for off-balance-sheet items that are not explicitly modeled is obtained from section 3.9.3.1, Off-Balance Sheet Items, of this Appendix.

3.12.3 Risk-Based Capital Requirement Procedures

[a] The following eight steps are used to determine the Stress Test capital subtotal and the risk-based capital requirement for an Enterprise:

1. Determine the effective tax rate in each month. If the provision for income taxes is positive (reflecting taxes owed) or negative (reflecting tax refunds to be received), then the effective tax rate is 30 percent. If the provision for income taxes is zero after applying any valuation adjustments (see section 3.10.3.6, Accounting, of this Appendix), then the effective tax rate applied in step 3. of this section is zero.
2. Determine whether an Enterprise is an investor or a borrower in each month of the Stress Period. In months where an Enterprise has outstanding six-month discount notes that were issued during the stress test, then the Enterprise is a borrower. Otherwise, the Enterprise is an investor.
3. Determine the appropriate monthly discount factor for each month of the Stress Period:
 - a. In months where an Enterprise is an investor, the monthly discount factor is based on the yield of short-term assets:

$$\text{Monthly Discount Factor} = \left[1 + \frac{(1 - \text{Effective Tax Rate}) \times 6\text{-month CMT yield}}{2} \right]^{1/6}$$

b. In months where an Enterprise is a borrower, the monthly discount factor is

based on the cost of the Enterprise’s short-term debt:

$$\text{Monthly Discount Factor} = \left[\frac{1 + \left[\frac{(1 - \text{Effective Tax Rate}) \times \left(\frac{6\text{-month Enterprise Cost of Funds}}{2} \right)}{1 - [(1 - \text{Effective Tax Rate}) \times 0.00025]} \right]}{1 - [(1 - \text{Effective Tax Rate}) \times 0.00025]} \right]^{1/6}$$

Where:

0.00025 is the factor that incorporates the issuance and administrative costs for an Enterprise’s new discount notes.

4. Compute the appropriate cumulative discount for each month of the Stress Period. The cumulative discount factor for a given month is the monthly discount factor for that month multiplied by the

cumulative discount factor for the preceding month. (The cumulative discount factor for the first month of the Stress Period is the monthly discount factor for that month.) Thus, the cumulative discount factor for any month incorporates all of the previous monthly discount factors.

5. Discount total capital for each month of the Stress Period to the start of the Stress Period for both interest rate scenarios. Divide the total capital for a given month by the cumulative discount factor for that month.
6. Identify the Stress Test capital subtotal, which is the lowest discounted total capital amount from among the 240 monthly discounted total capital amounts.
7. From the Stress Test capital subtotal, subtract the capital required for off-balance sheet items not explicitly modeled in the Stress Test, as calculated in section 3.9.3.1, Off-Balance Sheet Items, of this Appendix. Then subtract the resulting difference from the Enterprise's total capital at the start of the Stress Period. The resulting number is the amount of total capital that an Enterprise must hold at the start of the Stress Test in order to maintain positive total capital throughout the ten-year Stress Period.
8. Multiply the minimum total capital amount by 1.3 for management and operations risk.
9. Subtract the net increase (or add the net decrease) in Retained Earnings related to Fair Value Hedges at the start of the stress test made in accordance with section 3.10.3.6.2[a]1.b. of this appendix.

3.12.4 Risk-Based Capital Requirement Output

The output of the calculations in this section is the risk-based capital requirement for an Enterprise at the start date of the Stress Test.

4.0 GLOSSARY

This glossary is intended to define terms in the Regulatory Appendix that are used in a computationally specific sense that require a precise quantitative definition.

A

Accounting Flows: one or more series of numbers tracking various components of the accounting computations over time, analogous to "Cash Flows."

Age: of a Mortgage Loan, for computational purpose: the number of scheduled payment dates that have occurred prior to the time at which the Age is determined. The Age of a newly originated Mortgage is zero prior to its first payment date.

Amortization Expense: used in the accounting sense of the monthly allocation of a one-

time amount (positive or negative) over time, not to describe amortization of principal in a mortgage.

Amortization Schedule: for a Mortgage Loan, a series of numbers specifying the (1) principal and (2) interest components of each Mortgage Payment, and (3) the Unpaid Principal Balance after each such payment is made.

Allocated Interest: in certain accounting calculations, the amount of interest deemed to be received on a certain date according to an allocation formula, whether or not equal to the amount actually received on that date (see, e.g., section 3.6.3.8.3, Whole Loan Accounting Flows Procedures, of this Appendix).

Aggregate Limit: see section 3.6.3.6.4.1, Mortgage Credit Enhancement Overview, of this Appendix.

B

Balance Limit: see section 3.6.3.6.4.1, Mortgage Credit Enhancement Overview, of this Appendix.

Balloon Payment: the final payment of a Balloon Loan, the principal component of which is the entire Unpaid Principal Balance of said loan at the time the Balloon Payment is contractually due.

Balloon Loan: a Mortgage Loan that matures before the Unpaid Principal Balance is fully amortized to zero, thus requiring a large final Balloon Payment.

Balloon Date: the maturity date of a Balloon Loan.

Benchmark: used as an adjective to refer to the economic environment (including interest rates, house prices, and vacancy and rental rates) that prevailed in the region and time period of the Benchmark Loss Experience.

Benchmark Census Division: the Census Division, designated by OFHEO, that is used to determine house prices and vacancy and rental rates of the Stress Period.

Benchmark Loss Experience (BLE): the rates of default and loss severity of loans in the state/year combination (containing at least two consecutive origination years and contiguous areas with a total population equal to or greater than five percent of the population of the United States) with the highest loss rate.

Burnout: in describing Mortgage Prepayments, the reduced rates of Prepayment observed with Mortgage Loans that were not prepaid during earlier periods when it would have been advantageous to do so.

C

Cash Flow Hedges: cash flow hedges as defined by FAS 133.

Census Division: any one of the nine geographic areas of the United States so designated by the Bureau of the Census. The

OFHEO House Price Index determined at the Census Division level is used in the Stress Test.

Claim Amount: the amount of Credit Enhancement that an Enterprise is eligible to receive as a reimbursement on mortgage loan losses, which is often but not always equal to the total amount of the loss.

Commitment Loan Groups: hypothetical groups of Mortgage Loans assumed to be originated during the months immediately after the start of the Stress Test pursuant to Commitments made but not yet fulfilled by the Enterprises prior to the start of the Stress Test to purchase or securitize loans.

Contract: a Mortgage Credit Enhancement contract covering a distinct set of loans with a distinct set of contractual terms.

Constant Maturity Treasury (CMT) Rate: see table 3–18, Interest Rate and Index Inputs.

Counterparty Type: classification used to specify the appropriate Haircut level in section 3.5, Counterparty Defaults, of this Appendix.

Credit Enhancement: for the GSEs, agreements with lenders or third-parties put in place to reduce or limit mortgage credit (default) losses for an individual loan. See section 3.1.2.1.1, Loan Group Inputs, of this Appendix.

D

Debt Service Coverage Ratio: see section 3.6.3.5.3.1, Explanatory Variables, of this Appendix.

Default: for purposes of computing rates of mortgage default and losses, see the specific process specified in section 3.6.1, Whole Loan Cash Flows Overview, of this Appendix.

Defaulting Fraction: in any month, for any group of loans, the proportion of loans newly defaulted in that month expressed as a fraction of the *initial* loans (by number or by balance, depending on how Prepayment and Default Rates are measured) in the loan group; see, e.g., section 3.6.3.4.3.2, Prepayment and Default Rates and Performance Fractions, of this Appendix.

Defaulted UPB: the Unpaid Principal Balance (UPB) of a loan in the month that it Defaults.

Deferred Balances: see section 3.6.3.8.1, Whole Loan Accounting Flows Overview, of this Appendix.

Derivative Mortgage Security: generally refers to securities that receive cash flow with significantly different characteristics than the aggregate cash flow from the underlying mortgage loans, such as Interest-Only or Principal-Only Stripped MBSs or REMIC Residual Interests. See section 3.7.1, Mortgage-Related Securities Overview, of this Appendix.

Deposit Limit: see section 3.6.3.6.4.1, Mortgage Credit Enhancement Overview, of this Appendix.

Distinct Credit Combination (DCC): see section 3.6.3.6.4.1, Mortgage Credit Enhancement Overview, of this Appendix.

E

Enterprise Cost of Funds: Cost of funds used in computing the cost of new debt for the Enterprises during the Stress Test, as specified in section 3.3.3.[a]3.c., of this Appendix.

Enterprise Loss Position: see section 3.6.3.6.4.1, Mortgage Credit Enhancement Overview, of this Appendix.

F

Fair Value Hedges: fair value hedges as described in FAS 133.

Float Income: the earnings on the investment of loan principal and interest payments (net of the Servicing Fee and Guarantee Fee) from the time these payments are received from the servicer until they are remitted to security holders. See section 3.6.1, Whole Loan Cash Flows Overview, of this Appendix.

G

Gross Loss Severity: Loss Severity including the excess, if any, of Defaulted UPB over gross sale price of an REO property, fees, expenses and certain unpaid interest amounts, before giving effect to Credit Enhancement or any other amounts received on account of a defaulted loan (all such amounts expressed as a fraction of Defaulted UPB); see section 3.6.3.6.2, Single Family Gross Loss Severity, and section 3.6.3.6.3, Multifamily Gross Loss Severity, of this Appendix.

Guarantee Fee: the amount received by an Enterprise as payment for guaranteeing a mortgage loan; see, e.g., section 3.6.3.2, Payment Allocation Conventions, of this Appendix.

H

Haircut: the amount by which payments from a counterparty are reduced to account for a given probability of counterparty failure.

I

Initial: used as an adjective to specify conditions at the start of the Stress Test, except in defined terms; see also Time Zero.

Initial Rate Period: for an Adjustable Rate Mortgage, the number of months before the mortgage interest rate changes for the first time. Also known as “teaser period.”

Interest-only Period: for interest-only loans, the period of time for which the monthly payment covers only the interest due. (During the interest-only period, the UPB of the loan stays constant until maturity or a changeover date. For loans that mature, a Balloon Payment in the amount of the UPB is due at maturity. In other cases, the loan payment is recast at the changeover date

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and the loan begins to amortize over its remaining term.) See section 3.6.3.3.1, Mortgage Amortization Schedule Overview, of this Appendix.

Interest Rates: the Constant Maturity Treasury yields and other interest rates and indexes used in the Stress Test.

Investor-owned: a property that is not owner-occupied.

L

Loan Limit: used to describe a type of Credit Enhancement; see section 3.6.3.6.4.1, Mortgage Credit Enhancement Overview, of this Appendix.

Loan Group: a group of one or more mortgage loans with similar characteristics, that are treated identically for computational purposes in the Risk-Based Capital calculations.

Loss Severity: the amount of a mortgage loss divided by the Defaulted UPB.

Loss Sharing Arrangements (LSA): see section 3.6.3.6.4.1, Mortgage Credit Enhancement Overview, of this Appendix.

M

Maximum Haircut: as defined in section 3.5, Counterparty Defaults, of this Appendix.

Modified Pool Insurance: a form of Single Family Mortgage Credit Enhancement described in section 3.6.3.6.4.1, Mortgage Credit Enhancement Overview, of this Appendix.

Mortgage Insurance (Primary Mortgage Insurance): a type of credit enhancement that pays claims up to a given limit on each loan. See section 3.6.3.6.4.1, Mortgage Credit Enhancement Overview, of this Appendix.

Mortgage Related Security: a collective reference for (1) securities directly backed by mortgage loans, such as Single Class MBSS, Multi-Class MBSS (REMICs or Collateralized Mortgage Obligations (CMOs)); (2) Derivative Mortgage-Backed Securities (certain multi-class and strip securities) issued by Fannie Mae, Freddie Mac, and Ginnie Mae; (3) Mortgage Revenue Bonds issued by State and local governments and their instrumentalities; or (4) single class and Derivative Mortgage-Backed Securities issued by private entities. See section 3.1.2.2, Mortgage-Related Securities Inputs, of this Appendix.

N

Negative Amortization: as defined in section 3.6.3.2.1, Allocation of Mortgage Interest, of this Appendix.

Net Loss Severity: Gross Loss Severity reduced by Credit Enhancements and any other amounts received on account of a defaulted loan (all such amounts expressed as a fraction of Defaulted UPB).

Net Yield Rate: the Mortgage Interest Rate minus the Servicing Fee Rate.

New Activity: as defined in section 3.11, Treatment of New Enterprise Activities, of this Appendix.

Notional Amount: the amount analogous to a principal balance which is used to calculate interest payments in certain swap transactions or derivative securities.

O

Original: used as an adjective to specify values in effect at Loan Origination.

Origination: for a Mortgage Loan with monthly payments, the date one month prior to the first contractual payment date.

Owner-Occupied: a property, or a Mortgage Loan backed by a property, that is a single family residence which is the primary residence of the owner.

P

Pass-Through Rate: the Mortgage Interest Rate minus the Servicing Fee and the Guarantee Fee.

Performing Fraction: in any month, for any group of loans, the proportion of loans that have not either prepaid or defaulted in that month or any prior month, expressed as a fraction of the loans at the start of the Stress Test (by number or by balance, depending on how Prepayment and Default rates are measured) in a loan group; see e.g., section 3.6.3.4.3.2, Prepayment and Default Rates and Performance Fractions, of this Appendix.

Prepaying Fraction: in any month, for any group of loans, the proportion of loans that prepay in full in that month expressed as a fraction of the loans at the start of the Stress Test (by number or by balance, depending on how Prepayment and Default rates are measured) in the loan group; see e.g., section 3.6.3.4.3.2, Prepayment and Default Rates and Performance Fractions, of this Appendix.

Prepayment: the prepayment in full of a loan before its contractual maturity date

Prepayment Interest Shortfall: as defined in section 3.6.3.1, Timing Conventions, of this Appendix.

R

Risk-Based Capital (RBC) Report: The form in which Enterprise data is to be submitted for purposes of calculating the risk-based capital requirement, as described in section 3.1, Data, of this Appendix.

Relative Spread: as defined in section 3.6.3.4.3.1, Single Family Default and Prepayment Explanatory Variables, of this Appendix.

Retained Loans: as described in section 3.6.1, Whole Loan Cash Flows Overview, of this Appendix.

S

Scheduled Principal: the amount of principal reduction that occurs in a given month according to the Amortization Schedule of a mortgage loan; *see* section 3.6.3.3, Mortgage Amortization Schedule, of this Appendix.

Servicing Fee: portion of mortgage interest payment retained by servicer.

Sold Loans: as described in section 3.6.1, Whole Loan Cash Flows Overview, of this Appendix.

Spread Accounts: a form of Credit Enhancement; section 3.6.3.6.4, Mortgage Credit Enhancement, of this Appendix.

Stress Period: the 10-year period covered by the Stress Test simulation.

Stress Test: the calculation, which applies specified economic assumptions to Enterprise portfolios, described in this Appendix.

Strike Rate: the interest rate above/below which interest is received for caps/floors.

Subordination Agreements: a form of Credit Enhancement in which the cash flows allocable to a portion of a mortgage pool are used to cover losses on loans allocable to another portion of the mortgage pool; *see* section 3.6.3.6.4, Mortgage Credit Enhancement, of this Appendix.

T

Time Zero: used to designate the conditions in effect at the start of the Stress Test, as defined in section 3.6.3.1, Timing Conventions, of this Appendix.

U

Unpaid Principal Balance (UPB): the Unpaid Principal Balance of a loan or loan group based solely on its Amortization Schedule, without giving effect to any missed or otherwise unscheduled payments.

W

Whole Loan: a mortgage loan.

[66 FR 47806, Sept. 13, 2001, as amended at 67 FR 11861, Mar. 15, 2002; 67 FR 66535, Nov. 1, 2002; 68 FR 7312, Feb. 13, 2003; 71 FR 75087, Dec. 14, 2006]

APPENDIX B TO SUBPART B OF PART 1750
[RESERVED]

PART 1770—EXECUTIVE COMPENSATION

Sec.

1770.1 Authority and scope.

1770.2 Purpose.

1770.3 Definitions.

1770.4 Submission requirements.

1770.5 Compliance.

AUTHORITY: 12 U.S.C. 1452(h)(2), 1723a(d)(3)(B), 4501(6), 4502(3), 4502(7), 4513, 4514, 4517, 4518(a), 4631, 4632, 4636, 4641.

SOURCE: 66 FR 47554, Sept. 12, 2001, unless otherwise noted.

§ 1770.1 Authority and scope.

(a) *Authority*. Title XIII of the Housing and Community Development Act of 1992, Pub. L. No. 102-550, entitled the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (“the Act”) (12 U.S.C. 4501 *et seq.*), established the Office of Federal Housing Enterprise Oversight (“OFHEO”) as an independent office within the Department of Housing and Urban Development. In general, OFHEO is the safety and soundness regulator of two housing-related government sponsored enterprises: the Federal National Mortgage Association (“Fannie Mae”) and the Federal Home Loan Mortgage Corporation (“Freddie Mac”) (collectively, “the Enterprises”). The supervisory responsibilities of the Director of OFHEO (the “Director”) include oversight of compensation provided by the Enterprises to their executive officers.

(b) *Scope*. The procedures set forth in this part apply to OFHEO’s oversight of executive compensation under the following two statutory mandates:

(1) *Prohibition of excessive compensation*. The Act requires the Director to prohibit an Enterprise from providing compensation to any executive officer that is not reasonable and comparable with that paid by other similar businesses to executives doing similar work, *i.e.*, having similar duties and responsibilities. Businesses used for comparison purposes include publicly held financial institutions or major financial services companies. (12 U.S.C. 4518(a)). To effectuate this compensation oversight responsibility, the Act provides that the Director has full authority to take such actions as the Director determines are necessary. (12 U.S.C. 4513(8)). However, the Director may not prescribe or set a specific level or range of compensation for executive officers of the Enterprises. (12 U.S.C. 4518(b)).

