FEDERAL HOUSING FINANCE BOARD

12 CFR Parts 925 and 944

FEDERAL HOUSING FINANCE AGENCY

12 CFR Parts 1263 and 1290

RIN 2590–AA18

Federal Home Loan Bank Membership for Community Development Financial Institutions

AGENCIES: Federal Housing Finance Board and Federal Housing Finance Agency.

ACTION: Final rule.

SUMMARY: The Federal Housing Finance Agency (FHFA) is amending its membership regulations to implement provisions of the Housing and Economic Recovery Act of 2008 (HERA) that authorized community development financial institutions (CDFIs) that have been certified by the CDFI Fund of the U.S. Treasury Department (CDFI Fund) to become members of a Federal Home Loan Bank (Bank). The newly-eligible CDFIs include community development loan funds, venture capital funds, and State-chartered credit unions without Federal insurance. This final rule sets out the eligibility and procedural requirements that will enable CDFIs to become members of a Bank and relocates part 925 in its entirety to part 1263. FHFA also is amending its community support regulations to provide that certified CDFIs may be presumed to be in compliance with the statutory community support requirements by virtue of their certification by the CDFI Fund and relocates part 944 in its entirety to part 1290.

DATES: This rule is effective February 4, 2010.

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SUPPLEMENTARY INFORMATION:

I. Background

A. Regulatory History

On May 15, 2009, FHFA published a proposed rule to implement the provisions of HERA authorizing CDFIs to become members of the Banks. 74 FR 22848 (May 15, 2009). FHFA received 79 comment letters on the proposed rule, most of which were generally supportive of the proposal, and many of which recommended ways in which the regulation could be amended to better achieve its objectives. FHFA received comment letters from the Banks, numerous CDFIs, trade associations, and other community organizations. The key substantive issues raised by the comment letters focused principally on the criteria that FHFA had proposed for the Banks to use in evaluating the financial condition of CDFIs applying for membership. In this final rule, FHFA has incorporated certain revisions suggested by commenters, but in other respects retains the substance of the proposed rule.

B. HERA Amendments

On July 30, 2008, HERA, Public Law 110–289, 122 Stat. 2654 (2008), became law and created FHFA as an independent agency of the Federal government. Among other things, HERA transferred to FHFA the supervisory and oversight responsibilities over the Banks that formerly had been vested in the now abolished Federal Housing Finance Board (Finance Board). The Banks continue to operate under regulations promulgated by Finance Board until such time as the existing regulations are supplanted by regulations promulgated by FHFA. Section 1206 of HERA also amended section 4(a) of the Bank Act, 12 U.S.C. 1424(a), which relates to Bank membership, by expressly authorizing certified CDFIs to become members.

C. CDFIs

CDFIs are private institutions that provide financial services dedicated to economic development and community revitalization in underserved markets. The CDFIs may be organized as nonprofit or for-profit entities and comprise diverse institutional structures and business lines. The four categories of institutions eligible for CDFI certification and CDFI Fund financial support are: (1) Federally regulated insured depository institutions and their holding companies; (2) credit unions, whether federally or State-chartered; (3) community development loan funds, which are unregulated institutions specializing in financing of housing, businesses or community facilities that provide health care, childcare, educational, cultural, or social services; and (4) community development venture capital funds, which are unregulated institutions that provide equity and debt-with-equity-features to small and medium-sized businesses in distressed communities.

The CDFIs serve as intermediary financial institutions that promote economic growth and stability in low- and moderate-income communities. They provide a unique range of financial products and services, such as mortgage financing for low-income and first-time homebuyers; homeowner or homebuyer counseling; financing for not-for-profit affordable housing developers; flexible underwriting and risk capital for needed community facilities; financial literacy training; technical assistance; and commercial loans and investments to assist start-up businesses in low-income areas. Frequently, CDFIs serve communities that are underserved by conventional financial institutions and may offer products and services that are not available from conventional financial institutions. Although CDFIs are generally small in asset size, studies have demonstrated that CDFIs can have meaningful positive effects on the low-and-moderate income communities that they serve. One common problem facing non-depository CDFIs, however, is that they do not have access to long-term funding, which may limit their ability to provide housing finance to their communities.

The CDFI Fund of the US Treasury was created to promote economic revitalization and community development through investment in and financial and technical assistance to CDFIs. *See* 12 U.S.C. 4701(b). The CDFI Fund promotes these purposes through several programs, including the CDFI Program, the New Markets Tax Credit Program, the Bank Enterprise Award Program, and Native American Initiatives. *See* 12 U.S.C. 4701 *et seq.* and 12 CFR part 1805. An institution can obtain access to those resources by becoming certified by the CDFI Fund and then applying to the CDFI Fund to receive awards that are available under its programs. *See* 12 U.S.C. 4704 and 12 CFR 1805.200. In order to be certified as a CDFI, an institution must satisfy several statutory and regulatory requirements, including that it have a primary mission of promoting community development, that it provides development services in conjunction with equity investments or loans, and that it serves certain targeted areas or populations. The CDFI certification requirements are more fully elaborated in the statute and the CDFI

program regulations. *See* 12 U.S.C. 4702(5) and 12 CFR 1805.201. The CDFI Fund does not regulate the CDFIs that it certifies, nor does it evaluate their safety and soundness, either during the certification process or the awards application process. Thus, certification by the CDFI Fund does not represent a determination that a CDFI is in sound financial condition, although it does represent a determination by the CDFI fund that the entity satisfies the statutory requirements of being a CDFI. Indeed, the regulations of the CDFI Fund expressly state that certification does not constitute an opinion as to the financial viability of the certified CDFI or as to the likelihood that the CDFI will receive an award from the CDFI Fund. *See* 12 CFR 1805.201(a). If a period of time has passed since an organization became certified as a CDFI, the CDFI Fund may require the CDFI to attest that no events have occurred that would materially affect its strategic direction, mission or business operation, and thereby, its status as a CDFI, before it may receive an award from the CDFI Fund.

D. Membership Requirements

Each Bank is a cooperative institution that is owned by its members. Bank membership is limited to the several types of financial institutions listed in section 4(a)(1) of the Bank Act. Prior to HERA, section 4(a)(1) provided that any building and loan association, savings and loan association, cooperative bank, homestead association, insurance company, savings bank, or federally insured depository institution (including credit unions) was eligible to become a Bank member. Thus, prior to HERA a CDFI could not become a member of a Bank unless it was eligible for membership by virtue of being a federally insured bank, thrift or credit union. Section 1206 of HERA amended section 4(a)(1) to make all CDFIs that are certified by the CDFI Fund of the US Department of the Treasury under the Community Development Banking and Financial Institutions Act of 1994 (CDFI Act) eligible to become members of a Bank. *See* 12 U.S.C. 1424(a)(1) (as amended). As a result of the HERA amendments, any loan funds, venture capital funds, or State-chartered credit unions without Federal insurance that have been certified by the CDFI Fund are now eligible for Bank membership.

In order for any eligible institution to become a member of a Bank, however, it also must comply with certain additional criteria that are specified in section 4(a)(1) and (2) of the Bank Act. Specifically, section 4(a)(1) of the Bank Act requires each applicant to demonstrate that it: (a) Is duly organized under State or Federal law; (b) either is subject to inspection and regulation under banking or similar laws or is certified as a CDFI under the CDFI Act; and (c) makes such home mortgage loans as are, in the judgment of the Director, long-term loans. Those three statutory requirements apply to all types of institutions that are eligible for membership, including the newly-eligible CDFIs. In addition, section 4(a)(2) of the Bank Act requires that an applicant that is an insured depository institution must: (a) Have at least 10 percent of its total assets in residential mortgage loans (with certain limited exceptions); (b) be in sound financial condition such that a Bank may safely make advances to it; (c) have a character of management that is consistent with sound and economical home financing; and (d) have a home-financing policy that is consistent with sound and economical home financing. 12 U.S.C. 1424(a)(1) and (2).

Prior to HERA, the Finance Board had adopted detailed regulations governing the substantive and procedural requirements for institutions seeking to become members of a Bank. Those membership regulations applied the financial condition, character of management, and home financing policy requirements to insurance company applicants (in addition to depository institutions), and established a process for the review and approval of all applications for Bank membership. *See* 12 CFR part 925. The regulations included separate provisions governing the admission of depository institutions and insurance companies, respectively, recognizing that each type of institution operates under a different business model and a different regulatory regime. The regulations also included provisions dealing with several other matters, such as member stock purchase requirements, consolidation of Bank members, and withdrawal from Bank membership.

E. Proposed Rule

The proposed rule would have relocated the membership regulations of the Finance Board in their entirety from part 925 of the Finance Board regulations to part 1263 of the FHFA regulations, and also would have amended various provisions of the relocated regulations to implement the CDFI amendments. The proposed rule would have applied only to those CDFIs that had not been eligible for membership prior to HERA, such as loan funds, venture capital funds, and credit unions with State or private insurance. Federally insured depository institutions that also have been certified as CDFIs would be required to follow the membership regulations applicable to insured depository institutions generally, and could not become members under the CDFI provisions.

The key amendments to be made by the proposed rule related to how the Banks were to assess the financial condition of CDFI applicants. The proposed rule included two separate provisions relating to the financial condition of CDFI applicants. The first provision, which was set out in § 1263.11, applied only to CDFI credit unions, which are State-chartered credit unions that do not have National Credit Union Administration (NCUA) share insurance. The proposed rule would have required that the Banks assess the financial condition of all such CDFI credit unions under the same provisions that the Banks currently use in assessing the financial condition of NCUA-insured credit unions, which were eligible for Bank membership prior to HERA by virtue of their Federal share insurance. The second provision relating to financial condition was set out in § 1263.16(b) and applied to all other types of CDFI applicants. Those provisions were similar to the Finance Board's existing regulations relating to the financial condition of depository institution applicants, but were tailored to recognize the different structures and business models of the CDFIs. The proposed rule also included a number of conforming amendments, such as to the definitions and rebuttable presumptions, and sought comment on particular issues, such as whether CDFIs could take advantage of certain amendments made by HERA for the benefit of community financial institutions (CFIs) and whether the final rule should subject CDFIs to the existing community support requirements in the Finance Board regulations or to new requirements developed solely for CDFIs.

F. Differences

Section 1201 of HERA (codified at 12 U.S.C. 4513(f)) requires the Director of FHFA to consider the differences between the Federal Home Loan Mortgage Corporation (Freddie Mac) and the Federal National Mortgage Association (Fannie Mae) (collectively, the Enterprises) and the Banks with respect to the Banks' cooperative ownership structure, mission of providing liquidity to members, affordable housing and community development mission, capital structure, and joint and several liability, whenever promulgating regulations that affect the Banks. The Director may also consider

any other differences that are deemed appropriate. In preparing this final rule, the Director considered the differences between the Banks and the Enterprises as they relate to the above factors and determined that the rule is appropriate, particularly because this final rule implements a statutory provision that applies only to the Banks. *See* 12 U.S.C. 1424.