(2) *Prior approval of termination benefits*. The Enterprises’ enabling statutes (“charter acts”) similarly provide that an Enterprise may not enter into any agreement or contract to provide any payment of money or other thing of

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current or potential value in connection with the termination of employment of an executive officer unless the agreement or contract is approved in advance by the Director. The Director may only approve termination benefits that are comparable to benefits provided by other public or private entities involved in financial services and housing interests to executives with comparable duties and responsibilities. Agreements or contracts that provide for termination payments to executives that were entered into before October 28, 1992 are not retroactively subject to approval or disapproval by the Director. However, a renegotiation, amendment or change to such an agreement or contract entered into on or before October 28, 1992 shall be considered as entering into an agreement or contract that is subject to approval by the Director. (Section 309(d)(3)(B); 12 U.S.C. 1723a(d)(3)(B) of Fannie Mae's Charter Act; Section 303(h)(2); 12 U.S.C. 1452(h)(2) of Freddie Mac's Corporation Act)

§ 1770.2 Purpose.

In exercising responsibilities related to executive compensation, the Director has established a structured process for the submission of relevant information by each Enterprise. This part codifies those procedures and clarifies the terms used therein in order to facilitate and enhance the efficiency of OFHEO's oversight.

§ 1770.3 Definitions.

The following definitions apply to the terms used in this part:

(a) *The Act* is Title XIII of the Housing and Community Development Act of 1992, Pub. L. No. 102-550, Oct. 28, 1992, 106 Stat. 3672, 3941 through 4012 (1993), 12 U.S.C. 4501 *et seq.*, separately entitled the "Federal Housing Enterprises Financial Safety and Soundness Act of 1992."

(b) *Affiliate* means, except as provided by the Director, any entity that controls, is controlled by, or is under common control with, an Enterprise.

(c) *Charter acts* mean the Federal National Mortgage Association Charter Act and the Federal Home Loan Mortgage Corporation Act, which are codified at 12 U.S.C. 1716 through 1723i and

12 U.S.C. 1451 through 1459, respectively.

(d) *Compensation* means any payment of money or the provision of any other thing of current or potential value in connection with employment. Compensation includes all direct and indirect payments of benefits, both cash and non-cash, granted to or for the benefit of any executive officer, including, but not limited to, payments and benefits derived from an employment contract compensation or benefit agreement, fee arrangement, perquisite, stock option plan, post employment benefit or other compensatory arrangement.

(e) *Director* means the Director of OFHEO or his or her designee.

(f) *Enterprise* means the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation and, except as provided by the Director, any affiliate thereof.

(g)(1) *Executive officer* means, with respect to an Enterprise:

(i) The chairman of the board of directors, chief executive officer, chief financial officer, chief operating officer, president, vice chairman, any executive vice president, and any individual who performs functions similar to such positions whether or not the individual has an official title; and

(ii) Any senior vice president (SVP) or other individual with similar responsibilities, without regard to title:

(A) Who is in charge of a principal business unit, division or function, or

(B) Who reports directly to the Enterprise's chairman of the board of directors, vice chairman, president or chief operating officer.

(2) The Director shall inform the Enterprises of those officers covered by this definition.

(h) *OFHEO* means the Office of Federal Housing Enterprise Oversight.

§ 1770.4 Submission requirements.

(a) *Submission of information to OFHEO.* All information required to be filed for purposes of this part is to be provided in a timely fashion by each Enterprise to OFHEO's Associate Director of the Office of Policy Analysis and Research, as specified in this section, or as designated by the Director.

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(b) *Categories of information relating to prohibition of excessive compensation.* The following materials, unless otherwise specified, shall be provided by each Enterprise to OFHEO for review within one week after the specified action or event:

(1) Resolutions, including supporting materials and related reports, from meetings of the Enterprise's committee responsible for compensation when the committee takes any action regarding a compensation matter that under the committee's authority is effective without further action by the committee or the board of directors;

(2) Resolutions, including supporting materials and related reports (not otherwise provided to OFHEO under paragraph (b)(1) of this section), from meetings of the board of directors relating to executive compensation when the board of directors takes any action regarding a compensation matter that is effective without any further action by the board of directors;

(3) Minutes, including supporting materials and related reports, when adopted by the committee responsible for compensation and those portions of minutes of the board of directors, including supporting materials and related reports, related to compensation matters (except for materials previously provided under paragraphs (b)(1) or (2) of this section);

(4) General benefit plans applicable to executive officers when adopted or amended;

(5) Any study conducted by or on behalf of an Enterprise with respect to compensation of executive officers;

(6) The Enterprise's annual compensation report to Congress when submitted;

(7) A current organizational chart when changes occur affecting the status of executive officers under this part;

(8) Proxy statements when issued; and,

(9) Such other information as deemed appropriate by the Director, except that submissions required under this paragraph shall not include materials related to the performance of specific individuals.

(c) *Timing of submissions related to prior approval of termination benefits.* All

relevant information, except as provided under §1770.5(a), should be provided to OFHEO, unless already provided under paragraph (b) of this section:

(1) Before an Enterprise enters into any agreement or contract with a new or existing executive officer that includes termination benefits;

(2) Before an Enterprise makes any extension or other amendment to such an agreement or contract;

(3) Before an Enterprise takes any other action to provide termination benefits to a specific executive officer, regardless of how effected; or

(4) When an Enterprise makes any changes to the termination provisions of any compensation or benefit program affecting multiple executive officers.

(d) *Specific information required for calculation of termination benefits.* For submissions under paragraph (c) of this section, an Enterprise shall submit to OFHEO the following materials:

(1) The details of the agreement or program change, e.g., employment agreements, termination agreements, severance agreements, and portions of minutes of the board of directors relating to executive compensation and minutes and supporting materials of the compensation Committee of the board of directors;

(2) All information, data, assumptions and calculations for the potential total dollar value or range of values of the benefits provided, such as but not limited to salary, bonus opportunity, short-term incentives, long-term incentives, special incentives and pension provisions or related contract or benefit terms; and

(3) Such other information deemed appropriate by the Director, except that information required to be submitted under paragraph (c) of this section or under this paragraph shall not include information on benefit plans of general applicability.

§ 1770.5 Compliance.

(a) An employment agreement or contract subject to the Director's prior approval, as set forth in §1770.1(b)(2), may be entered into prior to that approval, *provided that* such agreement or

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contract specifically provides that termination benefits under the agreement or contract shall not be effective and no payments shall be made thereunder unless and until approved by OFHEO. Such notice should make clear that alteration of benefit plans subsequent to OFHEO approval under this section, that affect final termination benefits of an executive officer, requires review at the time of the individual's termination from the Enterprise and prior to the payment of any benefits.

(b) Failure by an Enterprise to comply with the requirements this regulation may warrant remedial action by OFHEO. Such action may be taken in the form determined appropriate by the Director and may be taken separately from, in conjunction with, or in addition to any other corrective or remedial action, including an enforcement action to require an individual to make restitution to or reimbursement to the Enterprise of excessive compensation or inappropriately paid termination benefits.

PART 1773—FLOOD INSURANCE

Sec.

1773.1 Authority and scope.

1773.2 Requirements.

1773.3 Civil money penalties.

AUTHORITY: 12 U.S.C. 4521(a)(4), 4513, 4536(a); 42 U.S.C. 4001 note; 28 U.S.C. 2461 note; 42 U.S.C. 4012a(f)(3), (4), (8), (9), (10).

SOURCE: 66 FR 65101, Dec. 18, 2001, unless otherwise noted.

§ 1773.1 Authority and scope.

(a) *Authority.* The National Flood Insurance Act of 1968, title XII of Public Law 90-448, Aug. 1, 1968, 42 U.S.C. 4002 *et seq.*, and the Flood Disaster Protection Act of 1973, 42 U.S.C. 4002 *et seq.*, as amended by the National Flood Insurance Reform Act of 1994 ("NFIRA"), Public Law 103-325, Sept. 23, 1994, 42 U.S.C. 4001-4129, together create the National Flood Insurance Program ("NFIP") which established specific requirements applicable to the Enterprises. NFIRA designates OFHEO as the Federal agency responsible for determining compliance by the Enterprises with these statutes and with reporting to Congress biannually for six years on the Enterprises' compliance.

OFHEO has the authority to issue any regulations necessary to carry out the applicable provisions of NFIRA. OFHEO is also charged with enforcing the requirements of NFIRA as to the Enterprises and provides for the assessment of civil money penalties for violations of the procedures established by the Enterprises pursuant to the law or implementing regulations.

(b) *Scope.* This part sets forth the responsibilities of the Enterprises under NFIRA and the procedures to be used in any proceeding to assess civil money penalties against an Enterprise under NFIRA.

§ 1773.2 Requirements.

(a) *Procedures.* Each Enterprise shall implement procedures reasonably designed to ensure for any loan that is secured by improved real estate or a mobile home located in an area that has been identified, at the time of the origination of the loan or at any time during the term of the loan, by the Director of the Federal Emergency Management Agency as an area having special flood hazards and in which flood insurance is available under the NFIP, and purchased by such entity, the building or mobile home and any personal property securing the loan is covered for the term of the loan by flood insurance in an amount at least equal to the lesser of the outstanding principal balance of the loan or the maximum limit of coverage made available with respect to the particular type of property under the NFIP.

(b) *Applicability.* (1) Paragraph (a) of this section shall apply only with respect to any loan made, increased, extended, or renewed after September 22, 1995.

(2) Paragraph (a) of this section shall not apply to any loan having an original outstanding balance of \$5,000 or less and a repayment term of one year or less.

§ 1773.3 Civil money penalties.

(a) *In general.* If an Enterprise is determined by the Director of OFHEO to have engaged in a pattern or practice of purchasing loans in violation of the procedures established pursuant to the

NFIA, as amended, or to §1773.2, the Director may assess civil money penalties against such Enterprise in such amount or amounts as deemed to be appropriate under paragraph (c) of this section.

(b) *Notice and hearing.* A civil money penalty under this section may be assessed only after notice and an opportunity for a hearing on the record has been provided under 12 CFR part 1780.

(c) *Amount.* A civil money penalty under this section may not exceed \$385 for each violation. The total amount of penalties assessed under this section against an Enterprise during any calendar year may not exceed \$110,000.

(d) *Deposit of penalties.* Any penalties collected under this section shall be paid into the National Flood Mitigation Fund in accordance with 42 U.S.C. 4104d.

(e) *Additional penalties.* Any penalty under this section shall be in addition to, and shall not preclude, any civil remedy or criminal penalty otherwise available.

(f) *Statute of limitations.* No civil money penalty may be imposed under this section after the expiration of the four-year period beginning on the date of the occurrence of the violation for which the penalty is authorized under this section.

PART 1777—PROMPT CORRECTIVE ACTION

Sec.

1777.1 Authority, purpose, scope, and implementation dates.

1777.2 Preservation of other authority.

1777.3 Definitions.

Subpart A—Prompt Supervisory Response

1777.10 Developments prompting supervisory response.

1777.11 Supervisory response.

1777.12 Other supervisory action.

Subpart B—Capital Classifications and Orders Under Section 1366 of the 1992 Act

1777.20 Capital classifications.

1777.21 Notice of capital category, and adjustments.

1777.22 Limitation on capital distributions.

1777.23 Capital restoration plans.

1777.24 Notice of intent to issue an order.

1777.25 Response to notice.

1777.26 Final notice of order.

1777.27 Exhaustion and review.

1777.28 Appointment of conservator for a significantly undercapitalized or critically undercapitalized Enterprise.

AUTHORITY: 12 U.S.C. 1452(b)(2), 1456(c), 1718(c)(2), 1723a(k), 4513(a), 4513(b), 4514, 4517, 4611–4619, 4622, 4623, 4631, 4635.

SOURCE: 67 FR 3598, Jan. 25, 2002, unless otherwise noted.

§ 1777.1 Authority, purpose, scope, and implementation dates.

(a) *Authority.* This part is issued by the Office of Federal Housing Enterprise Oversight (OFHEO) pursuant to sections 1313, 1371, 1372, and 1376 of the Federal Housing Enterprises Financial Safety and Soundness Act (1992 Act) (12 U.S.C. 4513, 4631, 4632, and 4636). These provisions broadly authorize OFHEO to take such actions as are deemed appropriate by the Director of OFHEO to ensure that the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation (collectively, the Enterprises) maintain adequate capital and operate in a safe and sound manner.

(b) *Authority, purpose and scope of subpart A.* In addition to the authority set forth in paragraph (a) of this section, subpart A of this part is also issued pursuant to section 1314 of the 1992 Act (12 U.S.C. 4514), section 307(c) of the Federal Home Loan Mortgage Corporation Act (12 U.S.C. 1456(c)), and section 309(k) of the Federal National Mortgage Association Charter Act (12 U.S.C. 1723a(k)), requiring each Enterprise to submit such reports to OFHEO as the Director of OFHEO determines, in his or her judgment, are necessary to carry out the purposes of the 1992 Act. Subpart A of this part is also issued in reliance on section 1317 of the 1992 Act (12 U.S.C. 4517) authorizing OFHEO to conduct examinations of the Enterprises. The purpose of subpart A of this part is to set forth a framework of early intervention supervisory measures, other than formal enforcement actions, that OFHEO may take to address emerging developments that merit supervisory review to ensure they do not pose a current or future threat to the safety and soundness of an Enterprise. OFHEO's initiation of procedures under subpart A does not necessarily indicate that any unsound condition exists. The

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supervisory responses enumerated in § 1777.11 do not constitute orders under the 1992 Act for purposes of sections 1371 and 1376 thereof (12 U.S.C. 4631 and 4636).

(c) *Authority, purpose, and scope of subpart B.* In addition to the authority set forth in paragraph (a) of this section, subpart B of this part is also issued pursuant to subtitle B of the 1992 Act (12 U.S.C. 4611 through 4623), section 303(b)(2) of the Federal Home Loan Mortgage Corporation Act (12 U.S.C. 1452(b)(2)), and section 303(c)(2) of the Federal National Mortgage Association Charter Act (12 U.S.C. 1718(c)(2)). These provisions authorize OFHEO to administer certain capital requirements for the Enterprises, to classify the capital of the Enterprises based on capital levels specified in the 1992 Act, and, in appropriate circumstances, to exercise discretion to reclassify an Enterprise into a lower capital category. Under these provisions, there are also automatic consequences for an Enterprise that is not classified as adequately capitalized, as well as discretionary authority for OFHEO to require an Enterprise to take remedial actions. Subpart B implements the provisions of sections 1364 through 1368, 1369(b) through (e), 1369C, and 1369D of the 1992 Act as they apply to the Enterprises (12 U.S.C. 4614 through 4618, 4619(b) through (e), 4622 and 4623). The principal purposes of subpart B are to identify the capital measures and capital levels that OFHEO uses in determining the capital classification of an Enterprise; to set out the procedures OFHEO uses in determining such capital classifications; to establish procedures for submission and review of capital restoration plans of an Enterprise that is not classified as adequately capitalized; and to establish procedures under which OFHEO issues orders pursuant to section 1366(b)(1) through (4) of the 1992 Act (12 U.S.C. 4616(b)(1) through (4)).

(d) *Effective dates of capital classifications.* Section 1364 of the 1992 Act (12 U.S.C. 4614(d)) directs OFHEO to determine capital classifications for the Enterprises by reference to two capital standards, consisting of the minimum or critical capital level on the one hand, and the risk-based capital level

on the other. Section 1364(d) of the 1992 Act (12 U.S.C. 4614(d)) excludes consideration of whether the Enterprises meet the risk-based capital level in determining capital classifications or reclassifications under 1364, until one year after the effective date of OFHEO's regulation implementing OFHEO's risk-based capital test (issued under section 1361(e) of the 1992 Act (12 U.S.C. 4611(e))), until such time, section 1364(d) provides that an Enterprise is to be classified as adequately capitalized so long as it meets the minimum capital level. Subpart B contains a currently effective set of capital classifications omitting consideration of the risk-based capital level, as well as another set of capital classifications which will take effect, and displace the current set of capital classifications, on September 13, 2002 that is, one year after the effective date of OFHEO's risk-based capital rule published at 66 FR 47730, September 13, 2001.

§ 1777.2 Preservation of other authority.

(a) *Supervisory standards.* Notwithstanding the existence of procedures in § 1777.10 for the Director of OFHEO to designate certain developments for supervisory response under subpart A of this part, nothing in this part in any way limits the authority of OFHEO otherwise to take such actions with respect to any issue as is deemed appropriate by the Director of OFHEO to ensure that the Enterprises maintain adequate capital, operate in a safe and sound manner, and comply with the 1992 Act and regulations, orders, and agreements thereunder.

(b) *Capital floor.* Classification of an Enterprise as adequately capitalized in accordance with subtitle B of the 1992 Act and subpart B of this part indicates that the Enterprise meets the capital levels under sections 1361 and 1362 of the 1992 Act (12 U.S.C. 4611 and 4612) and regulations promulgated thereunder as of the times specified in the classification determination. Nothing in subpart B of this part or subtitle

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B of the 1992 Act limits OFHEO's authority otherwise to address circumstances that would require additional capital through regulations, orders, notices, guidance, or other actions.

(c) *Form of supervisory action or response.* In addition to the supervisory responses contemplated under subpart A of this part, and the authority to classify and reclassify the Enterprises, to issue orders, and to appoint conservators under subpart B of this part, the 1992 Act grants OFHEO broad discretion to take such other supervisory actions as may be deemed by OFHEO to be appropriate, including issuing temporary and permanent cease and desist orders, imposing civil money penalties, appointing a conservator under section 1369(a)(1) through (2) of the 1992 Act (12 U.S.C. 4619(a)(1) through (2)), entering into a written agreement the violation of which is actionable through enforcement proceedings, or entering into any other formal or informal agreement with an Enterprise. Neither the 1992 Act nor this part in any way limit OFHEO's discretion over the selection of the type of these actions, and the selection of one type of action under this part or under these other statutory authorities, or a combination thereof, does not foreclose OFHEO from pursuing any other action.

§ 1777.3 Definitions.

For purposes of this part, the following definitions will apply:

1992 Act means the Federal Housing Enterprises Financial Safety and Soundness Act, 12 U.S.C. 4501 *et seq.*

Affiliate means an entity that controls an Enterprise, is controlled by an Enterprise, or is under common control with an Enterprise.

Capital distribution means:

(1) Any dividend or other distribution in cash or in kind made with respect to any shares of, or other ownership interest in, an Enterprise, except a dividend consisting only of shares of the Enterprise; and

(2) Any payment made by an Enterprise to repurchase, redeem, retire, or otherwise acquire any of its shares or other ownership interests, including any extension of credit made to finance

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an acquisition by the Enterprise of such shares or other ownership interests, except to the extent the Enterprise makes a payment to repurchase its shares for the purpose of fulfilling an obligation of the Enterprise under an employee stock ownership plan that is qualified under section 401 of the Internal Revenue Code of 1986 (26 U.S.C. 401 *et seq.*) or any substantially equivalent plan as determined by the Director of OFHEO in writing in advance.

Core capital has the same meaning as provided in 12 CFR 1750.2.

Critical capital level means the amount of core capital that is equal to the sum of one half of the amount determined under 12 CFR 1750.4(a)(1) and five-ninths of the amounts determined under 12 CFR 1750.4(a)(2) through 1750.4(a)(7).

Enterprise means the Federal National Mortgage Association and any affiliate thereof, and the Federal Home Loan Mortgage Corporation and any affiliate thereof.

Minimum capital level means the minimum amount of core capital specified for an Enterprise pursuant to section 1362 of the 1992 Act (12 U.S.C. 4612), as determined under 12 CFR 1750.4.

OFHEO means the Office of Federal Housing Enterprise Oversight.

Risk-based capital level means the amount of total capital specified for an Enterprise pursuant to section 1361 of the 1992 Act (12 U.S.C. 4611), as determined under OFHEO's regulations implementing section 1361.

Total capital has the same meaning as provided at 12 CFR 1750.11(n).

Subpart A—Prompt Supervisory Response

§ 1777.10 Developments prompting supervisory response.

In the event of any of the following developments, OFHEO shall undertake one of the supervisory responses enumerated in § 1777.11, or a combination thereof:

(a) OFHEO's national House Price Index (HPI) for the most recent quarter is more than two percent less than the national HPI four quarters previously, or for any Census Division or Divisions

in which are located properties securing more than 25 percent of single-family mortgages owned or securing securities guaranteed by an enterprise, the HPI for the most recent quarter for such Division or Divisions is more than five percent less than the HPI for that Division or Divisions four quarters previously;

(b) An Enterprise's publicly reported net income for the most recent calendar quarter is less than one-half of its average quarterly net income for any four-quarter period during the prior eight quarters;

(c) An Enterprise's publicly reported net interest margin (NIM) for the most recent quarter is less than one-half of its average NIM for any four-quarter period during the prior eight quarters;

(d) For single-family mortgage loans owned or securities by an Enterprise that are delinquent ninety days or more or in foreclosure, the proportion of such loans in the most recent quarter has increased more than one percentage point compared to the lowest proportion of such loans in any of the prior four quarters; or

(e) Any other development, including conduct of an activity by an Enterprise, that OFHEO determines in its discretion presents a risk to the safety and soundness of the Enterprise or a possible violation of applicable law, regulation, or order.

§ 1777.11 Supervisory response.

(a) *Level I supervisory response*—(1) *Supervisory letter*. Not later than five business days after OFHEO determines that a development enumerated in §1777.10 has transpired, OFHEO shall deliver a supervisory letter alerting the chief executive officer or the board of directors of the Enterprise to OFHEO's determination.

(2) *Contents of supervisory letter*. The supervisory letter shall notify the Enterprise that, pursuant to this subpart, OFHEO is commencing review of a potentially adverse development. As is appropriate under the particular circumstances and the nature of the potentially adverse development, the letter may direct the Enterprise to undertake one or more of the following actions, as of such time as OFHEO directs:

(i) Provide OFHEO with any relevant information known to the Enterprise about the potentially adverse development, in such format as OFHEO directs;

(ii) Respond to specific questions and concerns that OFHEO poses about the potentially adverse development; and

(iii) Take appropriate action.

(3) *Review; further action*. Based on the Enterprise's response to the supervisory letter and consideration of other relevant factors, OFHEO shall promptly determine whether the Level I supervisory response is adequate to resolve any supervisory issues implicated by the potentially adverse development, or whether additional supervisory response under this section is warranted.

(4) *Sequence of supervisory responses*. The Level II through Level IV supervisory responses in paragraphs (b) through (d) of this section may be carried out in any sequence, including simultaneous performance of two or more such responses. OFHEO may also carry out one or more such responses simultaneously with a Level I supervisory response pursuant to this paragraph (a).

(b) *Level II supervisory response*—(1) *Special review*. In addition to any other supervisory response described in this section, OFHEO may conduct a special review of an Enterprise in order to assess the impact of the potentially adverse development on the Enterprise.

(2) *Review; further action*. Based on the results of the special review and consideration of other factors deemed by OFHEO to be relevant, OFHEO shall promptly determine whether additional supervisory response under this section is warranted.

(c) *Level III supervisory response*—(1) *Action plan*. In addition to any other supervisory response described in this section, OFHEO may direct the Enterprise to prepare and submit an action plan to OFHEO, in such format and at such time as OFHEO directs.

(2) *Contents of action plan*. Such action plan shall include, subject to additional direction by OFHEO, the following:

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(i) In the case of any potentially adverse development arising from conditions or practices internal to the Enterprise, any relevant information known to the Enterprise about the circumstances that led to the potentially adverse development;

(ii) An assessment of likely consequences that the potentially adverse development may have for the Enterprise; and

(iii) The proposed course of action the Enterprise will undertake in response to the potentially adverse development, including an explanation as to why such approach is preferred to any other alternative actions by the Enterprise and how such approach will address the concerns of OFHEO.

(3) *Review; further action.* If OFHEO in its discretion determines that the information, assessment, or proposed course of action contained in the action plan is incomplete or inadequate, OFHEO shall promptly direct the Enterprise to correct such deficiencies to the extent OFHEO determines such corrections will aid in resolving supervisory issues implicated by the potentially adverse development, and will promptly determine whether additional supervisory response under this section is warranted.

(d) *Level IV supervisory response*—(1) *Notice to show cause.* In addition to any other supervisory response described in this section, OFHEO may issue written notice to the chief executive officer or the board of directors of the Enterprise directing the Enterprise to show cause, on or before the date specified in the notice, why OFHEO should not issue one or more of the following:

(i) A notice of charges to the Enterprise under section 1371 of the 1992 Act (12 U.S.C. 4631) and the procedures in 12 CFR part 1780 commencing an action to order the Enterprise to cease and desist conduct, conditions, or violations specified in the notice to show cause;

(ii) A temporary order to the Enterprise under section 1372 of the 1992 Act (12 U.S.C. 4632) and the procedures in 12 CFR part 1780 to cease and desist from, and take affirmative actions to prevent or remedy harm from, conduct, conditions, or violations specified in the notice to show cause;

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(iii) A notice of charges under section 1376 of the 1992 Act (12 U.S.C. 4636) and the procedures in 12 CFR part 1780 commencing imposition of a civil money penalty against the Enterprise; or

(iv) A notice of discretionary reclassification of the Enterprise's capital classification under section 1364(b) of the 1992 Act (12 U.S.C. 4614(b)) and subpart B of this part.

(2) *Review; further action.* Based on the Enterprise's response to the notice to show cause and consideration of other relevant factors, OFHEO shall promptly determine whether to commence the actions described in the notice, and whether additional supervisory response under this section is warranted.

§ 1777.12 Other supervisory action.

Notwithstanding the pendency or completion of one or more supervisory responses described in § 1777.11, OFHEO may at any time undertake additional supervisory steps and actions in the form of any informal or formal supervisory tool available to OFHEO under the 1992 Act, including, but not limited to, issuing guidance or directives under section 1313 (12 U.S.C. 4513), requiring reports under section 1314 (12 U.S.C. 4514), conducting other examinations under section 1317 (12 U.S.C. 4517), issuing discretionary reclassification under section 1364 (12 U.S.C. 4614), initiating discretionary action under section 1366(b) (12 U.S.C. 4616(b)), appointing a conservator under section 1369(a) (12 U.S.C. 4619(a)), or initiating administrative enforcement action under sections 1371, 1372, and 1376 (12 U.S.C. 4631, 4632 and 4636). In addition, OFHEO may take any such steps or actions with respect to an Enterprise that fails to make a submission or comply with a directive as required by § 1777.11, or to address an Enterprise's failure to implement an appropriate action in response to a supervisory letter or under an action plan under § 1777.11.

Subpart B—Capital Classifications and Orders Under Section 1366 of the 1992 Act

§ 1777.20 Capital classifications.

(a) *Capital classifications after the effective date of section 1365 of the 1992 Act.*

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The capital classification of an Enterprise for purposes of subpart B of this part is as follows:

(1) *Adequately capitalized.* Except as otherwise provided under paragraph (a)(5) of this section, an Enterprise will be classified as adequately capitalized if the Enterprise:

(i) As of the date specified in the notice of proposed capital classification, holds total capital equaling or exceeding the risk-based capital level; and

(ii) As of the date specified in the notice of proposed capital classification, holds core capital equaling or exceeding the minimum capital level.

(2) *Undercapitalized.* Except as otherwise provided under paragraph (a)(5) of this section or §1777.23(c) or §1777.23(h), an Enterprise will be classified as undercapitalized if the Enterprise:

(i) As of the date specified in the notice of proposed capital classification, holds total capital less than the risk-based capital level; and

(ii) As of the date specified in the notice of proposed capital classification, holds core capital equaling or exceeding the minimum capital level.

(3) *Significantly undercapitalized.* Except as otherwise provided under paragraph (a)(5) of this section or §1777.23(c) or §1777.23(h), an Enterprise will be classified as significantly undercapitalized if the Enterprise:

(i) As of the date specified in the notice of proposed capital classification, holds core capital less than the minimum capital level; and

(ii) As of the date specified in the notice of proposed capital classification, holds core capital equaling or exceeding the critical capital level.

(4) *Critically undercapitalized.* An Enterprise will be classified as critically undercapitalized if, as of the date specified in the notice of proposed capital classification, the Enterprise holds core capital less than the critical capital level.

(5) *Discretionary reclassification—determination to reclassify.* If OFHEO determines in writing that an Enterprise is engaging in action or inaction (including a failure to respond appropriately to changes in circumstances or unforeseen events) that could result in a rapid depletion of core capital, or that the value of property subject to mort-

gages held or securitized by the Enterprise has decreased significantly, or that reclassification is otherwise deemed necessary to ensure that the Enterprise holds adequate capital and operates safely, OFHEO may reclassify the Enterprise as:

(i) Undercapitalized if the Enterprise is otherwise classified as adequately capitalized;

(ii) Significantly undercapitalized if the Enterprise is otherwise classified as undercapitalized; or

(iii) Critically undercapitalized if the Enterprise is otherwise classified as significantly undercapitalized.

(b) *Duration of reclassification; successive reclassifications.* (1) A reclassification of an Enterprise based on action, inaction, or conditions under paragraph (a)(5) or (c)(5) of this section shall be considered in the determination of each subsequent capital classification of the Enterprise, and shall only cease being considered in the determination of the Enterprise's capital classification after OFHEO determines that the action, inaction or condition upon which the reclassification was based has ceased or been eliminated and remedied to OFHEO's satisfaction.

(2) If the action, inaction, or condition upon which a reclassification was based under paragraph (a)(5) or (c)(5) of this section has not ceased or been eliminated and remedied to OFHEO's satisfaction within such reasonable time as is determined by OFHEO to be appropriate, OFHEO may consider such failure to be the basis for additional reclassification under such paragraph (a)(5) or (c)(5) of this section into a lower capital classification.

(c) *Capital classifications before the effective date of section 1365 of the 1992 Act.* Notwithstanding paragraph (a) of this section, until September 13, 2002, the capital classification of an Enterprise for purposes of subpart B of this part is as follows:

(1) *Adequately capitalized.* Except as otherwise provided in paragraph (c)(5) of this section, an Enterprise will be classified as adequately capitalized if the Enterprise, as of the date specified in the notice of proposed capital classification, holds core capital equaling or exceeding the minimum capital level.

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(2) *Undercapitalized.* An Enterprise will be classified as undercapitalized if the Enterprise:

(i) As of the date specified in the notice of proposed capital classification, holds core capital equaling or exceeding the minimum capital level; and

(ii) Is reclassified as undercapitalized by OFHEO under paragraph (c)(5) of this section.

(3) *Significantly undercapitalized.* Except as otherwise provided under paragraph (c)(5) of this section or § 1777.23(c) or § 1777.23(h), an Enterprise will be classified as significantly undercapitalized if the Enterprise:

(i) As of the date specified in the notice of proposed capital classification, held core capital less than the minimum capital level; and

(ii) As of the date specified in the notice of proposed capital classification, held core capital equaling or exceeding the critical capital level.

(4) *Critically undercapitalized.* An Enterprise will be classified as critically undercapitalized if, as of the date specified in the notice of proposed capital classification, the Enterprise held core capital less than the critical capital level.

(5) *Discretionary reclassification.* If OFHEO determines in writing that an Enterprise is engaging in action or inaction (including a failure to respond appropriately to changes in circumstances or unforeseen events) that could result a rapid depletion of core capital, or that the value of the property subject to mortgages held or securitized by the Enterprise has decreased significantly or that reclassification is deemed necessary to ensure that the Enterprise holds adequate capital and operates safely, OFHEO may reclassify the Enterprise as:

(i) Undercapitalized if the Enterprise is otherwise classified as adequately capitalized;

(ii) Significantly undercapitalized if the Enterprise is otherwise classified as undercapitalized; or

(iii) Critically undercapitalized if the Enterprise is otherwise classified as significantly undercapitalized.

(d) *Prior approvals.* In making a determination to reclassify an Enterprise under paragraph (a)(5) or (c)(5) of this section, OFHEO will not base its deci-

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sion to reclassify solely on action or inaction that previously was given specific approval by the Director of OFHEO in connection with the Director's approval of the Enterprise's capital restoration plan under section 1369C of the 1992 Act (12 U.S.C. 4622), or of a written agreement with the Enterprise that is enforceable in accordance with section 1371 of the 1992 Act.

§ 1777.21 Notice of capital category, and adjustments.

(a) *Notice of capital classification.* OFHEO will classify each Enterprise according to the capital classifications in § 1777.20(a) or § 1777.20(c) on at least a quarterly basis. OFHEO may classify an Enterprise according to the capital classifications in § 1777.20(a) or § 1777.20(c), or reclassify an Enterprise as set out in § 1777.20(a)(5), § 1777.20(c)(5), § 1777.23(c), or § 1777.23(h), at such other times as OFHEO deems appropriate.

(1) *Notice of proposed capital classification.* (i) Before OFHEO classifies or reclassifies an Enterprise, OFHEO will provide the Enterprise with written notice containing the proposed capital classification, the information upon which the proposed classification is based, and the reason for the proposed classification.

(ii) Notices proposing to classify or reclassify an Enterprise as undercapitalized or significantly undercapitalized may be combined with a notice that OFHEO may further reclassify the Enterprise under § 1777.23(c), without additional notice.

(iii) Notices proposing to classify or reclassify an Enterprise as significantly undercapitalized or critically undercapitalized may be combined with a notice under § 1777.24 that OFHEO intends to issue an order under section 1366 of the 1992 Act (12 U.S.C. 4616).

(iv) Notices proposing to classify an Enterprise as undercapitalized or significantly undercapitalized may be combined with a notice proposing to simultaneously reclassify the Enterprise under § 1777.20(a)(5) or § 1777.20(c)(5).

(2) *Response by the Enterprise.* The Enterprise may submit a response to OFHEO containing information for

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OFHEO's consideration in classifying or reclassifying the Enterprise.

(i) The Enterprise may, within thirty calendar days from receipt of a notice of proposed capital classification, submit a response to OFHEO, unless OFHEO determines the condition of the Enterprise requires a shorter period or the Enterprise consents to a shorter period.

(ii) The Enterprise's response period may be extended for up to an additional thirty calendar days if OFHEO determines there is good cause for such extension.

(iii) The Enterprise's failure to submit a response during the response period (as extended or shortened, if applicable) shall waive any right of the Enterprise to comment on or object to the proposed capital classification.

(3) *Classification determination and written notice of capital classification.* After the Enterprise has submitted its response under paragraph (a)(2) of this section or the response period (as extended or shortened, if applicable) has expired, whichever occurs first, OFHEO will make its determination of the Enterprise's capital classification, taking into consideration such relevant information as is provided by the Enterprise in its response, if any, under paragraph (a)(2) of this section. OFHEO will provide the Enterprise with a written notice of capital classification, which shall include a description of the basis for OFHEO's determination.

(4) *Timing.* OFHEO may, in its discretion, issue a notice of proposed capital classification to an Enterprise at any time. If a notice of proposed classification is pending (under the process set out in paragraphs (a)(1) through (3) of this section) at that time, OFHEO may, in its discretion, specify whether the subsequent notice of proposed capital classification supersedes the pending notice.

(b) *Developments warranting possible change to capital classification—(1) Notice to OFHEO.* An Enterprise shall promptly provide OFHEO with written notice of any material development that would result in the Enterprise's core or total capital to fall to a point causing the Enterprise to be placed in a lower capital classification than the capital classification assigned to the

Enterprise in its most recent notice of capital classification from OFHEO, or than is proposed to be assigned in the Enterprise's most recent notice of proposed capital classification from OFHEO. The Enterprise shall deliver such notice to OFHEO no later than ten calendar days after the Enterprise becomes aware of such development.

(2) OFHEO, in its discretion, will determine whether to issue a new notice of proposed capital classification under paragraph (a) of this section, based on OFHEO's review of the notice under paragraph (b)(1) of this section from the Enterprise and any other information deemed relevant by OFHEO.

§ 1777.22 Limitation on capital distributions.

(a) *Capital distributions in general.* An Enterprise shall make no capital distribution that would decrease the total capital of the Enterprise to an amount less than the risk-based capital level or the core capital of the Enterprise to an amount less than the minimum capital level without the prior written approval of OFHEO.

(b) *Capital distributions by an Enterprise that is not adequately capitalized—*

(1) *Prohibited distributions.* An Enterprise that is not classified as adequately capitalized shall make no capital distribution that would result in the Enterprise being classified into a lower capital classification than the one to which it is classified at the time of such distribution.