II. Summary of Comments

FHFA received 79 comment letters on the proposed rule. The preponderance of the comments came from the CDFI sector, which was represented by three national CDFI associations, a sign-on letter with 134 organizational signatures, and letters from nonprofit organizations and individuals. FHFA also received comments from nine Banks, three credit union associations, and two bank trade associations.

The comments from the CDFI sector were supportive of the general direction of the proposed rule but offered recommendations on specific membership standards, particularly those establishing thresholds for financial condition. Several commenters also recommended changes to current regulations as they relate to advances and collateral. The proposed rule sought to amend only the membership regulations and the community support regulations, and did not propose any revisions to the advances and collateral regulations. As a result, FHFA does not have the authority under the Administrative Procedure Act to amend those provisions as part of this rulemaking. To the extent that the collateral and advances regulations may need to be revised to better accommodate CDFI members, FHFA would undertake those changes as part of a separate rulemaking.

A number of commenters urged FHFA to establish a CDFI membership goal for each Bank, *i.e.,* require each Bank to admit a certain number of CDFIs as members each year, and requested that FHFA publicly release the number of CDFIs that become members, the amount of advances made to by CDFIs, and the reasons for the denial of any CDFI membership applications. At present, the number of members by type of institution is made available through the Federal Home Loan Banks' Combined Financial Report, and in the future, the number of CDFIs that become members each year should be included in the report for that year. FHFA also intends to release the number of CDFI members through its Public Use Data Base.

The final rule does not establish goals for CDFI membership. Whether any institution may become a member of a Bank depends on whether the institution has satisfied the statutory and regulatory requirements for membership. Because each application must be evaluated individually, FHFA does not believe that it is appropriate to establish membership goals, which suggest that CDFIs should be granted membership without regard to those requirements.

In a similar fashion, the final rule does not require the Banks to disclose the reasons for denying membership to a CDFI. Generally speaking, the Banks may deny an application only if an institution does not satisfy the statutory or regulatory requirements for membership, and the Banks do not disclose the reasons for the denial of individual applications. FHFA expects that the Banks will deny applications from CDFIs only in those circumstances, and further believes that releasing reasons for the denial of a membership application might result in reputational harm to the applicant with no public benefit. FHFA intends to monitor the Banks' implementation of the final rule, to ensure that they carry out the intent and spirit of the HERA amendments authorizing CDFIs to become members.

With respect to advances, neither FHFA nor the Banks track the use of member advances, and the final rule does not impose that requirement for advances made to CDFI members. With the exception of Community Investment Program Funds (12 U.S.C. 1430(i)), Bank advances to their members are not project-specific. As is the case with any member, the proceeds of advances are fungible and can be used by the CDFIs for overall asset-liability management, to enhance liquidity, and for other purposes.

Bank and depository institution commenters, in general, expressed concern that CDFI membership would compromise safe and sound lending practices and have an adverse financial impact on the Banks. Those concerns appear to be more closely related to risks of lending to a member, rather than to the key issue of this rulemaking, which relates to whether particular CDFIs have satisfied the statutory and regulatory requirements for membership. FHFA finds that these comments reflect a perception of risk that is not warranted by the performance of the CDFI sector or the asset size of these institutions.[1] The Banks are protected from the risks of doing business with their members through stock purchase requirements, sound underwriting, and collateral requirements. Moreover, CDFIs are small institutions. In 2008, the average size of a non-depository CDFI was $21,000,000, which suggests that, in the case of any single CDFI member the dollar amount of advances outstanding to that member is apt to be comparatively modest. Thus, even if a non-depository CDFI were to fail, the financial impact on a Bank would likely not be material. Notwithstanding those safety and soundness concerns, Congress has unambiguously spoken on the matter of CDFI membership and has determined that CDFIs that satisfy the requirements for membership are entitled to become Bank members. FHFA also is confident that CDFIs will bring added value to the Federal Home Loan Bank System (Bank System) consistent with the Banks' mission and without compromising their safety and soundness and it expects the Banks to be proactive in educating themselves about the CDFIs' lines of business and risk profiles.

The commenters also raised a number of other issues relating to specific provisions of the proposed rule. To the extent that FHFA either adopts revisions in the final rule in response to those comments or declines to adopt comments that raised significant issues about the proposed rule, those matters are addressed below as part of the discussion about the individual sections of the final rule.

III. The Final Rule

A. General

The proposed rule would have relocated many provisions of the Finance Board's membership regulations without substantive changes. In the final rule, FHFA is adopting those provisions of the proposed rule without any further substantive changes. Thus, the provisions of the final rule that are located in Subpart B (Membership Application Process), Subpart D (Stock Requirements), Subpart E (Consolidations Involving Members), Subpart F (Withdrawal and Removal From Membership), Subpart G (Orderly Liquidation of Advances and Redemption of Stock), Subpart H (Reacquisition of Membership), Subpart I (Bank Access to Information) and Subpart J (Membership Insignia) are all

[1] *See* Social Funds Community Investment Center, ''Community Investing'' (*http://www.communityinvest.org/overview/index.cfm.* Accessed on 7/27/09). According to this study, between 2003 and 2005, loan loss ratios among CDFIs were less than one percent. Through their tax exempt status not-for-profit CDFIs can address risk through patient investments, equity capital, risk-sharing arrangements, charitable contributions and private investments.

unchanged from the proposed rule and the predecessor provisions of the Finance Board regulations, apart from certain technical or conforming changes. All of the substantive revisions to the membership regulations relating to CDFI membership were located in Subpart A (Definitions) and Subpart C (Eligibility Requirements) of the proposed rule, and that remains the case with respect to the final rule. Those revisions are described separately below.

B. Definitions—Subpart A

Section 1263.1—Definitions. The proposed rule would have carried over into part 1263 without substantive change to nearly all of the existing definitions from the Finance Board regulations, but would have revised certain definitions and added a number of new definitions to implement the statutory amendments regarding CDFI members. Except as described below, the final rule adopts the definitions from the proposed rule without further change.

Community development financial institution or CDFI (holding companies). Section 1263.1 of the proposed rule defined ''community development financial institution'' and ''CDFI'' to include any institution that is certified by the CDFI Fund of the US Department of the Treasury, but excluded any bank or savings association that is insured under the Federal Deposit Insurance Act (12 U.S.C. 1811 *et seq.*) or a credit union that is insured under the Federal Credit Union Act (12 U.S.C. 1751 *et seq.*). The proposal excluded federally insured depository institutions and credit unions because they already were eligible for membership under the pre-HERA law. The final rule retains those aspects of the proposed definition, and also adds a new provision relating to bank or savings and loan holding companies that have been certified as CDFIs. The proposal did not include CDFI holding companies among the entities eligible for membership under the HERA amendments, and sought comment on that issue. One holding company, that has been certified as a CDFI and that controls a depository institution that is a member of a Bank, favored allowing similarly situated holding companies to become members in addition to the membership of their depository institution subsidiaries. That view was endorsed by another commenter, but several other commenters opposed allowing a bank or savings and loan holding company to obtain its own membership via the CDFI provisions. As a matter of general policy, FHFA believes that the benefits of Bank membership are best conveyed through depository institutions that have direct relationships with the communities in which they do business, and has decided not to allow depository institution holding companies to become Bank members at this time. FHFA intends to monitor the implementation of the CDFI membership provisions and is open to reconsidering this issue at a later date. FHFA notes, however, that there may be certain practical impediments to any holding company becoming a member, in addition to its depository institution subsidiaries, because a holding company would have to purchase its own membership stock in the Bank, in addition to any Bank stock owned by its subsidiaries. Moreover, the additional membership for the holding company would not necessarily provide any additional borrowing capacity beyond that already available to the subsidiary depository institution because current law allows a member to borrow against collateral owned and pledged by an affiliate. In the final rule, the definition of CDFI has been revised to make clear that holding companies for depository institutions cannot obtain membership via the CDFI membership provisions.

Community financial institutions. The proposed rule also carried over without change from the Finance Board regulations the definition of ''community financial institution.'' The Bank Act defines CFIs as FDIC-insured members that have average total assets of $1 billion or less, as adjusted annually for inflation. Section 1211 of HERA amended the Bank Act to allow CFIs to obtain long-term advances for the purpose of funding ''community development activities'' and further allowed CFIs to pledge secured loans for ''community development activities'' as collateral for their advances. As HERA authorized CDFIs to become members and separately authorized CFIs to pledge community development collateral, the proposal requested comment on whether there was any basis in the legislative history to HERA that would allow FHFA to construe the new CFI provisions as applying to CDFIs as well as to CFIs. Commenters addressing this issue overwhelmingly favored allowing CDFI members to be deemed to be CFIs so they could take advantage of the HERA amendments relating to community development collateral for CFIs, although no commenters identified anything in the legislative history to support that view. In the absence of any such evidence of Congressional intent, FHFA must give effect to the language that Congress actually has used in the Bank Act. That language allows an institution to be designated as a CFI, and thus benefit from the expanded collateral available to CFIs, only if it has FDIC deposit insurance and also has total assets less than the statutory amount. Because none of the newly-eligible CDFIs are insured by the FDIC, they cannot be CFIs and thus cannot either pledge community development loans as collateral or obtain long-term advances to support community development purposes. Accordingly, the final rule does not change the existing definition of CFI.

FHFA did not propose any revisions to the definitions of ''home mortgage loan,'' ''long-term,'' ''manufactured housing,'' or ''residential mortgage loan.'' Nonetheless, a number of commenters suggested that FHFA amend each of those provisions in certain respects to bring them more in line with the business of CDFIs generally or with the business of the commenters. Those provisions are discussed separately below.

Home mortgage loan. Some commenters asked that FHFA expand the definition of ''home mortgage loan'' to include certain other types of loans, such as loans secured by second liens, community acquisition loans (loans made to manufactured home communities), or pre-development or construction bridge loans. The Bank Act defines both ''home mortgage'' and ''home mortgage loan'' and FHFA cannot adopt a regulation that would include loans that would be precluded by the statutory definitions. The Bank Act defines a ''home mortgage loan'' as a loan made by a member upon the security of a home mortgage. It further defines a ''home mortgage'' as a mortgage upon real estate (held either in fee simple or a leasehold) on which one or more homes is located, and includes first mortgages and other types of first liens commonly used in the State where the real estate is located. 12 U.S.C. 1422(4) and (5). FHFA believes, for purposes of meeting the Bank Act standard, that an applicant must make long-term mortgage loans the existing definition of ''home mortgage loan'' in § 1263.1 is sufficiently expansive to accommodate loans typically made by CDFIs. Such loans as loans on one-to-four family properties, multifamily properties, residential properties that are partially used for business or farm purposes, or interests in long-term mortgages and mortgage pass-through securities backed by such mortgages qualify as home mortgage loans. FHFA is confident that most CDFIs would be able to meet the home mortgage loan eligibility requirements in the Bank Act.