(2) *Restricted distributions.* An Enterprise classified as significantly or critically undercapitalized shall make no capital distribution without the prior written approval of OFHEO. OFHEO may grant a request for such a capital distribution only if OFHEO determines, in its discretion, that the distribution:

(i) Will enhance the ability of the Enterprise to meet the risk-based capital level and the minimum capital level promptly;

(ii) Will contribute to the long-term financial safety and soundness of the Enterprise; or

(iii) Is otherwise in the public interest.

§ 1777.23 Capital restoration plans.

(a) *Schedule for filing plans*—(1) *In general.* An Enterprise shall file a capital restoration plan in writing with OFHEO within ten days of receiving a notice of capital classification under § 1777.21(a)(3) stating that the Enterprise is classified as undercapitalized, significantly undercapitalized, or critically undercapitalized, unless OFHEO in its discretion determines an extension of the ten-day period is necessary and provides the Enterprise with written notice of the date the plan is due.

(2) *Successive capital classifications.* Notwithstanding paragraph (a)(1) of this section, an Enterprise that has already submitted and is operating under a capital restoration plan approved by OFHEO under this part is not required to submit an additional capital restoration plan based on a subsequent notice of capital classification, unless OFHEO notifies the Enterprise that it must submit a new or amended capital restoration plan. An Enterprise that receives such a notice to submit a new or amended capital restoration plan shall file in writing with OFHEO a complete plan that is responsive to the terms of and within the deadline specified in such notice.

(b) *Contents of capital restoration plan.* (1) The capital restoration plan submitted under paragraph (a)(1) or (2) of this section shall:

(i) Specify the level of capital the Enterprise will achieve and maintain;

(ii) Describe the actions that the Enterprise will take to become classified as adequately capitalized;

(iii) Establish a schedule for completing the actions set forth in the plan;

(iv) Specify the types and levels of activities (including existing and new programs) in which the Enterprise will engage during the term of the plan;

(v) Describe the actions that the Enterprise will take to comply with any mandatory or discretionary requirements to be imposed under Subtitle B of the 1992 Act (12 U.S.C. 4611 through 4623) or subpart B of this part;

(vi) To the extent the Enterprise is required to submit or revise a capital restoration plan as the result of a reclassification of the Enterprise under § 1777.20(a)(5) or § 1777.20(c)(5), describe

the steps the Enterprise will take to cease or eliminate and remedy the action, inaction, or conditions that caused the reclassification; and

(vii) Provide any other information or discuss any other issues as instructed by OFHEO.

(2) The plan shall include a declaration by the chief executive officer, treasurer, or other officer designated by the Board of Directors of the Enterprise to make such declaration, that the material contained in the plan is true and correct to the best of such officer's knowledge and belief.

(c) *Failure to submit*—(1) *Failure to submit; submission of unacceptable plan.* If, upon the expiration of the period provided in paragraph (a)(1) or (2) of this section for an Enterprise to submit a capital restoration plan, an Enterprise fails to comply with the requirement to file a complete capital restoration plan, or if the capital restoration plan is disapproved after review under paragraph (d) of this section, OFHEO may, in accordance with § 1777.21(a)(1)(ii) without additional notice, reclassify the Enterprise:

(i) As significantly undercapitalized if it is otherwise classified as undercapitalized; or

(ii) As critically undercapitalized if it is otherwise classified as significantly undercapitalized.

(2) *Duration of reclassification.* An Enterprise's failure to submit an approved capital restoration plan as described in paragraph (c)(1) of this section shall continue to be grounds for reclassification at each subsequent capital classification of the Enterprise, and shall only cease being considered grounds for reclassification after the Enterprise files a capital restoration plan that receives OFHEO's approval under paragraph (d) of this section.

(3) *Successive reclassifications.* If an Enterprise has not remedied its failure to file a complete capital restoration plan or an acceptable capital restoration plan within such period as is determined by OFHEO to be appropriate, OFHEO may consider such failure to be the basis for additional reclassification under paragraph (c)(1) of this section into a lower capital classification. Such reclassification may be made

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without additional notice in accordance with §1777.21(a)(1)(ii).

(d) *Order approving or disapproving plan.* Not later than thirty calendar days after receipt of the Enterprise's complete or amended capital restoration plan under this section (subject to extension upon written notice to the Enterprise for an additional thirty calendar days as OFHEO deems necessary), OFHEO shall issue an order to the Enterprise approving or disapproving the plan. An order disapproving a plan shall include the reasons therefore.

(e) *Resubmission.* An Enterprise that receives an order disapproving its capital restoration plan shall submit an amended capital plan acceptable to OFHEO within thirty calendar days of the date of such order, or a longer period if OFHEO determines an extension is in the public interest.

(f) *Amendment.* An Enterprise that has received an order approving its capital restoration plan may amend the capital restoration plan only after written notice to OFHEO and OFHEO's written approval of the modification. Pending OFHEO's review and approval of the amendment in OFHEO's discretion, the Enterprise shall continue to implement the capital restoration plan under the original approval order.

(g) *Termination—(1) Termination under the terms of the plan.* An Enterprise that has received an order approving its capital restoration plan remains bound by each of its obligations under the plan until each such obligation terminates under express terms of the plan itself identifying a date, event, or condition upon which such obligation shall terminate.

(2) *Termination orders.* To the extent the plan does not include such express terms for any obligation thereunder, the Enterprise's obligation continues until OFHEO issues an order terminating such obligation under the plan. The Enterprise may also submit a written request to OFHEO seeking termination of such obligations. OFHEO will approve termination of such obligation to the extent that OFHEO determines, in its discretion, that the obligation's purpose under the plan has been fulfilled and that termination of the obli-

gation is consistent with the overall safety and soundness of the Enterprise.

(h) *Implementation—(1) An Enterprise that has received an order approving its capital restoration plan is required to implement the plan.*

(i) If OFHEO determines, in its discretion, that an Enterprise has failed to make, in good faith, reasonable efforts necessary to comply with the capital restoration plan and fulfill the schedule thereunder, OFHEO may reclassify the Enterprise:

(A) As significantly undercapitalized if it is otherwise classified as undercapitalized; or

(B) As critically undercapitalized if it is otherwise classified as significantly undercapitalized.

(ii) *Duration of reclassification.* An Enterprise's failure to implement an approved capital restoration plan as described in paragraph (h)(1)(i) of this section shall continue to be grounds for reclassification at each subsequent capital classification of the Enterprise, and shall only cease being considered grounds for reclassification after OFHEO determines, in its discretion, that the Enterprise is making such efforts as are reasonably necessary to comply with the capital restoration plan and fulfill the schedule thereunder.

(iii) *Successive reclassifications.* If an Enterprise has not remedied its failure to implement an approved capital restoration plan within such period as is determined by OFHEO to be appropriate, OFHEO may consider such failure to be the basis for additional reclassification under paragraph (h)(1)(i) of this section into a lower capital classification.

(2) *Administrative enforcement action.* A capital plan that has received an approval order from OFHEO under this section shall constitute an order under the 1992 Act. An Enterprise, regardless of its capital classification, as well as its executive officers, and directors may be subject to action by OFHEO under sections 1371, 1372, and 1376 of the 1992 Act (12 U.S.C. 4631, 4632, and 4636) and 12 CFR part 1780 for failure to comply with such plan.

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§ 1777.24 Notice of intent to issue an order.

(a) *Orders under section 1366 of the 1992 Act (12 U.S.C. 4616)*. In addition to any other action taken under this part, part 1780 of this chapter, or any other applicable authority, OFHEO may, in its discretion, issue an order to an Enterprise that is classified as significantly undercapitalized or critically undercapitalized, or is in conservatorship, directing the Enterprise to take one or more of the following actions:

(1) Limit any increase in, or reduce, any obligations of the Enterprise, including off-balance sheet obligations;

(2) Limit or eliminate growth of the Enterprise's assets or reduce the amount of the Enterprise's assets;

(3) Acquire new capital, in such form and amount as determined by OFHEO; or

(4) Terminate, reduce, or modify any activity of the Enterprise that OFHEO determines creates excessive risk to the Enterprise.

(b) *Notice of intent to issue an order*. Before OFHEO issues an order to an Enterprise pursuant to section 1366 of the 1992 Act (12 U.S.C. 4616), OFHEO will provide the Enterprise with written notice containing the proposed order.

(c) *Contents of notice*. A notice of intent to issue an order under this subpart shall include:

(1) A statement of the Enterprise's capital classification and its minimum capital level or critical capital level, and its risk-based capital level;

(2) A description of the restrictions, prohibitions, or affirmative actions that OFHEO proposes to impose or require; and

(3) The proposed date when such restrictions or prohibitions would become effective or the proposed date for the commencement and/or completion of the affirmative actions.

§ 1777.25 Response to notice.

(a) *Content of response*. The Enterprise may submit a response to OFHEO containing information for OFHEO's consideration in connection with the proposed order. The response should include, but is in no way limited to, the following:

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(1) Any relevant information, mitigating circumstances, documentation, or other information the Enterprise wishes OFHEO to consider in support of the Enterprise's position regarding the proposed order; and

(2) Any recommended modification to the proposed order, and justification thereof.

(b) *Time to respond*. The Enterprise may, within thirty calendar days after receipt of the notice of proposed order, submit a response to OFHEO, unless OFHEO determines a shorter period to be appropriate or the Enterprise consents to a shorter period. OFHEO may extend the Enterprise's response period for up to an additional thirty calendar days if OFHEO determines, in its discretion, that there is good cause for such extension.

(c) *Waiver and consent*. The Enterprise's failure to submit a response during the response period (as extended or shortened, if applicable) shall waive any right of the Enterprise to comment on or object to the proposed order.

§ 1777.26 Final notice of order.

(a) *Determination and notice*. After the Enterprise has submitted its response under § 1777.25 or the response period (as extended or shortened, if applicable) has expired, whichever occurs first, OFHEO will determine, in its discretion, whether to take into consideration such relevant information as is provided by the Enterprise in its response, if any, under § 1777.25. OFHEO will provide the Enterprise with a written final notice of any order issued by OFHEO under this subpart, which is to include a description of the basis for OFHEO's determination.

(b) *Termination or modification*. An Enterprise that has received an order under paragraph (a) of this section remains subject to each provision of the order until each such provision terminates under the express terms of the order. The Enterprise may submit a written request to OFHEO seeking modification or termination of one or more provisions of the order. Pending OFHEO's review and approval, in OFHEO's discretion of the Enterprise's request, the Enterprise shall remain subject to the provisions of the order.

(c) *Enforcement of order*—(1) *Judicial enforcement*. An order issued under paragraph (a) of this section is an order for purposes of section 1375 of the 1992 Act (12 U.S.C. 4635). An Enterprise in any capital classification may be subject to enforcement of such order in the United States District Court for the District of Columbia pursuant to such section.

(2) *Administrative enforcement*. An order issued under paragraph (a) of this section constitutes an order under the 1992 Act. An Enterprise, regardless of its capital classification, as well as its executive officers and directors may be subject to action by OFHEO under sections 1371, 1372, and 1376 of the 1992 Act (12 U.S.C. 4631, 4632, and 4636) and 12 CFR part 1780 for failure to comply with such order.

§ 1777.27 Exhaustion and review.

(a) *Judicial review*—(1) *Review of certain actions*. An Enterprise that is not classified as critically undercapitalized may seek judicial review of a final notice of capital classification issued pursuant to §1777.21(a)(3) or a final notice of order issued pursuant to §1777.26(a) in accordance with section 1369D of the 1992 Act (12 U.S.C. 4623)

(2) *Other review barred*. Except as set out in paragraph (a)(1) of this section, or review of conservatorship appointments to the limited extent provided in section 1369(b) of the 1992 Act (12 U.S.C. 4619(b)) and §1777.28(c), no court shall have jurisdiction to affect, by injunction or otherwise, the issuance or effectiveness of a capital classification or any other action of OFHEO pursuant to this subpart B, as provided in section 1369D of the 1992 Act (12 U.S.C. 4623).

(b) *Exhaustion of administrative remedies*. In connection with any issue for which an Enterprise seeks judicial review in connection with an action described in paragraph (a)(1) of this section, the Enterprise must have first exhausted its administrative remedies, by presenting all its objections, arguments, and information relating to such issue for OFHEO's consideration pursuant to §1777.21(a)(2), as part of the Enterprise's response to OFHEO's notice of capital classification, or pursuant to §1777.25, as part of the Enter-

prise's response to OFHEO's notice of intent to issue an order.

(c) *No stay pending review*. The commencement of proceedings for judicial review of a final capital classification or order as described in paragraph (a)(1) of this section shall not operate as a stay thereof.

§ 1777.28 Appointment of conservator for a significantly undercapitalized or critically undercapitalized Enterprise.

(a) *Significantly undercapitalized Enterprise*. At any time after an Enterprise is classified as significantly undercapitalized, OFHEO may issue an order appointing a conservator for the Enterprise upon determining that:

(1) The amount of core capital of the Enterprise is less than the minimum capital level; and

(2) The alternative remedies available to OFHEO under the 1992 Act are not satisfactory.

(b) *Critically undercapitalized Enterprise*—(1) *Appointment upon classification*. Not later than thirty days after issuing a final notice of capital classification pursuant to §1777.21(a)(3) classifying an Enterprise as significantly undercapitalized, OFHEO shall issue an order appointing a conservator for the Enterprise.

(2) *Exception*. Notwithstanding paragraph (b)(1) of this section, OFHEO may determine not to appoint a conservator if OFHEO makes a written finding, with the written concurrence of the Secretary of the Treasury, that:

(i) The appointment of a conservator would have serious adverse effects on economic conditions of national financial markets or on the financial stability of the housing finance market; and

(ii) The public interest would be better served by taking some other enforcement action authorized under this title.

(c) *Judicial review*. An Enterprise for which a conservator has been appointed pursuant to paragraph (a) or (b) of this section may seek judicial review of the appointment in accordance with section 1369(b) of the 1992 Act (12 U.S.C. 4619(b)). Except as provided therein, no court may take any action regarding the removal of a conservator

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or otherwise restrain or affect the exercise of the powers or functions of a conservator.

(d) *Termination*—(1) *Upon reaching the minimum capital level.* OFHEO will issue an order terminating a conservatorship appointment under paragraph (a) or (b) of this section upon a determination that the Enterprise has maintained an

amount of core capital that is equal to or exceeds the minimum capital level.

(2) *In OFHEO's discretion.* OFHEO may, in its discretion, issue an order terminating a conservatorship appointment under paragraph (a) or (b) of this section upon a determination that such termination order is in the public interest and may safely be accomplished.

SUBCHAPTER D—RULES OF PRACTICE AND PROCEDURE

PART 1780—RULES OF PRACTICE AND PROCEDURE

Subpart A—General Rules

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AUTHORITY: 12 U.S.C. 4501, 4513(b), 4517, 4521, 4631–4641.

SOURCE: 62 FR 68154, Dec. 31, 1997, unless otherwise noted.

Subpart A—General Rules

SOURCE: 64 FR 72510, Dec. 28, 1999, unless otherwise noted.

§ 1780.1 Scope.

(a) *Types of proceedings governed by these rules.* This part prescribes rules of practice and procedure applicable to the following adjudicatory proceedings:

(1) Cease-and-desist proceedings under sections 1371 and 1373, title XIII of the Housing and Community Development Act of 1992, Pub. L. No. 102–550, entitled The Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (1992 Act) (12 U.S.C. 4631 and 4633);

(2) Civil money penalty assessment proceedings under sections 1373 and 1376 of the 1992 Act (12 U.S.C. 4633 and 4636);

(3) Civil money penalty assessment proceedings under section 102 of the Flood Disaster Protection Act of 1973, as amended, 42 U.S.C. 4012a; and

(4) Other adjudications required by statute to be determined on the record after opportunity for hearing, except to the extent otherwise provided for in the regulations specifically governing such an adjudication.

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(b) *Cease and desist orders.* (1) Grounds for instituting proceedings. Sections 1371(a) and (b) of the 1992 Act specify when the Director of OFHEO may issue a notice of charges instituting cease and desist proceedings, to be conducted according to the procedural rules in this part. The Director may issue a notice of charges as described in §1780.20 if the Director determines, or the Director has reasonable cause to believe that, an Enterprise or an executive officer or director thereof has engaged in, or it is about to engage in, any of the following conduct or violations:

(i) For an adequately capitalized Enterprise, any conduct which threatens to cause a significant depletion of the Enterprise's core capital; or for an Enterprise which is not in the adequately capitalized category, any conduct that is likely to result in a material depletion of the Enterprise's core capital;

(ii) Any conduct that may result in the issuance of a cease and desist order that requires an executive officer or director of an Enterprise to make restitution, provide reimbursement, indemnification or guarantee against loss to the Enterprise, where such person was either unjustly enriched or engaged in knowing misconduct likely to cause substantial loss to the Enterprise;

(iii) Any conduct that violates a written agreement entered into by an Enterprise with the Director; or

(iv) Any conduct that violates the 1992 Act, the Federal National Mortgage Association Charter Act (12 U.S.C. 1716 *et seq.*), the Federal Home Loan Mortgage Corporation Act (12 U.S.C. 1451 *et seq.*), or any regulation, rule, or order under such Acts, or any unsafe and unsound practice (in that it is contrary to prudent standards of operation which might cause loss or damage to the Enterprise, or is likely to cause such loss or damage if continued unabated), or any unsafe and unsound condition, except that the Director may not enforce compliance with housing goals established under subpart B of part 2 of subtitle A of the 1992 Act (12 U.S.C. 4561 through 4567), with section 1336 or 1337 of the 1992 Act (12 U.S.C. 4566 or 4567), or with subsection (m) or (n) of section 309 of the Federal National Mortgage Association Charter

Act (12 U.S.C. 4566 or 4567), or subsection (e) or (f) of section 307 of the Federal Home Loan Mortgage Corporation Act (12 U.S.C. 1456(e) or (f)).