Because the statute requires a ''home mortgage'' to be a first mortgage or other type of first lien, which requirement has long been in the Finance Board regulations, a loan secured by a subordinate lien cannot qualify as a ''home mortgage loan.'' Similarly, if a pre-development loan or construction bridge loan is not secured by real estate, or is secured by real estate that has no homes on it, then those loans also could not qualify as ''home mortgage loans'' under the statute. Whether other types of loans identified by the commenters may constitute ''home mortgage loans'' is largely a question of whether the particular types of loans at issue satisfy the statutory requirements noted above. FHFA believes that this issue is more appropriately addressed on a case-by-case basis, rather than by revisions to the regulatory definitions. In each such case, however, the inquiry will be the same, *i.e.,* whether the loan at issue is secured by a mortgage instrument, whether that instrument creates a first lien on real estate, and whether there are one or more homes or other dwelling units on the real estate at the time the loan is made and the security interest is created. If each of those questions can be answered in the affirmative, then the particular types of loans made by a CDFI applicant could qualify as ''home mortgage loans.'' To the extent that issues may arise about whether a particular type of loan made or held by a CDFI applicant in fact qualifies as a home mortgage loan, FHFA staff can assist the Banks and CDFI applicants in resolving that question on a case-by-case basis.

Long-term. The proposed regulation retained the existing definition of ''long-term,'' which meant a term-to-maturity of five years or greater. Some CDFI commenters noted that many CDFIs make short-term pre-development or construction bridge loans and requested that the definition of ''long-term'' be changed to accommodate these loan types. The phrase ''long-term'' appears only in four provisions of the proposed rules, just two of which—§§ 1263.6(a)(3) and 1263.9—are relevant to CDFI applicants. In each of those cases, the phrase modifies the term ''home mortgage loan.'' As noted above, ''home mortgage loan'' is also defined by statute and requires that the loan be secured by a first lien on real estate on which a home is located. To the extent that the pre-development or construction bridge loans are unsecured or are secured by property that has no homes on it, those loans would not qualify as home mortgage loans under the Bank Act irrespective of their maturity. Accordingly, the final rule does not change the definition of ''long-term.''

Manufactured housing. The existing regulation defines ''manufactured housing'' to mean a manufactured home as defined in section 603 of the National Manufactured Housing Construction and Safety Standards Act of 1974. This provision establishes safety and quality standards for the housing units. Some commenters proposed expanding the definition of ''manufactured housing'' and the definitions of ''one-to-four family property'' and ''multifamily property'' in § 1263.1 to accommodate real property loans for such uses as resident-owned manufactured housing cooperatives in which the land is owned in common or rented, and, to include real estate loans used to finance community facilities, infrastructure, and access roads within a manufactured housing complex. FHFA finds that for purposes of meeting the requirement in § 1263.9, the existing definitions of ''home mortgage loans,'' ''multifamily property,'' and ''one-to-four family property'' in § 1263.1 are adequate to accommodate real property loans to manufactured housing complexes where the property is used for residential purposes and dwellings are located on the property. Therefore, no change to the definition is necessary.

Residential mortgage loan. Certain CDFI commenters asked that FHFA revise the definition of ''residential mortgage loan'' to expressly include loans made to manufactured housing communities. The term ''residential mortgage loan'' appears only in two provisions of the membership regulations—§§ 1263.6(b) and 1263.10—both of which relate to the statutory requirement that federally insured depository institutions must have at least 10 percent of their assets in residential mortgage loans in order to become a member of a Bank. That 10 percent requirement applies only to depository institutions and thus is not relevant for CDFI members. Because any amendments to this definition would have no effect on the newly-eligible CDFIs, the final rule does not amend that provision.

C. Eligibility Requirements—Subpart C

The proposed rule would have carried over into part 1263 all of the existing provisions from Subpart C of the Finance Board regulations, which established the various eligibility requirements for Bank membership. Subpart C is made up of 13 separate sections, and the proposed rule would have carried over six of those sections without any substantive changes. The final rule adopts each of those six sections without any substantive change. Those unchanged provisions are §§ 1263.8 (which relates to the inspection and regulation requirement, and includes a nonsubstantive conforming change to the existing language), 1263.10 (which requires depository institutions to have 10 percent of assets in residential mortgage loans), 1263.13 (which relates to an applicant's home financing policy), 1263.14 (which relates to applicants that are de novo depository institutions), 1263.15 (relating to applicants that have recently merged) and 1263.18 (relating to which Bank an applicant may join).

Although FHFA did not propose to amend any of those provisions, certain commenters raised questions about them or asked that they be revised in certain respects. For example, a number of commenters asked that CDFI applicants not be required to demonstrate that they have 10 percent of their assets in residential mortgage loans in order to become Bank members. The provisions about which those commenters expressed concern are §§ 1263.6(b) and 1263.10, both of which implement section 4(a)(2)(A) of the Bank Act, which requires federally insured depository institutions to have at least 10 percent of their assets in residential mortgage loans as a condition to becoming a Bank member. The proposed rule did not subject the newly-eligible CDFI applicants (which are not federally insured depository institutions) to the 10 percent requirement, nor does the final rule.

Certain other commenters asked that FHFA revise § 1263.14, which establishes special procedures for de novo insured depository institutions, so that newly organized CDFIs could also have the benefit of those procedures. FHFA declines to amend § 1263.14 to accommodate newly organized CDFI applicants because the requirements for obtaining a depository institution charter and Federal deposit insurance are considerably more rigorous than are the processes for obtaining certification from the CDFI Fund. A de novo depository institution typically is allowed to commence business and obtain deposit insurance only after one or more bank regulatory agencies have determined that the institution is adequately capitalized, has a sound business plan, capable management, and can operate in a safe and sound manner. There is no comparable regulatory review for CDFIs; indeed, the regulations of the CDFI Fund expressly state that CDFI certification does not represent an assessment that the entity is financially viable. 12 CFR 1805.201(a). In the absence of any such

independent financial evaluation of the CDFI applicants, FHFA does not believe that they should be included within the provisions for de novo depository institutions.

With respect to each of the seven other sections located within Subpart C, the proposed rule included some substantive revisions, all of which were intended to implement the HERA amendments. In the final rule, FHFA is adopting certain of those provisions as proposed, but is revising other provisions in response to comments received on the proposed rule. Each of those sections is described separately below.

Section 1263.6—General Eligibility Requirements. Section 1263.6 of the proposed rule closely followed the requirements of section 4(a) of the Bank Act, which established the eligibility requirements for Bank membership. 12 U.S.C. 1424(a). That statutory provision lists the types of entities that are eligible to apply for membership, and then establishes several requirements that each entity must satisfy in order to be approved for membership. Certain of those statutory requirements apply to all applicants. Those requirements are located at section 4(a)(1)(A) through (C) and require that an applicant: (1) Is duly organized under Federal or State law; (2) is subject to inspection and regulation under Federal or State banking laws, or is a certified CDFI; and (3) makes long-term home mortgage loans. The other statutory requirements apply only to federally insured depository institutions, although the Finance Board also had long applied them to insurance company applicants, based on its authority to oversee the Banks to ensure that they operate in a safe and sound manner and carry out their housing finance mission. *See* 12 CFR 925.6(a)(4) to (6). Those other statutory provisions are located at section 4(a)(2)(B) through (C) and require that an applicant: (1) Be in sound financial condition so that a Bank may safely make advances to it; and (2) have a character of management and a home financing policy that are consistent with sound and economical home financing. That Finance Board regulation also included a requirement that any applicant that is not an insured depository institution must have mortgage-related assets that reflect a commitment to housing finance, as determined by the Bank in its discretion. 12 CFR 925.6(c).

In § 1263.6 of the proposed rule, FHFA made only one substantive change to the Finance Board regulations, which was to add CDFIs to the list of entities that are eligible for membership. As a result, the proposed rule would have required CDFI applicants to comply with each of the three eligibility requirements imposed by section 4(a)(1) of the Bank Act, *i.e.,* duly organized, certified, and making home mortgage loans, as well as with the regulatory requirements relating to financial condition, character of management, and home financing policy. The proposed rule also retained the requirement that applicants that are not insured depository institutions must have mortgage-related assets that reflect a commitment to housing finance, and relocated it to § 1263.6(c). FHFA stated that it expected the Banks to assess the commitment to housing finance requirement in light of the unique community development orientation of CDFI applicants.

In the final rule, FHFA has retained the language of the proposed rule regarding the general eligibility requirements, but has also made certain further revisions in response to the comments. In paragraph (a), FHFA has added a clarifying parenthetical reference to CDFI credit unions. In paragraph (a)(1), FHFA has added a reference to ''Tribal law.'' Certain commenters had suggested this revision in order to allow CDFIs that are organized under the laws of Tribal governments to become members, which FHFA believes is permissible under the statute and is consistent with the intent of Congress. In paragraph (a)(2), FHFA has added a reference to certified CDFIs, to make clear that the ''inspection and regulation'' eligibility requirement does not apply to a CDFI applicant, which need only demonstrate that it has been certified by the CDFI Fund.

With respect to the requirement that applicants other than insured depository institutions must have mortgage-related assets that reflect a commitment to housing finance, FHFA is also retaining that provision in the final rule without change. The term ''mortgage-related assets'' is not defined, and FHFA believes that the term can be construed broadly in considering whether a CDFI applicant meets this requirement. Moreover, the regulations do not require that a CDFI applicant's assets be exclusively, or even predominantly, oriented to traditional housing finance. What is required is that the CDFI applicant has assets that, when viewed in the overall context of the applicant's business and how it provides products and services to its targeted markets, can be fairly said to support housing finance. Because CDFI applicants are apt to have asset profiles that differ from those that the Banks typically review, FHFA expects that the Banks will consider the assets of CDFI applicants in light of their unique products and mission. Thus, although a CDFI may be able to demonstrate its commitment to housing finance through traditional means, such as by originating mortgage loans or otherwise to supporting the development or acquisition of housing, it also may demonstrate its commitment through other means. Examples of such other means would include, but are not limited to, loans related to manufactured housing (regardless of whether the unit is deemed to be real estate), pre-development or construction loans for real estate that will become or include residential property, or loans secured by subordinated liens on residential real estate.

Section 1263.7—Duly Organized Requirement. Section 4(a)(1)(A) of the Bank Act requires an applicant to be duly organized under the laws of any State or of the United States. 12 U.S.C. 1424(a)(1)(A). The regulations of the Finance Board provided that an applicant would be deemed to be duly organized if it is chartered by a State or Federal agency as one of several types of entities eligible for Bank membership. In the proposed rule, FHFA retained the existing language from the Finance Board regulation and added new language providing that being incorporated under State law would be sufficient for a CDFI to demonstrate that it is duly organized. As noted in the prior section, several commenters asked that FHFA also allow CDFIs that are organized under Tribal law to be deemed to be duly organized, and the final rule includes an additional reference to Tribal law to clarify that a CDFI that is incorporated under State or Tribal law is deemed to satisfy the statutory requirement.