(2) *Remedial provisions of cease and desist orders.* As provided by sections 1371(c) and (d) of the 1992 Act, a cease and desist order issued as set out in §1780.55 may require the Enterprise, or an executive officer or director thereof, to refrain from engaging in conduct or violations specified in paragraphs (b)(1)(i) through (iv) of this section and/or require correction of an unsafe or unsound condition specified in paragraph (b)(1)(iv) of this section, as found by the Director, and may also require the Enterprise, an executive officer, or director thereof to take such action as the Director determines to be appropriate to correct or remedy the conditions resulting from such conduct or violation. This may include, but is not limited to, provisions to:

(i) Require the Enterprise to seek restitution, or to obtain reimbursement, indemnification, or guarantee against loss;

(ii) Require the Enterprise to obtain new capital;

(iii) Restrict asset or liability growth of the Enterprise;

(iv) Require the Enterprise to dispose of any asset involved;

(v) Require the Enterprise to improve design or implementation of internal policies, compliance efforts, internal controls, risk measurement and limits, and management reporting systems;

(vi) Require the Enterprise to employ qualified officers or employees (who may be subject to approval by the Director at the direction of the Director);

(vii) Require the Enterprise, an executive officer or director thereof to adhere to limits on activities or functions; or

(viii) Require the Enterprise to take such other action as the Director determines appropriate.

(3) *Restitution and indemnification by executive officers and directors.* As part of the affirmative relief described in paragraph (b)(2) of this section, section 1371(d)(1) of the 1992 Act provides that the Director may require an executive officer or director of an Enterprise to make restitution or reimbursement to

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the Enterprise, or to provide indemnification or guarantee against loss, to the extent such person was:

(i) Unjustly enriched in connection with the conduct or violation in question; or

(ii) Engaged in such conduct or violation knowingly, and such conduct or violation caused or would be likely to cause a substantial loss to the Enterprise.

(4) *Temporary cease and desist orders.*

(i) Under sections 1372(a) and (b) of the 1992 Act, if the Director determines that any conduct or violation or threatened conduct or violation described in the notice of charges in cease and desist proceedings described under §1780.20 is likely to cause insolvency, to cause significant depletion of core capital, or to cause other irreparable harm to an Enterprise before proceedings described in this part will be completed, the Director may issue a temporary cease and desist order. Such order may direct the Enterprise, executive officer or director thereof to refrain from the conduct or violation, and to take whatever affirmative action the Director determines to be appropriate to prevent or remedy such insolvency, depletion, or harm pending completion of such cease and desist proceedings.

(ii) In addition, section 1372(c) of the 1992 Act addresses cases in which the Director determines that the books and records of an Enterprise are so incomplete or inaccurate that the Director is unable through normal supervisory processes to determine either the financial condition of the Enterprise or the details or purpose of transactions that may have a material effect on the financial condition of the Enterprise. In connection with issuance of the notice of charges in cease and desist proceedings specified by §1780.20, the Director may issue a temporary order directing the Enterprise to cease the activity or practice that gave rise, whether in whole or in part, to the incomplete or inaccurate state of the records, and may require the Enterprise to take affirmative action to make the records complete and accurate.

(c) *Civil money penalties*—(1) *First tier CMPs.* Section 1736 of the 1992 Act au-

thorizes the Director to assess civil money penalties against an Enterprise, in proceedings to be conducted according to the procedural rules in this part. The Director may issue a notice of charges to an Enterprise, as described in §1780.20, to impose money penalties of up to \$5,000 (adjusted for inflation as described in §1780.80) for each day that the Enterprise engages in conduct that violates:

(i) The 1992 Act, the Federal National Mortgage Association Charter Act, the Federal Home Loan Mortgage Corporation Act, or any regulation, rule, or order under such Acts, except with regard to housing goals established under subpart B of part 2 of subtitle A of the 1992 Act, with section 1336 or 1337 of the 1992 Act, or with subsection (m) or (n) of section 309 of the Federal National Mortgage Association Charter Act, or subsection (e) or (f) of section 307 of the Federal Home Loan Mortgage Corporation Act;

(ii) Any written agreement entered into by the Enterprise with the Director; or

(iii) Any permanent or temporary cease and desist order entered under sections 1371 or 1372 of the 1992 Act, or sections 1365 (12 U.S.C. 4615, setting out supervisory actions applicable to undercapitalized Enterprises) or 1366 (12 U.S.C. 4616, setting out supervisory actions applicable to significantly undercapitalized institutions) of the 1992 Act.

(2) *Second tier CMPs.* The Director may issue a notice of charges to an Enterprise to impose money penalties of up to \$25,000 (adjusted for inflation as described in §1780.80) for each day that the Enterprise engages in the following violation or conduct, or to an executive officer or director of an Enterprise to impose money penalties of up to \$10,000 (adjusted for inflation as described in §1780.80) for each day such person or persons engages in the following violation or conduct, if the Director finds that the violation or conduct was either part of a pattern of misconduct or involved recklessness and causes or is likely to cause a material loss to the Enterprise:

(i) Any violation described in paragraphs (c)(1)(i) through (iii) of this section; or

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(ii) Any conduct that causes or is likely to cause a loss to the Enterprise.

(3) *Third tier CMPs.* The Director may issue a notice of charges to an Enterprise to impose money penalties of up to \$1,000,000 (adjusted for inflation as described in §1780.80) for each day that the Enterprise engages in a violation or conduct described in paragraphs (c)(2)(i) and (ii) of this section, or to an executive officer or director of an Enterprise to impose money penalties of up to \$100,000 (adjusted for inflation as described in §1780.80) for each day such person or persons engages in such violation or conduct described in paragraphs (c)(2)(i) and (ii) of this section, if the Director finds that the violation or conduct was knowing and caused or is likely to cause a substantial loss to the Enterprise.

(4) *Amount of CMPs.* In determining the amount of a civil money penalty within the range of penalties described in paragraphs (c)(1) through (3) of this section, the Director may fashion sanctions in any such amount as deemed to be appropriate taking into consideration such factors as:

- (i) The gravity of the violation or conduct;
- (ii) Any loss or risk of loss to the Enterprise;
- (iii) Any benefits received;
- (iv) Any attempts at concealment;
- (v) Any history of prior violations or conduct;
- (vi) Any related or unrelated previous supervisory actions;
- (vii) Any injury to the public;
- (viii) Deterrence of future violations or conduct;
- (ix) The effect of the penalty on the safety and soundness of the Enterprise;
- (x) Any circumstances of hardship upon an executive officer or director;
- (xi) Promptness and effectiveness of any efforts to ameliorate the consequences of the violations or conduct; and
- (xii) Candor and cooperation after the fact.

(d) *Coordination with other supervisory actions.* In addition to cease and desist and/or civil money penalty proceedings under this part, the 1992 Act grants the Director other authority to take supervisory action, including requiring mandatory and discretionary supervisory

actions against an Enterprise that fails to remain adequately capitalized; appointment of a conservator for an Enterprise; entering into a written agreement the violation of which is actionable through proceedings under this part, or any other formal or informal agreement with an Enterprise as may be deemed by the Director to be appropriate. Under the 1992 Act, the selection of the form of supervisory action is within the Director's discretion, and the selection of one form of action or a combination of actions does not foreclose the Director from pursuing any other supervisory action.

(e) *Proceedings against affiliates.* Under subtitle C of the 1992 Act, the Director may institute proceedings as described under this part against an affiliate of an Enterprise as well as an executive officer or director of such affiliate. An entity is affiliated with an Enterprise if the entity controls the Enterprise, is controlled by the Enterprise, or is under common control with the Enterprise. For purposes of this part, control means the ability to exercise a controlling influence over the management and policies of the entity or Enterprise, whether it be by ownership of or the power to vote a concentration of any class of voting securities, the ability to elect or appoint members of the board of directors or officers of the entity, or otherwise.

(f) *Public nature of proceedings.* As described in §1780.6 of this part, all hearings shall be open to the public unless the Director in his discretion determines to the contrary based on public interest. The Director shall also make final orders available to the public, as well as modifications to or terminations thereof, except that the Director may determine in writing to delay public disclosure of such final orders for a reasonable time if immediate disclosure would seriously threaten the financial health or security of the Enterprise.

[66 FR 18043, Apr. 5, 2001]

§ 1780.2 Rules of construction.

For purposes of this part—

- (a) Any term in the singular includes the plural and the plural includes the singular, if such use would be appropriate;

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(b) Any use of a masculine, feminine, or neuter gender encompasses all three, if such use would be appropriate; and

(c) Unless the context requires otherwise, a party's representative of record, if any, may, on behalf of that party, take any action required to be taken by the party.

§ 1780.3 Definitions.

For purposes of this part, unless explicitly stated to the contrary—

(a) *Adjudicatory proceeding* means a proceeding conducted pursuant to these rules and leading to the formulation of a final order other than a regulation;

(b) *Decisional employee* means any member of the Director's or the presiding officer's staff who has not engaged in an investigative or prosecutorial role in a proceeding and who may assist the Director or the presiding officer, respectively, in preparing orders, recommended decisions, decisions and other documents under this subpart.

(c) *Director* means the Director of OFHEO.

(d) *Enterprise* means the Federal National Mortgage Association and any affiliate thereof and the Federal Home Loan Mortgage Corporation and any affiliate thereof.

(e) *OFHEO* means the Office of Federal Housing Enterprise Oversight of the Department of Housing and Urban Development.

(f) *Party* means OFHEO and any person named as a party in any notice.

(g) *Person* means an individual, sole proprietor, partnership, corporation, unincorporated association, trust, joint venture, pool, syndicate, agency, or other entity or organization.

(h) *Presiding officer* means an administrative law judge or any other person appointed by the Director under applicable law to conduct a hearing.

(i) *Representative of record* means an individual who is authorized to represent a person or is representing himself and who has filed a notice of appearance in accordance with §1780.72.

(j) *Respondent* means any party other than OFHEO.

(k) *Violation* includes any action (alone or with another or others) for or toward causing, bringing about, par-

ticipating in, counseling, or aiding or abetting a violation.

(1) The *1992 Act* is title XIII of the Housing and Community Development Act of 1992, Pub. L. No. 102-550, known as the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (1992 Act) (12 U.S.C. 4501-4641).

§ 1780.4 Authority of the Director.

The Director may, at any time during the pendency of a proceeding, perform, direct the performance of, or waive performance of any act that could be done or ordered by the presiding officer.

§ 1780.5 Authority of the presiding officer.

(a) *General rule.* All proceedings governed by this subpart shall be conducted in accordance with the provisions of 5 U.S.C. chapter 5. The presiding officer shall have complete charge of the hearing, conduct a fair and impartial hearing, avoid unnecessary delay and assure that a record of the proceeding is made.

(b) *Powers.* The presiding officer shall have all powers necessary to conduct the proceeding in accordance with paragraph (a) of this section and 5 U.S.C. 556(c). The presiding officer is authorized to—

(1) Set and change the date, time and place of the hearing upon reasonable notice to the parties;

(2) Continue or recess the hearing in whole or in part for a reasonable period of time;

(3) Hold conferences to identify or simplify the issues, or to consider other matters that may aid in the expeditious disposition of the proceeding;

(4) Administer oaths and affirmations;

(5) Issue subpoenas, subpoenas *duces tecum*, and protective orders, as authorized by this part, and to revoke, quash, or modify such subpoenas;

(6) Take and preserve testimony under oath;

(7) Rule on motions and other procedural matters appropriate in an adjudicatory proceeding, except that only the Director shall have the power to grant any motion to dismiss the proceeding or make a final determination of the merits of the proceeding;

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(8) Regulate the scope and timing of discovery;

(9) Regulate the course of the hearing and the conduct of representatives and parties;

(10) Examine witnesses;

(11) Receive, exclude, limit, or otherwise rule on evidence;

(12) Upon motion of a party, take official notice of facts;

(13) Recuse himself upon motion made by a party or on his own motion;

(14) Prepare and present to the Director a recommended decision as provided in this part;

(15) To establish time, place and manner limitations on the attendance of the public and the media for any public hearing; and

(16) Do all other things necessary and appropriate to discharge the duties of a presiding officer.

§ 1780.6 Public hearings.

(a) *General rule.* All hearings shall be open to the public, unless the Director, in his discretion, determines that holding an open hearing would be contrary to the public interest. The Director may make such determination *sua sponte* at any time by written notice to all parties.

(b) *Motion for closed hearing.* Within 20 days of service of the notice of charges, any party may file with the presiding officer a motion for a private hearing and any party may file a pleading in reply to the motion. The presiding officer shall forward the motion and any reply, together with a recommended decision on the motion, to the Director, who shall make a final determination. Such motions and replies are governed by §1780.25.

(c) *Filing documents under seal.* OFHEO's counsel of record, in his discretion, may file any document or part of a document under seal if such counsel makes a written determination that disclosure of the document would be contrary to the public interest. The presiding officer shall take all appropriate steps to preserve the confidentiality of such documents or parts thereof, including closing portions of the hearing to the public.

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§ 1780.7 Good faith certification.

(a) *General requirement.* Every filing or submission of record following the issuance of a notice by the Director shall be signed by at least one representative of record in his individual name and shall state that representative's address and telephone number and the names, addresses and telephone numbers of all other representatives of record for the person making the filing or submission.

(b) *Effect of signature.* (1) By signing a document, the representative of record or party certifies that—

(i) The representative of record or party has read the filing or submission of record;

(ii) To the best of his knowledge, information and belief formed after reasonable inquiry, the filing or submission of record is well-grounded in fact and is warranted by existing law or a good faith, nonfrivolous argument for the extension, modification, or reversal of existing law; and

(iii) The filing or submission of record is not made for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation.

(2) If a filing or submission of record is not signed, the presiding officer shall strike the filing or submission of record, unless it is signed promptly after the omission is called to the attention of the pleader or movant.

(c) *Effect of making oral motion or argument.* The act of making any oral motion or oral argument by any representative or party shall constitute a certification that to the best of his knowledge, information, and belief, formed after reasonable inquiry, his statements are well-grounded in fact and are warranted by existing law or a good faith, nonfrivolous argument for the extension, modification, or reversal of existing law and are not made for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation.

§ 1780.8 Ex parte communications.

(a) *Definition.* (1) Ex parte communication means any material oral or written communication relevant to the merits of an adjudicatory proceeding

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that was neither on the record nor on reasonable prior notice to all parties that takes place between—

(i) An interested person outside OFHEO (including the person's representative); and

(ii) The presiding officer handling that proceeding, the Director, a decisional employee assigned to that proceeding, or any other person who is or may reasonably be expected to be involved in the decisional process.

(2) A communication that does not concern the merits of an adjudicatory proceeding, such as a request for status of the proceeding, does not constitute an ex parte communication.

(b) *Prohibition of ex parte communications.* From the time the notice commencing the proceeding is issued by the Director until the date that the Director issues his final decision pursuant to §1780.55, no person referred to in paragraph (a)(1)(i) of this section shall knowingly make or cause to be made an ex parte communication. The Director, presiding officer, or a decisional employee shall not knowingly make or cause to be made an ex parte communication.

(c) *Procedure upon occurrence of ex parte communication.* If an ex parte communication is received by any person identified in paragraph (a) of this section, that person shall cause all such written communications (or, if the communication is oral, a memorandum stating the substance of the communication) to be placed on the record of the proceeding and served on all parties. All parties to the proceeding shall have an opportunity, within ten days of receipt of service of the ex parte communication, to file responses thereto and to recommend any sanctions, in accordance with paragraph (d) of this section, that they believe to be appropriate under the circumstances.

(d) *Sanctions.* Any party or representative for a party who makes an ex parte communication, or who encourages or solicits another to make any such communication, may be subject to any appropriate sanction or sanctions imposed by the Director or the presiding officer, including, but not limited to, exclusion from the proceedings and an adverse ruling on the

issue that is the subject of the prohibited communication.

(e) *Consultations by presiding officer.* Except to the extent required for the disposition of ex parte matters as authorized by law, the presiding officer may not consult a person or party on any matter relevant to the merits of the adjudication, unless on notice and opportunity for all parties to participate.

(f) *Separation of functions.* An employee or agent engaged in the performance of investigative or prosecuting functions for OFHEO in a case may not, in that or a factually related case, participate or advise in the decision, recommended decision, or Director review under §1780.55 of the recommended decision, except as witness or counsel in public proceedings.

§ 1780.9 Filing of papers.

(a) *Filing.* Any papers required to be filed shall be addressed to the presiding officer and filed with OFHEO, 1700 G Street, NW., Fourth Floor, Washington, DC 20552.

(b) *Manner of filing.* Unless otherwise specified by the Director or the presiding officer, filing shall be accomplished by:

(1) Personal service;

(2) Delivery to the U.S. Postal Service or to a reliable commercial delivery service for same day or overnight delivery;

(3) Mailing by first class, registered, or certified mail; or

(4) Transmission by electronic media, only if expressly authorized by and upon any conditions specified by the Director or the presiding officer. All papers filed by electronic media shall also concurrently be filed in accordance with paragraph (c) of this section.

(c) *Formal requirements as to papers filed—*(1) *Form.* All papers must set forth the name, address and telephone number of the representative or party making the filing and must be accompanied by a certification setting forth when and how service has been made on all other parties. All papers filed must be double-spaced and printed or typewritten on 8½×11-inch paper and must be clear and legible.

(2) *Signature.* All papers must be dated and signed as provided in §1780.7.

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(3) *Caption.* All papers filed must include at the head thereof, or on a title page, the name of OFHEO and of the filing party, the title and docket number of the proceeding and the subject of the particular paper.

(4) *Number of copies.* Unless otherwise specified by the Director or the presiding officer, an original and one copy of all documents and papers shall be filed, except that only one copy of transcripts of testimony and exhibits shall be filed.

§ 1780.10 Service of papers.

(a) *By the parties.* Except as otherwise provided, a party filing papers or serving a subpoena shall serve a copy upon the representative of record for each party to the proceeding so represented and upon any party not so represented.

(b) *Method of service.* Except as provided in paragraphs (c)(2) and (d) of this section, a serving party shall use one or more of the following methods of service:

(1) Personal service;

(2) Delivery to the U.S. Postal Service or to a reliable commercial delivery service for same day or overnight delivery;

(3) Mailing by first class, registered, or certified mail; or

(4) Transmission by electronic media, only if the parties mutually agree. Any papers served by electronic media shall also concurrently be served in accordance with the requirements of §1780.9(c).

(c) *By the Director or the presiding officer.* (1) All papers required to be served by the Director or the presiding officer upon a party who has appeared in the proceeding in accordance with §1780.72 shall be served by any means specified in paragraph (b) of this section.