Section 1263.8—Subject to Inspection and Regulation Requirement. Section 4(a)(1)(B) of the Bank Act generally requires an applicant for membership to be subject to inspection and regulation under State or Federal banking or similar laws. In the case of a CDFI, the statute imposes an alternative requirement, which is that the applicant be certified by the CDFI Fund. *See* 12 U.S.C. 1424(a)(1)(B). The proposed rule simply carried over the language from the Finance Board regulations without any changes. Nonetheless, several commenters asked that the final rule make clear that a CDFI applicant is not subject to the inspection and regulation requirement because of the alternative requirement noted above. FHFA agrees that clarification of this issue is appropriate and has addressed that

matter in both the general eligibility provisions of § 1263.6(a)(2) of the final rule, which states that an applicant must be either subject to inspection and regulation by a regulatory agency or be certified as a CDFI by the CDFI Fund, and in § 1263.8, which states that a certified CDFI is not subject to the ''inspection and regulation'' requirement.

Section 1263.9—Makes Long-Term Mortgage Loans Requirement. As noted previously, section 4(a)(1)(C) of the Bank Act requires that every applicant for membership, including CDFIs, must make such home mortgage loans that the Director determines to be ''long-term loans.'' 12 U.S.C. 1424(a)(1)(C). The regulations of the Finance Board presumed that an applicant had satisfied that requirement if the regulatory reports that it filed with its regulator showed that it originates or purchases long-term home mortgage loans. Section 1263.9 of the proposed rule carried over the substance of the Finance Board regulation, with some modifications to accommodate CDFI applicants. Under that provision of the proposed rule, a CDFI applicant also would have been presumed to have satisfied that requirement if it provides to the Bank other documentation showing that the applicant originates or purchases long-term home mortgage loans.

In the final rule, FHFA is adopting this provision without change. Because certain commenters sought FHFA guidance on how the Banks are to apply this provision, as well as the other provisions relating to an applicant's home financing policy and its commitment to housing finance, FHFA is providing such guidance in this preamble. Although it is clear that a CDFI applicant must originate or purchase long-term home mortgage loans in order to become a member, the Bank Act and the implementing regulations do not set a minimum threshold for the amount of home mortgage loans that an applicant must make in order to satisfy that requirement. Similarly, neither the statute nor the regulations characterize this as an ongoing requirement for membership.

Given the differences between the business of a typical depository institution and that of a typical CDFI, the amount of home mortgage loans that a CDFI applicant originates or purchases will likely be considerably less than the amount that a similarly sized depository institution would originate or purchase. FHFA expects that in assessing a CDFI applicant's compliance with this ''makes long-term home mortgage loans'' requirement the Banks will view the extent to which the CDFI originates or purchases long-term home mortgage loans in light of their unique mission and community development orientation, and thus will deem such applicants to have satisfied this requirement if they in fact have originated or purchased home mortgage loans and can document that fact. Moreover, an applicant's compliance with this provision need be assessed only at the time that a CDFI applies for membership. This approach is consistent with how the Banks assess compliance with section 4(a)(2)(A) of the Bank Act, which requires certain insured depository institution applicants to have at least 10 percent of their assets in ''residential mortgage loans.''

In an earlier portion of this preamble FHFA discussed in some detail the definitions of the terms ''home mortgage loan'' and ''long-term'' as they are used in the context of the membership regulations. As discussed earlier, FHFA believes that for purposes of meeting the ''makes long-term home mortgage loans'' requirement the definition of home mortgage loans in § 1263.1 is sufficiently expansive to accommodate loans typically made by CDFIs, such as loans on one-to-four family properties, multifamily properties, residential properties with business components, interests in long-term mortgages, and mortgage pass-through securities backed by such mortgages.

Section 1263.11—Financial Condition Requirement for Depository Institutions and CDFI Credit Unions. The proposed rule included two separate provisions for evaluating the financial condition of CDFI applicants: § 1263.11, which related to CDFI credit unions, and § 1263.16, which related to all other types of CDFIs. The proposal defined ''CDFI credit unions'' as State-chartered credit unions that have been certified as CDFIs but do not have Federal share insurance. Because the Finance Board had previously adopted regulations for evaluating the financial condition of all depository institution applicants, including State-chartered credit unions with NCUA share insurance, FHFA proposed to require CDFI credit unions to comply with the same regulations under which all other depository institution applicants are evaluated. In brief, the proposal would require the Banks to evaluate the financial condition of CDFI credit unions based on information in the regulatory financial reports they file with their applicable regulators, their audited financial statements, and the examination reports prepared by their regulators. Although CDFI credit unions do not file financial regulatory reports with the NCUA, they do file comparable reports with their appropriate State regulator, and FHFA believes that those documents may be used to assess the financial condition of the CDFI credit unions. The proposed rule would have amended the Finance Board's regulatory text in two respects—by adding CDFI credit unions to the list of institutions that are subject to § 1263.11, and by requiring all CDFI credit unions to meet certain performance trend criteria.

These provisions of the proposed rule generated few comments, and FHFA is adopting § 1263.11 as proposed. One commenter asked that FHFA revise the ''earnings'' provision of the regulation to require a CDFI credit union to demonstrate positive earnings for two of the last three years, rather than for four of the six most recent calendar quarters, as was in the proposed rule. As noted above, the financial condition requirements for CDFI credit unions are essentially identical to those of the Finance Board regulations, which the Banks have long used to evaluate the condition other depository institutions that apply for membership. FHFA believes that those requirements are well understood by the Banks and by depository institutions generally, and does not believe that there is a compelling reason to alter the earnings requirement solely for the benefit of CDFI credit union applicants. Moreover, to revise the regulation in the manner requested would change the earnings analysis for all other depository institution applicants, which FHFA does not believe is warranted.