(2) If a notice of appearance has not been filed in the proceeding for a party in accordance with §1780.72, the Director or the presiding officer shall make service upon the party by any of the following methods:

(i) By personal service;

(ii) If the person to be served is an individual, by delivery to a person of suitable age and discretion at the physical location where the individual resides or works;

(iii) If the person to be served is a corporation or other association, by delivery to an officer, managing or general agent, or to any other agent authorized by appointment or by law to receive service and, if the agent is one authorized by statute to receive service and the statute so requires, by also mailing a copy to the party;

(iv) By registered or certified mail addressed to the person's last known address; or

(v) By any other method reasonably calculated to give actual notice.

(d) *Subpoenas.* Service of a subpoena may be made:

(1) By personal service;

(2) If the person to be served is an individual, by delivery to a person of suitable age and discretion at the physical location where the individual resides or works;

(3) If the person to be served is a corporation or other association, by delivery to an officer, managing or general agent, or to any other agent authorized by appointment or by law to receive service and, if the agent is one authorized by statute to receive service and the statute so requires, by also mailing a copy to the party; or

(4) By registered or certified mail addressed to the person's last known address; or

(5) By any other method reasonably calculated to give actual notice.

(e) *Area of service.* Service in any State, commonwealth, possession, territory of the United States or the District of Columbia on any person doing business in any State, commonwealth, possession, territory of the United States or the District of Columbia, or on any person as otherwise permitted by law, is effective without regard to the place where the hearing is held.

(f) *Proof of service.* Proof of service of papers filed by a party shall be filed before action is taken thereon. The proof of service, which shall serve as *prima facie* evidence of the fact and date of service, shall show the date and manner of service and may be by written acknowledgment of service, by declaration of the person making service, or by certificate of a representative of record. However, failure to file proof of service contemporaneously with the papers shall not affect the validity of

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actual service. The presiding officer may allow the proof to be amended or supplied, unless to do so would result in material prejudice to a party.

§ 1780.11 Computing time.

(a) *General rule.* In computing any period of time prescribed or allowed by this subpart, the date of the act or event that commences the designated period of time is not included. The last day so computed is included unless it is a Saturday, Sunday, or Federal holiday. When the last day is a Saturday, Sunday or Federal holiday, the period shall run until the end of the next day that is not a Saturday, Sunday, or Federal holiday. Intermediate Saturdays, Sundays and Federal holidays are included in the computation of time. However, when the time period within which an act is to be performed is 10 days or less, not including any additional time allowed for in paragraph (c) of this section, intermediate Saturdays, Sundays and Federal holidays are not included.

(b) *When papers are deemed to be filed or served.* (1) Filing and service are deemed to be effective—

(i) In the case of personal service or same day reliable commercial delivery service, upon actual service;

(ii) In the case of U.S. Postal Service or reliable commercial overnight delivery service, or first class, registered, or certified mail, upon deposit in or delivery to an appropriate point of collection; or

(iii) In the case of transmission by electronic media, as specified by the authority receiving the filing in the case of filing, and as agreed among the parties in the case of service.

(2) The effective filing and service dates specified in paragraph (b)(1) of this section may be modified by the Director or the presiding officer in the case of filing or by agreement of the parties in the case of service.

(c) *Calculation of time for service and filing of responsive papers.* Whenever a time limit is measured by a prescribed period from the service of any notice or paper, the applicable time limits shall be calculated as follows:

(1) If service was made by first class, registered, or certified mail, or by delivery to the U.S. Postal Service for

longer than overnight delivery service, add three calendar days to the prescribed period for the responsive filing.

(2) If service was made by U.S. Postal Service or reliable commercial overnight delivery service, add 1 calendar day to the prescribed period for the responsive filing.

(3) If service was made by electronic media transmission, add one calendar day to the prescribed period for the responsive filing, unless otherwise determined by the Director or the presiding officer in the case of filing, or by agreement among the parties in the case of service.

§ 1780.12 Change of time limits.

Except as otherwise provided by law, the presiding officer may, for good cause shown, extend the time limits prescribed above or prescribed by any notice or order issued in the proceedings. After the referral of the case to the Director pursuant to §1780.53, the Director may grant extensions of the time limits for good cause shown. Extensions may be granted on the motion of a party after notice and opportunity to respond is afforded all non-moving parties, or on the Director's or the presiding officer's own motion.

§ 1780.13 Witness fees and expenses.

Witnesses (other than parties) subpoenaed for testimony or depositions shall be paid the same fees for attendance and mileage as are paid in the United States district courts in proceedings in which the United States is a party, provided that, in the case of a discovery subpoena addressed to a party, no witness fees or mileage shall be paid. Fees for witnesses shall be tendered in advance by the party requesting the subpoena, except that fees and mileage need not be tendered in advance where OFHEO is the party requesting the subpoena. OFHEO shall not be required to pay any fees to or expenses of any witness not subpoenaed by OFHEO.

§ 1780.14 Opportunity for informal settlement.

Any respondent may, at any time in the proceeding, unilaterally submit to OFHEO's counsel of record written offers or proposals for settlement of a

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proceeding without prejudice to the rights of any of the parties. No such offer or proposal shall be made to any OFHEO representative other than OFHEO's counsel of record. Submission of a written settlement offer does not provide a basis for adjourning or otherwise delaying all or any portion of a proceeding under this part. No settlement offer or proposal, or any subsequent negotiation or resolution, is admissible as evidence in any proceeding.

§ 1780.15 OFHEO's right to conduct examination.

Nothing contained in this part limits in any manner the right of OFHEO to conduct any examination, inspection, or visitation of any Enterprise or affiliate, or the right of OFHEO to conduct or continue any form of investigation authorized by law.

§ 1780.16 Collateral attacks on adjudicatory proceeding.

If an interlocutory appeal or collateral attack is brought in any court concerning all or any part of an adjudicatory proceeding, the challenged adjudicatory proceeding shall continue without regard to the pendency of that court proceeding. No default or other failure to act as directed in the adjudicatory proceeding within the times prescribed in this subpart shall be excused based on the pendency before any court of any interlocutory appeal or collateral attack.

Subpart B—Prehearing Proceedings

SOURCE: 64 FR 72513, Dec. 28, 1999, unless otherwise noted.

§ 1780.20 Commencement of proceeding and contents of notice of charges.

Proceedings under this subpart are commenced by the issuance of a notice of charges by the Director, which must be served upon the respondent. Such notice shall state all of the following:

(a) The legal authority for the proceeding and for OFHEO's jurisdiction over the proceeding;

(b) A statement of the matters of fact or law showing that OFHEO is entitled to relief;

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(c) A proposed order or prayer for an order granting the requested relief;

(d) The time, place and nature of the hearing;

(e) The time within which to file an answer;

(f) The time within which to request a hearing; and

(g) The address for filing the answer and/or request for a hearing.

§ 1780.21 Answer.

(a) *When.* Unless otherwise specified by the Director in the notice, respondent shall file an answer within 20 days of service of the notice.

(b) *Content of answer.* An answer must respond specifically to each paragraph or allegation of fact contained in the notice and must admit, deny, or state that the party lacks sufficient information to admit or deny each allegation of fact. A statement of lack of information has the effect of a denial. Denials must fairly meet the substance of each allegation of fact denied; general denials are not permitted. When a respondent denies part of an allegation, that part must be denied and the remainder specifically admitted. Any allegation of fact in the notice that is not denied in the answer is deemed admitted for purposes of the proceeding. A respondent is not required to respond to the portion of a notice that constitutes the prayer for relief or proposed order. The answer must set forth affirmative defenses, if any, asserted by the respondent.

(c) *Default.* Failure of a respondent to file an answer required by this section within the time provided constitutes a waiver of such respondent's right to appear and contest the allegations in the notice. If no timely answer is filed, OFHEO's counsel of record may file a motion for entry of an order of default. Upon a finding that no good cause has been shown for the failure to file a timely answer, the presiding officer shall file with the Director a recommended decision containing the findings and the relief sought in the notice. Any final order issued by the Director based upon a respondent's failure to answer is deemed to be an order issued upon consent.

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§ 1780.22 Amended pleadings.

(a) *Amendments.* The notice or answer may be amended or supplemented at any stage of the proceeding. The respondent must answer an amended notice within the time remaining for the respondent's answer to the original notice, or within ten days after service of the amended notice, whichever period is longer, unless the Director or presiding officer orders otherwise for good cause shown.

(b) *Amendments to conform to the evidence.* When issues not raised in the notice or answer are tried at the hearing by express or implied consent of the parties, they will be treated in all respects as if they had been raised in the notice or answer, and no formal amendments are required. If evidence is objected to at the hearing on the ground that it is not within the issues raised by the notice or answer, the presiding officer may admit the evidence when admission is likely to assist in adjudicating the merits of the action. The presiding officer will do so freely when the determination of the merits of the action is served thereby and the objecting party fails to satisfy the presiding officer that the admission of such evidence would unfairly prejudice that party's action or defense upon the merits. The presiding officer may grant a continuance to enable the objecting party to meet such evidence.

§ 1780.23 Failure to appear.

Failure of a respondent to appear in person at the hearing or by a duly authorized representative constitutes a waiver of respondent's right to a hearing and is deemed an admission of the facts as alleged and consent to the relief sought in the notice. Without further proceedings or notice to the respondent, the presiding officer shall file with the Director a recommended decision containing the findings and the relief sought in the notice.

§ 1780.24 Consolidation and severance of actions.

(a) *Consolidation.* On the motion of any party, or on the presiding officer's own motion, the presiding officer may consolidate, for some or all purposes, any two or more proceedings, if each such proceeding involves or arises out

of the same transaction, occurrence or series of transactions or occurrences, or involves at least one common respondent or a material common question of law or fact, unless such consolidation would cause unreasonable delay or injustice. In the event of consolidation under this section, appropriate adjustment to the prehearing schedule must be made to avoid unnecessary expense, inconvenience, or delay.

(b) *Severance.* The presiding officer may, upon the motion of any party, sever the proceeding for separate resolution of the matter as to any respondent only if the presiding officer finds that undue prejudice or injustice to the moving party would result from not severing the proceeding and such undue prejudice or injustice would outweigh the interests of judicial economy and expedition in the complete and final resolution of the proceeding.

§ 1780.25 Motions.

(a) *In writing.* (1) Except as otherwise provided herein, an application or request for an order or ruling must be made by written motion.

(2) All written motions must state with particularity the relief sought and must be accompanied by a proposed order.

(3) No oral argument may be held on written motions except as otherwise directed by the presiding officer. Written memoranda, briefs, affidavits, or other relevant material or documents may be filed in support of or in opposition to a motion.

(b) *Oral motions.* A motion may be made orally on the record unless the presiding officer directs that such motion be reduced to writing.

(c) *Filing of motions.* Motions must be filed with the presiding officer, except that following the filing of a recommended decision, motions must be filed with the Director.

(d) *Responses.* (1) Except as otherwise provided herein, any party may file a written response to a motion within ten days after service of any written motion, or within such other period of time as may be established by the presiding officer or the Director. The presiding officer shall not rule on any oral or written motion before each party

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has had an opportunity to file a response.

(2) The failure of a party to oppose a written motion or an oral motion made on the record is deemed a consent by that party to the entry of an order substantially in the form of the order accompanying the motion.

(e) *Dilatory motions.* Frivolous, dilatory, or repetitive motions are prohibited. The filing of such motions may form the basis for sanctions.

(f) *Dispositive motions.* Dispositive motions are governed by §§1780.31 and 1780.32.

§ 1780.26 Discovery.

(a) *Limits on discovery.* Subject to the limitations set out in paragraphs (b), (d), and (e) of this section, a party to a proceeding under this subpart may obtain document discovery by serving a written request to produce documents. For purposes of a request to produce documents, the term “documents” may be defined to include drawings, graphs, charts, photographs, recordings, data stored in electronic form, and other data compilations from which information can be obtained or translated, if necessary, by the parties through detection devices into reasonably usable form, as well as written material of all kinds.

(b) *Relevance.* A party may obtain document discovery regarding any matter not privileged that has material relevance to the merits of the pending action. Any request to produce documents that calls for irrelevant material, that is unreasonable, oppressive, excessive in scope, unduly burdensome, or repetitive of previous requests, or that seeks to obtain privileged documents will be denied or modified. A request is unreasonable, oppressive, excessive in scope, or unduly burdensome if, among other things, it fails to include justifiable limitations on the time period covered and the geographic locations to be searched, the time provided to respond in the request is inadequate, or the request calls for copies of documents to be delivered to the requesting party and fails to include the requestor’s written agreement to pay in advance for the copying, in accordance with §1780.27.

(c) *Forms of discovery.* Discovery shall be limited to requests for production of documents for inspection and copying. No other form of discovery shall be allowed. Discovery by use of interrogatories is not permitted. This paragraph shall not be interpreted to require the creation of a document.

(d) *Privileged matter.* Privileged documents are not discoverable. Privileges include the attorney-client privilege, work-product privilege, any government’s or government agency’s deliberative process privilege and any other privileges provided by the Constitution, any applicable act of Congress, or the principles of common law.

(e) *Time limits.* All discovery, including all responses to discovery requests, shall be completed at least 20 days prior to the date scheduled for the commencement of the hearing. No exception to this time limit shall be permitted, unless the presiding officer finds on the record that good cause exists for waiving the requirements of this paragraph.

§ 1780.27 Request for document discovery from parties.

(a) *General rule.* Any party may serve on any other party a request to produce for inspection any discoverable documents that are in the possession, custody, or control of the party upon whom the request is served. Copies of the request shall be served on all other parties. The request must identify the documents to be produced either by individual item or by category and must describe each item and category with reasonable particularity. Documents must be produced as they are kept in the usual course of business or they shall be labeled and organized to correspond with the categories in the request.

(b) *Production or copying.* The request must specify a reasonable time, place and manner for production and performing any related acts. In lieu of inspecting the documents, the requesting party may specify that all or some of the responsive documents be copied and the copies delivered to the requesting party. If copying of fewer than 250 pages is requested, the party to whom the request is addressed shall bear the cost of copying and shipping charges. If

a party requests more than 250 pages of copying, the requesting party shall pay for copying and shipping charges. Copying charges are at the current rate per page imposed by OFHEO at §1710.22(b)(2) of this chapter for requests for documents filed under the Freedom of Information Act, 12 U.S.C. 552. The party to whom the request is addressed may require payment in advance before producing the documents.

(c) *Obligation to update responses.* A party who has responded to a discovery request is not required to supplement the response, unless:

(1) The responding party learns that in some material respect the information disclosed is incomplete or incorrect, and

(2) The additional or corrective information has not otherwise been made known to the other parties during the discovery process or in writing.

(d) *Motions to strike or limit discovery requests.* (1) Any party that objects to a discovery request may, within ten days of being served with such request, file a motion in accordance with the provisions of §1780.25 to strike or otherwise limit the request. If an objection is made to only a portion of an item or category in a request, the objection shall specify that portion. Any objections not made in accordance with this paragraph and §1780.25 are waived.

(2) The party who served the request that is the subject of a motion to strike or limit may file a written response within five days of service of the motion. No other party may file a response.

(e) *Privilege.* At the time other documents are produced, all documents withheld on the grounds of privilege must be reasonably identified, together with a statement of the basis for the assertion of privilege. When similar documents that are protected by deliberative process, attorney work-product, or attorney-client privilege are voluminous, these documents may be identified by category instead of by individual document. The presiding officer has discretion to determine when the identification by category is insufficient.

(f) *Motions to compel production.* (1) If a party withholds any documents as privileged or fails to comply fully with

a discovery request, the requesting party may, within ten days of the assertion of privilege or of the time the failure to comply becomes known to the requesting party, file a motion in accordance with the provisions of §1780.25 for the issuance of a subpoena compelling production.

(2) The party who asserted the privilege or failed to comply with the request may, within five days of service of a motion for the issuance of a subpoena compelling production, file a written response to the motion. No other party may file a response.

(g) *Ruling on motions.* After the time for filing responses to motions pursuant to this section has expired, the presiding officer shall rule promptly on all such motions. If the presiding officer determines that a discovery request or any of its terms calls for irrelevant material, is unreasonable, oppressive, excessive in scope, unduly burdensome, or repetitive of previous requests, or seeks to obtain privileged documents, he may deny or modify the request and may issue appropriate protective orders, upon such conditions as justice may require. The pendency of a motion to strike or limit discovery or to compel production shall not be a basis for staying or continuing the proceeding, unless otherwise ordered by the presiding officer. Notwithstanding any other provision in this part, the presiding officer may not release, or order a party to produce, documents withheld on grounds of privilege if the party has stated to the presiding officer its intention to file a timely motion for interlocutory review of the presiding officer's order to produce the documents, until the motion for interlocutory review has been decided.

(h) *Enforcing discovery subpoenas.* If the presiding officer issues a subpoena compelling production of documents by a party, the subpoenaing party may, in the event of noncompliance and to the extent authorized by applicable law, apply to any appropriate United States district court for an order requiring compliance with the subpoena. A party's right to seek court enforcement of a subpoena shall not in any manner limit the sanctions that may be imposed by the presiding officer against a party who fails to produce or induces

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another to fail to produce subpoenaed documents.

§ 1780.28 Document subpoenas to non-parties.

(a) *General rules.* (1) Any party may apply to the presiding officer for the issuance of a document discovery subpoena addressed to any person who is not a party to the proceeding. The application must contain a proposed document subpoena and a brief statement showing the general relevance and reasonableness of the scope of documents sought. The subpoenaing party shall specify a reasonable time, place, and manner for production in response to the subpoena.

(2) A party shall only apply for a document subpoena under this section within the time period during which such party could serve a discovery request under §1780.27. The party obtaining the document subpoena is responsible for serving it on the subpoenaed person and for serving copies on all parties. Document subpoenas may be served in any State, territory, or possession of the United States, the District of Columbia, or as otherwise provided by law.

(3) The presiding officer shall issue promptly any document subpoena applied for under this section; except that, if the presiding officer determines that the application does not set forth a valid basis for the issuance of the subpoena, or that any of its terms are unreasonable, oppressive, excessive in scope, or unduly burdensome, he may refuse to issue the subpoena or may issue it in a modified form upon such conditions as may be determined by the presiding officer.

(b) *Motion to quash or modify.* (1) Any person to whom a document subpoena is directed may file a motion to quash or modify such subpoena, accompanied by a statement of the basis for quashing or modifying the subpoena. The movant shall serve the motion on all parties and any party may respond to such motion within ten days of service of the motion.

(2) Any motion to quash or modify a document subpoena must be filed on the same basis, including the assertion of privilege, upon which a party could object to a discovery request under

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§1780.27 and during the same time limits during which such an objection could be filed.

(c) *Enforcing document subpoenas.* If a subpoenaed person fails to comply with any subpoena issued pursuant to this section or any order of the presiding officer that directs compliance with all or any portion of a document subpoena, the subpoenaing party or any other aggrieved party may, to the extent authorized by applicable law, apply to an appropriate United States district court for an order requiring compliance with the subpoena. A party's right to seek court enforcement of a document subpoena shall in no way limit the sanctions that may be imposed by the presiding officer on a party who induces a failure to comply with subpoenas issued under this section.

§ 1780.29 Deposition of witness unavailable for hearing.

(a) *General rules.* (1) If a witness will not be available for the hearing, a party desiring to preserve that witness' testimony for the record may apply in accordance with the procedures set forth in paragraph (a)(2) of this section to the presiding officer for the issuance of a subpoena, including a subpoena *duces tecum*, requiring the attendance of the witness at a deposition. The presiding officer may issue a deposition subpoena under this section upon a showing that—

(i) The witness will be unable to attend or may be prevented from attending the hearing because of age, sickness, or infirmity, or will be otherwise unavailable;

(ii) The witness' unavailability was not produced or caused by the subpoenaing party;

(iii) The testimony is reasonably expected to be material; and

(iv) Taking the deposition will not result in any undue burden to any other party and will not cause undue delay of the proceeding.

(2) The application must contain a proposed deposition subpoena and a brief statement of the reasons for the issuance of the subpoena. The subpoena must name the witness whose deposition is to be taken and specify the time and place for taking the deposition. A deposition subpoena may require the

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witness to be deposed anywhere within the United States and its possessions and territories in which that witness resides or has a regular place of employment or such other convenient place as the presiding officer shall fix.

(3) Subpoenas must be issued promptly upon request, unless the presiding officer determines that the request fails to set forth a valid basis under this section for its issuance. Before making a determination that there is no valid basis for issuing the subpoena, the presiding officer shall require a written response from the party requesting the subpoena or require attendance at a conference to determine whether there is a valid basis upon which to issue the requested subpoena.

(4) The party obtaining a deposition subpoena is responsible for serving it on the witness and for serving copies on all parties. Unless the presiding officer orders otherwise, no deposition under this section shall be taken on fewer than 10 days' notice to the witness and all parties. Deposition subpoenas may be served anywhere within the United States or its possessions or territories on any person doing business anywhere within the United States or its possessions or territories, or as otherwise permitted by law.

(b) *Objections to deposition subpoenas.*

(1) The witness and any party who has not had an opportunity to oppose a deposition subpoena issued under this section may file a motion under §1780.25 with the presiding officer to quash or modify the subpoena prior to the time for compliance specified in the subpoena, but not more than 10 days after service of the subpoena.

(2) A statement of the basis for the motion to quash or modify a subpoena issued under this section must accompany the motion. The motion must be served on all parties.

(c) *Procedure upon deposition.* (1) Each witness testifying pursuant to a deposition subpoena must be duly sworn and each party shall have the right to examine the witness. Objections to questions or documents must be in short form, stating the grounds for the objection. Failure to object to questions or documents is not deemed a waiver except where the ground for objection might have been avoided if the objec-

tion had been presented timely. All questions, answers and objections must be recorded.

(2) Any party may move before the presiding officer for an order compelling the witness to answer any questions the witness has refused to answer or submit any evidence that, during the deposition, the witness has refused to submit.

(3) The deposition must be subscribed by the witness, unless the parties and the witness, by stipulation, have waived the signing, or the witness is ill, cannot be found, or has refused to sign. If the deposition is not subscribed by the witness, the court reporter taking the deposition shall certify that the transcript is a true and complete transcript of the deposition.

(d) *Enforcing subpoenas.* If a subpoenaed person fails to comply with any subpoena issued pursuant to this section or with any order of the presiding officer made upon motion under paragraph (c)(2) of this section, the subpoenaing party or other aggrieved party may, to the extent authorized by applicable law, apply to an appropriate United States district court for an order requiring compliance with the portions of the subpoena that the presiding officer has ordered enforced. A party's right to seek court enforcement of a deposition subpoena in no way limits the sanctions that may be imposed by the presiding officer on a party who fails to comply with or induces a failure to comply with a subpoena issued under this section.

§ 1780.30 Interlocutory review.

(a) *General rule.* The Director may review a ruling of the presiding officer prior to the certification of the record to the Director only in accordance with the procedures set forth in this section.

(b) *Scope of review.* The Director may exercise interlocutory review of a ruling of the presiding officer if the Director finds that—

(1) The ruling involves a controlling question of law or policy as to which substantial grounds exist for a difference of opinion;

(2) Immediate review of the ruling may materially advance the ultimate termination of the proceeding;

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(3) Subsequent modification of the ruling at the conclusion of the proceeding would be an inadequate remedy; or

(4) Subsequent modification of the ruling would cause unusual delay or expense.

(c) *Procedure.* Any motion for interlocutory review shall be filed by a party with the presiding officer within ten days of his ruling. Upon the expiration of the time for filing all responses, the presiding officer shall refer the matter to the Director for final disposition. In referring the matter to the Director, the presiding officer may indicate agreement or disagreement with the asserted grounds for interlocutory review of the ruling in question.

(d) *Suspension of proceeding.* Neither a request for interlocutory review nor any disposition of such a request by the Director under this section suspends or stays the proceeding unless otherwise ordered by the presiding officer or the Director.

§ 1780.31 Summary disposition.

(a) *In general.* The presiding officer shall recommend that the Director issue a final order granting a motion for summary disposition if the undisputed pleaded facts, admissions, affidavits, stipulations, documentary evidence, matters as to which official notice may be taken and any other evidentiary materials properly submitted in connection with a motion for summary disposition show that—

(1) There is no genuine issue as to any material fact; and

(2) The movant is entitled to a decision in its favor as a matter of law.

(b) *Filing of motions and responses.* (1) Any party who believes there is no genuine issue of material fact to be determined and that such party is entitled to a decision as a matter of law may move at any time for summary disposition in its favor of all or any part of the proceeding. Any party, within 20 days after service of such motion or within such time period as allowed by the presiding officer, may file a response to such motion.

(2) A motion for summary disposition must be accompanied by a statement of material facts as to which the movant contends there is no genuine issue.

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Such motion must be supported by documentary evidence, which may take the form of admissions in pleadings, stipulations, written interrogatory responses, depositions, investigatory depositions, transcripts, affidavits and any other evidentiary materials that the movant contends support its position. The motion must also be accompanied by a brief containing the points and authorities in support of the contention of the movant. Any party opposing a motion for summary disposition must file a statement setting forth those material facts as to which such party contends a genuine dispute exists. Such opposition must be supported by evidence of the same type as that submitted with the motion for summary disposition and a brief containing the points and authorities in support of the contention that summary disposition would be inappropriate.

(c) *Hearing on motion.* At the request of any party or on his own motion, the presiding officer may hear oral argument on the motion for summary disposition.

(d) *Decision on motion.* Following receipt of a motion for summary disposition and all responses thereto, the presiding officer shall determine whether the movant is entitled to summary disposition. If the presiding officer determines that summary disposition is warranted, the presiding officer shall submit a recommended decision to that effect to the Director, under § 1780.53. If the presiding officer finds that the moving party is not entitled to summary disposition, the presiding officer shall make a ruling denying the motion.

§ 1780.32 Partial summary disposition.

If the presiding officer determines that a party is entitled to summary disposition as to certain claims only, he shall defer submitting a recommended decision to the Director as to those claims. A hearing on the remaining issues must be ordered. Those claims for which the presiding officer has determined that summary disposition is warranted will be addressed in the recommended decision filed at the conclusion of the hearing.

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§ 1780.33 Scheduling and prehearing conferences.

(a) *Scheduling conference.* Within 30 days of service of the notice or order commencing a proceeding or such other time as the parties may agree, the presiding officer shall direct representatives for all parties to meet with him in person at a specified time and place prior to the hearing or to confer by telephone for the purpose of scheduling the course and conduct of the proceeding. This meeting or telephone conference is called a “scheduling conference.” The identification of potential witnesses, the time for and manner of discovery and the exchange of any prehearing materials including witness lists, statements of issues, stipulations, exhibits and any other materials may also be determined at the scheduling conference.

(b) *Prehearing conferences.* The presiding officer may, in addition to the scheduling conference, on his own motion or at the request of any party, direct representatives for the parties to meet with him (in person or by telephone) at a prehearing conference to address any or all of the following:

- (1) Simplification and clarification of the issues;
- (2) Stipulations, admissions of fact and the contents, authenticity and admissibility into evidence of documents;
- (3) Matters of which official notice may be taken;
- (4) Limitation of the number of witnesses;
- (5) Summary disposition of any or all issues;
- (6) Resolution of discovery issues or disputes;
- (7) Amendments to pleadings; and
- (8) Such other matters as may aid in the orderly disposition of the proceeding.

(c) *Transcript.* The presiding officer, in his discretion, may require that a scheduling or prehearing conference be recorded by a court reporter. A transcript of the conference and any materials filed, including orders, becomes part of the record of the proceeding. A party may obtain a copy of the transcript at such party’s expense.

(d) *Scheduling or prehearing orders.* Within a reasonable time following the conclusion of the scheduling con-

ference or any prehearing conference, the presiding officer shall serve on each party an order setting forth any agreements reached and any procedural determinations made.

§ 1780.34 Prehearing submissions.

(a) Within the time set by the presiding officer, but in no case later than 10 days before the start of the hearing, each party shall serve on every other party the serving party’s—

- (1) Prehearing statement;
- (2) Final list of witnesses to be called to testify at the hearing, including name and address of each witness and a short summary of the expected testimony of each witness;
- (3) List of the exhibits to be introduced at the hearing along with a copy of each exhibit; and
- (4) Stipulations of fact, if any.

(b) *Effect of failure to comply.* No witness may testify and no exhibits may be introduced at the hearing if such witness or exhibit is not listed in the prehearing submissions pursuant to paragraph (a) of this section, except for good cause shown.

§ 1780.35 Hearing subpoenas.

(a) *Issuance.* (1) Upon application of a party showing general relevance and reasonableness of scope of the testimony or other evidence sought, the presiding officer may issue a subpoena or a subpoena *duces tecum* requiring the attendance of a witness at the hearing or the production of documentary or physical evidence at such hearing. The application for a hearing subpoena must also contain a proposed subpoena specifying the attendance of a witness or the production of evidence from any State, commonwealth, possession, territory of the United States, or the District of Columbia, or as otherwise provided by law at any designated place where the hearing is being conducted. The party making the application shall serve a copy of the application and the proposed subpoena on every other party.

(2) A party may apply for a hearing subpoena at any time before the commencement of or during a hearing. During a hearing, a party may make an application for a subpoena orally on the record before the presiding officer.

(3) The presiding officer shall promptly issue any hearing subpoena applied for under this section; except that, if the presiding officer determines that the application does not set forth a valid basis for the issuance of the subpoena, or that any of its terms are unreasonable, oppressive, excessive in scope, or unduly burdensome, he may refuse to issue the subpoena or may issue the subpoena in a modified form upon any conditions consistent with this subpart. Upon issuance by the presiding officer, the party making the application shall serve the subpoena on the person named in the subpoena and on each party.

(b) *Motion to quash or modify.* (1) Any person to whom a hearing subpoena is directed or any party may file a motion to quash or modify such subpoena, accompanied by a statement of the basis for quashing or modifying the subpoena. The movant must serve the motion on each party and on the person named in the subpoena. Any party may respond to the motion within ten days of service of the motion.

(2) Any motion to quash or modify a hearing subpoena must be filed prior to the time specified in the subpoena for compliance, but no more than 10 days after the date of service of the subpoena upon the movant.

(c) *Enforcing subpoenas.* If a subpoenaed person fails to comply with any subpoena issued pursuant to this section or any order of the presiding officer that directs compliance with all or any portion of a hearing subpoena, the subpoenaing party or any other aggrieved party may seek enforcement of the subpoena pursuant to §1780.28(c). A party's right to seek court enforcement of a hearing subpoena shall in no way limit the sanctions that may be imposed by the presiding officer on a party who induces a failure to comply with subpoenas issued under this section.

Subpart C—Hearing and Posthearing Proceedings

SOURCE: 64 FR 72518, Dec. 28, 1999, unless otherwise noted.

§ 1780.50 Conduct of hearings.

(a) *General rules.* (1) Hearings shall be conducted in accordance with 5 U.S.C. chapter 5 and other applicable law and so as to provide a fair and expeditious presentation of the relevant disputed issues. Except as limited by this subpart, each party has the right to present its case or defense by oral and documentary evidence and to conduct such cross examination as may be required for full disclosure of the facts.

(2) *Order of hearing.* OFHEO's counsel of record shall present its case-in-chief first, unless otherwise ordered by the presiding officer or unless otherwise expressly specified by law or regulation. OFHEO's counsel of record shall be the first party to present an opening statement and a closing statement and may make a rebuttal statement after the respondent's closing statement. If there are multiple respondents, respondents may agree among themselves as to their order or presentation of their cases, but if they do not agree, the presiding officer shall fix the order.

(3) *Examination of witnesses.* Only one representative for each party may conduct an examination of a witness, except that in the case of extensive direct examination, the presiding officer may permit more than one representative for the party presenting the witness to conduct the examination. A party may have one representative conduct the direct examination and another representative conduct re-direct examination of a witness, or may have one representative conduct the cross examination of a witness and another representative conduct the re-cross examination of a witness.

(4) *Stipulations.* Unless the presiding officer directs otherwise, all documents that the parties have stipulated as admissible shall be admitted into evidence upon commencement of the hearing.

(b) *Transcript.* The hearing shall be recorded and transcribed. The transcript shall be made available to any party upon payment of the cost thereof. The presiding officer shall have authority to order the record corrected, either upon motion to correct, upon stipulation of the parties, or following notice to the parties upon the presiding officer's own motion.

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§ 1780.51 Evidence.

(a) *Admissibility.* (1) Except as is otherwise set forth in this section, relevant, material and reliable evidence that is not unduly repetitive is admissible to the fullest extent authorized by the Administrative Procedure Act and other applicable law.

(2) Evidence that would be admissible under the Federal Rules of Evidence is admissible in a proceeding conducted pursuant to this subpart.

(3) Evidence that would be inadmissible under the Federal Rules of Evidence may not be deemed or ruled to be inadmissible in a proceeding conducted pursuant to this subpart if such evidence is relevant, material, reliable and not unduly repetitive.

(b) *Official notice.* (1) Official notice may be taken of any material fact that may be judicially noticed by a United States district court and any material information in the official public records of any Federal or State government agency.

(2) All matters officially noticed by the presiding officer or the Director shall appear on the record.

(3) If official notice is requested of any material fact, the parties, upon timely request, shall be afforded an opportunity to object.

(c) *Documents.* (1) A duplicate copy of a document is admissible to the same extent as the original, unless a genuine issue is raised as to whether the copy is in some material respect not a true and legible copy of the original.

(2) Subject to the requirements of paragraph (a)(1) of this section, any document, including a report of examination, oversight activity, inspection, or visitation, prepared by OFHEO or by another Federal or State financial institutions regulatory agency is admissible either with or without a sponsoring witness.

(3) Witnesses may use existing or newly created charts, exhibits, calendars, calculations, outlines, or other graphic material to summarize, illustrate, or simplify the presentation of testimony. Such materials may, subject to the presiding officer's discretion, be used with or without being admitted into evidence.

(d) *Objections.* (1) Objections to the admissibility of evidence must be time-

ly made and rulings on all objections must appear in the record.

(2) When an objection to a question or line of questioning is sustained, the examining representative of record may make a specific proffer on the record of what he expected to prove by the expected testimony of the witness. The proffer may be by representation of the representative or by direct interrogation of the witness.

(3) The presiding officer shall retain rejected exhibits, adequately marked for identification, for the record and transmit such exhibits to the Director.

(4) Failure to object to admission of evidence or to any ruling constitutes a waiver of the objection.

(e) *Stipulations.* The parties may stipulate as to any relevant matters of fact or the authentication of any relevant documents. Such stipulations must be received in evidence at a hearing and are binding on the parties with respect to the matters therein stipulated.

(f) *Depositions of unavailable witnesses.* (1) If a witness is unavailable to testify at a hearing and that witness has testified in a deposition in accordance with § 1780.29, a party may offer as evidence all or any part of the transcript of the deposition, including deposition exhibits, if any.

(2) Such deposition transcript is admissible to the same extent that testimony would have been admissible had that person testified at the hearing, provided that if a witness refused to answer proper questions during the depositions, the presiding officer may, on that basis, limit the admissibility of the deposition in any manner that justice requires.

(3) Only those portions of a deposition received in evidence at the hearing constitute a part of the record.

§ 1780.52 Post hearing filings.

(a) *Proposed findings and conclusions and supporting briefs.* (1) Using the same method of service for each party, the presiding officer shall serve notice upon each party that the certified transcript, together with all hearing exhibits and exhibits introduced but not admitted into evidence at the hearing, has been filed. Any party may file with the presiding officer proposed findings of fact, proposed conclusions

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of law and a proposed order within 30 days after the parties have received notice that the transcript has been filed with the presiding officer, unless otherwise ordered by the presiding officer.

(2) Proposed findings and conclusions must be supported by citation to any relevant authorities and by page references to any relevant portions of the record. A posthearing brief may be filed in support of proposed findings and conclusions, either as part of the same document or in a separate document.

(3) Any party is deemed to have waived any issue not raised in proposed findings or conclusions timely filed by that party.

(b) *Reply briefs.* Reply briefs may be filed within 15 days after the date on which the parties' proposed findings and conclusions and proposed order are due. Reply briefs must be limited strictly to responding to new matters, issues, or arguments raised in another party's papers. A party who has not filed proposed findings of fact and conclusions of law or a posthearing brief may not file a reply brief.

(c) *Simultaneous filing required.* The presiding officer shall not order the filing by any party of any brief or reply brief supporting proposed findings and conclusions in advance of the other party's filing of its brief.

§ 1780.53 Recommended decision and filing of record.

(a) *Filing of recommended decision and record.* Within 45 days after expiration of the time allowed for filing reply briefs under § 1780.52(b), the presiding officer shall file with and certify to the Director, for decision, the record of the proceeding. The record must include the presiding officer's recommended decision, recommended findings of fact and conclusions of law, and proposed order; all prehearing and hearing transcripts, exhibits and rulings; and the motions, briefs, memoranda and other supporting papers filed in connection with the hearing. The presiding officer shall serve upon each party the recommended decision, recommended findings and conclusions, and proposed order.

(b) *Filing of index.* At the same time the presiding officer files with and cer-

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tifies to the Director, for final determination, the record of the proceeding, the presiding officer shall furnish to the Director a certified index of the entire record of the proceeding. The certified index shall include, at a minimum, an entry for each paper, document or motion filed with the presiding officer in the proceeding, the date of the filing, and the identity of the filer. The certified index shall also include an exhibit index containing, at a minimum, an entry consisting of exhibit number and title or description for: Each exhibit introduced and admitted into evidence at the hearing; each exhibit introduced but not admitted into evidence at the hearing; each exhibit introduced and admitted into evidence after the completion of the hearing; and each exhibit introduced but not admitted into evidence after the completion of the hearing.

§ 1780.54 Exceptions to recommended decision.

(a) *Filing exceptions.* Within 30 days after service of the recommended decision, recommended findings and conclusions, and proposed order under § 1780.53, a party may file with the Director written exceptions to the presiding officer's recommended decision, recommended findings and conclusions, or proposed order; to the admission or exclusion of evidence; or to the failure of the presiding officer to make a ruling proposed by a party. A supporting brief may be filed at the time the exceptions are filed, either as part of the same document or in a separate document.

(b) *Effect of failure to file or raise exceptions.* (1) Failure of a party to file exceptions to those matters specified in paragraph (a) of this section within the time prescribed is deemed a waiver of objection thereto.

(2) No exception need be considered by the Director if the party taking exception had an opportunity to raise the same objection, issue, or argument before the presiding officer and failed to do so.

(c) *Contents.* (1) All exceptions and briefs in support of such exceptions must be confined to the particular

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matters in or omissions from the presiding officer's recommendations to which that party takes exception.

(2) All exceptions and briefs in support of exceptions must set forth page or paragraph references to the specific parts of the presiding officer's recommendations to which exception is taken, the page or paragraph references to those portions of the record relied upon to support each exception and the legal authority relied upon to support each exception. Exceptions and briefs in support shall not exceed a total of 30 pages, except by leave of the Director on motion.

(3) One reply brief may be submitted by each party within ten days of service of exceptions and briefs in support of exceptions. Reply briefs shall not exceed 15 pages, except by leave of the Director on motion.

§ 1780.55 Review by Director.

(a) *Notice of submission to the Director.* When the Director determines that the record in the proceeding is complete, the Director shall serve notice upon the parties that the proceeding has been submitted to the Director for final decision.

(b) *Oral argument before the Director.* Upon the initiative of the Director or on the written request of any party filed with the Director within the time for filing exceptions under §1780.54, the Director may order and hear oral argument on the recommended findings, conclusions, decision and order of the presiding officer. A written request by a party must show good cause for oral argument and state reasons why arguments cannot be presented adequately in writing. A denial of a request for oral argument may be set forth in the Director's final decision. Oral argument before the Director must be transcribed.

(c) *Director's final decision.* (1) Decisional employees may advise and assist the Director in the consideration and disposition of the case. The final decision of the Director will be based upon review of the entire record of the proceeding, except that the Director may limit the issues to be reviewed to those findings and conclusions to which opposing arguments or exceptions have been filed by the parties.

(2) The Director shall render a final decision and issue an appropriate order within 90 days after notification of the parties that the case has been submitted for final decision, unless the Director orders that the action or any aspect thereof be remanded to the presiding officer for further proceedings. Copies of the final decision and order of the Director shall be served upon each party to the proceeding and upon other persons required by statute.

§ 1780.56 Exhaustion of administrative remedies.

To exhaust administrative remedies as to any issue on which a party disagrees with the presiding officer's recommendations, a party must file exceptions with the Director under §1780.54. A party must exhaust administrative remedies as a precondition to seeking judicial review of any decision issued under this subpart.

§ 1780.57 Stays pending judicial review.

The commencement of proceedings for judicial review of a final decision and order of the Director may not, unless specifically ordered by the Director or a reviewing court, operate as a stay of any order issued by the Director. The Director may, in his discretion and on such terms as he finds just, stay the effectiveness of all or any part of an order of the Director pending a final decision on a petition for review of that order.

Subpart D—Rules of Practice Before the Office of Federal Housing Enterprise Oversight

SOURCE: 64 FR 72520, Dec. 28, 1999, unless otherwise noted.

§ 1780.70 Scope.

This subpart contains rules governing practice by parties or their representatives before OFHEO. This subpart addresses the imposition of sanctions by the presiding officer or the Director against parties or their representatives in an adjudicatory proceeding under this part. This subpart also covers other disciplinary sanctions—censure, suspension or disbarment—against individuals who appear

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before OFHEO in a representational capacity either in an adjudicatory proceeding under this part or in any other matters connected with presentations to OFHEO relating to a client's or other principal's rights, privileges, or liabilities. This representation includes, but is not limited to, the practice of attorneys and accountants. Employees of OFHEO are not subject to disciplinary proceedings under this subpart.

§ 1780.71 Definitions.

Practice before OFHEO for the purposes of this subpart, includes, but is not limited to, transacting any business with OFHEO as counsel, representative or agent for any other person, unless the Director orders otherwise. Practice before OFHEO also includes the preparation of any statement, opinion, or other paper by a counsel, representative or agent that is filed with OFHEO in any certification, notification, application, report, or other document, with the consent of such counsel, representative or agent. Practice before OFHEO does not include work prepared for an Enterprise solely at the request of the Enterprise for use in the ordinary course of its business.

§ 1780.72 Appearance and practice in adjudicatory proceedings.

(a) *Appearance before OFHEO or a presiding officer*—(1) *By attorneys*. A party may be represented by an attorney who is a member in good standing of the bar of the highest court of any State, commonwealth, possession, territory of the United States, or the District of Columbia and who is not currently suspended or disbarred from practice before OFHEO.

(2) *By nonattorneys*. An individual may appear on his own behalf. A member of a partnership may represent the partnership and a duly authorized officer, director, employee, or other agent of any corporation or other entity not specifically listed herein may represent such corporation or other entity; provided that such officer, director, employee, or other agent is not currently suspended or disbarred from practice before OFHEO. A duly authorized officer or employee of any Government

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unit, agency, or authority may represent that unit, agency, or authority.

(b) *Notice of appearance*. Any person appearing in a representative capacity on behalf of a party, including OFHEO, shall execute and file a notice of appearance with the presiding officer at or before the time such person submits papers or otherwise appears on behalf of a party in the adjudicatory proceeding. Such notice of appearance shall include a written declaration that the individual is currently qualified as provided in paragraphs (a)(1) or (a)(2) of this section and is authorized to represent the particular party. By filing a notice of appearance on behalf of a party in an adjudicatory proceeding, the representative thereby agrees and represents that he is authorized to accept service on behalf of the represented party and that, in the event of withdrawal from representation, he or she will, if required by the presiding officer, continue to accept service until a new representative has filed a notice of appearance or until the represented party indicates that he or she will proceed on a pro se basis. Unless the representative filing the notice is an attorney, the notice of appearance shall also be executed by the person represented or, if the person is not an individual, by the chief executive officer, or duly authorized officer of that person.

§ 1780.73 Conflicts of interest.

(a) *Conflict of interest in representation*. No representative shall represent another person in an adjudicatory proceeding if it reasonably appears that such representation may be limited materially by that representative's responsibilities to a third person or by that representative's own interests. The presiding officer may take corrective measures at any stage of a proceeding to cure a conflict of interest in representation, including the issuance of an order limiting the scope of representation or disqualifying an individual from appearing in a representative capacity for the duration of the proceeding.

(b) *Certification and waiver*. If any person appearing as counsel or other representative represents two or more parties to an adjudicatory proceeding or

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also represents a nonparty on a matter relevant to an issue in the proceeding, that representative must certify in writing at the time of filing the notice of appearance required by § 1780.72—

(1) That the representative has personally and fully discussed the possibility of conflicts of interest with each such party and nonparty;

(2) That each such party and nonparty waives any right it might otherwise have had to assert any known conflicts of interest or to assert any non-material conflicts of interest during the course of the proceeding.

§ 1780.74 Sanctions.

(a) *General rule.* Appropriate sanctions may be imposed during the course of any proceeding when any party or representative of record has acted or failed to act in a manner required by applicable statute, regulation, or order, and that act or failure to act—

(1) Constitutes contemptuous conduct. Contemptuous conduct includes dilatory, obstructionist, egregious, contumacious, unethical, or other improper conduct at any phase of any adjudicatory proceeding;

(2) Has caused some other party material and substantive injury, including, but not limited to, incurring expenses including attorney's fees or experiencing prejudicial delay;

(3) Is a clear and unexcused violation of an applicable statute, regulation, or order; or

(4) Has delayed the proceeding unduly.

(b) *Sanctions.* Sanctions that may be imposed include, but are not limited to, any one or more of the following:

(1) Issuing an order against a party;

(2) Rejecting or striking any testimony or documentary evidence offered, or other papers filed, by the party;

(3) Precluding the party from contesting specific issues or findings;

(4) Precluding the party from offering certain evidence or from challenging or contesting certain evidence offered by another party;

(5) Precluding the party from making a late filing or conditioning a late filing on any terms that are just;

(6) Assessing reasonable expenses, including attorney's fees, incurred by

any other party as a result of the improper action or failure to act.

(c) *Procedure for imposition of sanctions.* (1) The presiding officer, on the motion of any party, or on his own motion, and after such notice and responses as may be directed by the presiding officer, may impose any sanction authorized by this section. The presiding officer shall submit to the Director for final ruling any sanction that would result in a final order that terminates the case on the merits or is otherwise dispositive of the case.

(2) Except as provided in paragraph (d) of this section, no sanction authorized by this section, other than refusing to accept late papers, shall be imposed without prior notice to all parties and an opportunity for any representative or party against whom sanctions would be imposed to be heard. The presiding officer shall determine and direct the appropriate notice and form for such opportunity to be heard. The opportunity to be heard may be limited to an opportunity to respond verbally immediately after the act or inaction in question is noted by the presiding officer.

(3) For purposes of interlocutory review, motions for the imposition of sanctions by any party and the imposition of sanctions shall be treated the same as motions for any other ruling by the presiding officer.

(4) Nothing in this section shall be read to preclude the presiding officer or the Director from taking any other action or imposing any other restriction or sanction authorized by any applicable statute or regulation.

(d) *Sanctions for contemptuous conduct.* If, during the course of any proceeding, a presiding officer finds any representative or any individual representing himself to have engaged in contemptuous conduct, the presiding officer may summarily suspend that individual from participating in that or any related proceeding or impose any other appropriate sanction.

§ 1780.75 Censure, suspension, disbarment and reinstatement.

(a) *Discretionary censure, suspension and disbarment.* (1) The Director may censure any individual who practices or attempts to practice before OFHEO

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or suspend or revoke the privilege to appear or practice before OFHEO of such individual if, after notice of and opportunity for hearing in the matter, that individual is found by the Director—

(i) Not to possess the requisite qualifications or competence to represent others;

(ii) To be seriously lacking in character or integrity or to have engaged in material unethical or improper professional conduct;

(iii) To have caused unfair and material injury or prejudice to another party, such as prejudicial delay or unnecessary expenses including attorney's fees;

(iv) To have engaged in, or aided and abetted, a material and knowing violation of the 1992 Act, the Federal Home Loan Mortgage Corporation Act, the Federal National Mortgage Association Charter Act or the rules or regulations issued under those statutes or any other law or regulation governing Enterprise operations;

(v) To have engaged in contemptuous conduct before OFHEO;

(vi) With intent to defraud in any manner, to have willfully and knowingly deceived, misled, or threatened any client or prospective client; or

(vii) Within the last 10 years, to have been convicted of an offense involving moral turpitude, dishonesty or breach of trust, if the conviction has not been reversed on appeal. A conviction within the meaning of this paragraph shall be deemed to have occurred when the convicting court enters its judgment or order, regardless of whether an appeal is pending or could be taken and includes a judgment or an order on a plea of *nolo contendere* or on consent, regardless of whether a violation is admitted in the consent.

(2) Suspension or revocation on the grounds set forth in paragraphs (a)(1)(ii), (iii), (iv), (v), (vi) and (vii) of this section shall only be ordered upon a further finding that the individual's conduct or character was sufficiently egregious as to justify suspension or revocation. Suspension or disbarment under this paragraph shall continue until the applicant has been reinstated by the Director for good cause shown

or until, in the case of a suspension, the suspension period has expired.

(3) If the final order against the respondent is for censure, the individual may be permitted to practice before OFHEO, but such individual's future representations may be subject to conditions designed to promote high standards of conduct. If a written letter of censure is issued, a copy will be maintained in OFHEO's files.

(b) *Mandatory suspension and disbarment.* (1) Any counsel who has been and remains suspended or disbarred by a court of the United States or of any State, commonwealth, possession, territory of the United States or the District of Columbia; any accountant or other licensed expert whose license to practice has been revoked in any State, commonwealth, possession, territory of the United States or the District of Columbia; any person who has been and remains suspended or barred from practice before the Department of Housing and Urban Development, the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Office of Thrift Supervision, the Federal Deposit Insurance Corporation, the National Credit Union Administration, the Federal Housing Finance Board, the Farm Credit Administration, the Securities and Exchange Commission, or the Commodity Futures Trading Commission is also suspended automatically from appearing or practicing before OFHEO. A disbarment or suspension within the meaning of this paragraph shall be deemed to have occurred when the disbarring or suspending agency or tribunal enters its judgment or order, regardless of whether an appeal is pending or could be taken and regardless of whether a violation is admitted in the consent.

(2) A suspension or disbarment from practice before OFHEO under paragraph (b)(1) of this section shall continue until the person suspended or disbarred is reinstated under paragraph (d)(2) of this section.

(c) *Notices to be filed.* (1) Any individual appearing or practicing before OFHEO who is the subject of an order, judgment, decree, or finding of the types set forth in paragraph (b)(1) of this section shall file promptly with

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the Director a copy thereof, together with any related opinion or statement of the agency or tribunal involved.

(2) Any individual appearing or practicing before OFHEO who is or within the last 10 years has been convicted of a felony or of a misdemeanor that resulted in a sentence of prison term or in a fine or restitution order totaling more than \$5,000 shall file a notice promptly with the Director. The notice shall include a copy of the order imposing the sentence or fine, together with any related opinion or statement of the court involved.

(d) *Reinstatement.* (1) Unless otherwise ordered by the Director, an application for reinstatement for good cause may be made in writing by a person suspended or disbarred under paragraph (a)(1) of this section at any time more than three years after the effective date of the suspension or disbarment and, thereafter, at any time more than one year after the person's most recent application for reinstatement. An applicant for reinstatement under this paragraph (d)(1) may, in the Director's sole discretion, be afforded a hearing.

(2) An application for reinstatement for good cause by any person suspended or disbarred under paragraph (b)(1) of this section may be filed at any time, but not less than 1 year after the applicant's most recent application. An applicant for reinstatement for good cause under this paragraph (d)(2) may, in the Director's sole discretion, be afforded a hearing. However, if all the grounds for suspension or disbarment under paragraph (b)(1) of this section have been removed by a reversal of the order of suspension or disbarment or by termination of the underlying suspension or disbarment, any person suspended or disbarred under paragraph (b)(1) of this section may apply immediately for reinstatement and shall be reinstated by OFHEO upon written application notifying OFHEO that the grounds have been removed.

(e) *Conferences—(1) General.* Counsel for OFHEO may confer with a proposed respondent concerning allegations of misconduct or other grounds for censure, disbarment or suspension, regard-

less of whether a proceeding for censure, disbarment or suspension has been commenced. If a conference results in a stipulation in connection with a proceeding in which the individual is the respondent, the stipulation may be entered in the record at the request of either party to the proceeding.

(2) *Resignation or voluntary suspension.* In order to avoid the institution of or a decision in a disbarment or suspension proceeding, a person who practices before OFHEO may consent to censure, suspension or disbarment from practice. At the discretion of the Director, the individual may be censured, suspended or disbarred in accordance with the consent offered.

(f) *Hearings under this section.* Hearings conducted under this section shall be conducted in substantially the same manner as other hearings under this part, provided that in proceedings to terminate an existing OFHEO suspension or disbarment order, the person seeking the termination of the order shall bear the burden of going forward with an application and with proof and that the Director may, in the Director's sole discretion, direct that any proceeding to terminate an existing suspension or disbarment by OFHEO be limited to written submissions. All hearings held under this section shall be closed to the public unless the Director, on the Director's own motion or upon the request of a party, otherwise directs.

Subpart E—Civil Money Penalty Inflation Adjustments

SOURCE: 70 FR 51243, Aug. 30, 2005, unless otherwise noted.

§ 1780.80 Inflation adjustments.

The maximum amount of each civil money penalty within OFHEO's jurisdiction is adjusted in accordance with the Federal Civil Penalties Inflation Adjustment Act of 1990, as amended by the Debt Collection Improvement Act of 1996 (28 U.S.C. 2461 note) as follows:

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U.S. code citation	Description	New adjusted maximum penalty amount
12 U.S.C. 4636(b)(1)	First Tier	6,500
12 U.S.C. 4636(b)(2)	Second Tier (Executive Officer or Director)	11,000
12 U.S.C. 4636(b)(2)	Second Tier (Enterprise)	32,500
12 U.S.C. 4636(b)(3)	Third Tier (Executive Officer or Director)	130,000
12 U.S.C. 4636(b)(3)	Third Tier (Enterprise)	1,275,000

§ 1780.81 Applicability.

The inflation adjustments in § 1780.80 apply to civil money penalties assessed

in accordance with the provisions of 12 U.S.C. 4636 for violations occurring after the effective date, August 30, 2005.