A few commenters, including those representing State-chartered credit unions, objected to the provisions of the proposed rule that would have required all CDFI credit union applicants to meet certain performance trend criteria. For all other depository institution applicants, those performance trend criteria apply only if the applicant has received a composite regulatory examination rating of ''2'' or ''3.'' FHFA did not receive comments from any prospective CDFI credit union member on this proposal. As was stated in the proposed rule, CDFI credit unions are not subject to oversight by the NCUA and have not previously been eligible for membership. As a result, the Banks may be less familiar with State examination processes and ratings, and FHFA believes that it is prudent to require all CDFI credit unions to demonstrate that their earnings, nonperforming assets, and allowance for loan and lease losses are consistent with the existing performance criteria. Thus,

the final rule adopts the language of the proposed rule on this issue without change.

Section 1263.12—Character of Management Requirement. The proposed rule carried over all of the substance of the Finance Board regulation relating to the character of management standard and added a separate paragraph for assessing the management of all CDFI applicants other than CDFI credit unions. Under the proposed rule, the character of a CDFI applicant's management would be deemed to be consistent with sound and economical home financing if the applicant provides the Bank with an unqualified written certification that neither the applicant nor its senior officials are subject to any enforcement actions, criminal, civil or administrative proceedings, or criminal, civil or administrative monetary liabilities, lawsuits or judgments. The proposed rule would have required CDFI credit unions to comply with the existing provisions applicable to depository institutions generally, but would have imposed slightly different standards on other types of CDFIs, such as loan funds and venture capital funds, because they are not regulated and thus are not subject to regulatory examinations or administrative enforcement actions. This provision of the proposed rule did not generate any significant comments and is being adopted in final form without change.

Section 1263.13—Home Financing Policy Requirement. Section 4(a)(2)(C) of the Bank Act provides that any insured depository institution applicant must have a home financing policy that is consistent with sound and economical home financing. Although the Bank Act applies this requirement only to depository institutions, the Finance Board regulations have applied it to all entities applying for Bank membership. *See* 12 CFR 925.6(a)(6). The Finance Board regulations provide that an insured depository institution applicant may be deemed to have satisfied the statutory requirement if it has a satisfactory Community Reinvestment Act (CRA) rating, but requires that applicants not subject to the CRA file with the Bank a written justification showing how and why their home financing policy is consistent with the housing finance mission of the Bank System. *Id.* at 925.13.

FHFA did not propose any changes to the Finance Board regulation, and stated that CDFI applicants would be required to provide a written justification, acceptable to the Bank, explaining how and why their home financing policy is consistent with the Bank System's housing finance mission. Certain commenters asked that CDFI applicants be presumed to comply with this requirement by virtue of their certification from the CDFI Fund. Although some certified CDFIs may in fact have a housing finance orientation that would satisfy this requirement, that will not necessarily be the case for every CDFI that is certified by the CDFI Fund, given the potential variety of activities in which a CDFI may engage. Because not all CDFIs will have the same degree of involvement in housing finance activities, FHFA believes that the better approach is to have the Banks assess the housing finance policies of the CDFI applicants on an individual basis, which is what the proposed rule required. Accordingly, a CDFI applicant must provide to the Bank a written narrative describing the manner in which the CDFI supports housing finance generally, which may include direct support such as originating loans, as well as indirect support through other investments, activities, or services. FHFA believes that this should not be a burdensome requirement for most CDFI applicants, as they are likely to have some direct or indirect nexus to housing finance in their communities. Thus, FHFA expects that most CDFI applicants can readily demonstrate that their business operations and housing finance policies are consistent with the mission of the Bank System, which includes both traditional housing finance as well as other community investment activities.

Section 1263.16—Financial Condition Requirement for Insurance Company and Certain CDFI Applicants. In the proposed rule, FHFA included new provisions for evaluating the financial condition of CDFI applicants. The provisions for evaluating CDFI credit unions were located in § 1263.11 and were discussed earlier in this document. The provisions for evaluating all other types of CDFI applicants, such as loan funds and venture capital funds, were located in § 1263.16(b) of the proposed rule. Those new provisions were similar in substance to the provisions relating to depository institutions, although their specific requirements differed somewhat, in recognition of the differences between depository institutions and the newly-eligible CDFIs. The structure of proposed § 1263.16(b) generally paralleled that of the provisions used for depository institutions, *i.e.,* the regulation identified the types of financial documents that a Bank must review in assessing a CDFI applicant's financial condition and established standards for determining whether the financial condition of a particular applicant was such that a Bank could safely make advances to the applicant. These provisions of the proposed rule generated a significant number of comment letters, which raised a variety of issues relating to the manner in which the Banks were to assess the financial condition of CDFI applicants. The following paragraphs address the various provisions of § 1263.16(b) in the order they appear within the regulation, and describe key aspects of the proposal, the comments, and the approach taken in the final rule.

Review requirement. Section 1263.16(b)(1) of the proposed rule required a Bank to obtain certain specified financial statements from each CDFI applicant, as well as its certification from the CDFI Fund, and any other information the Bank deemed necessary to assessing the applicant's financial condition. In the introductory language for this provision, the proposed rule restated language from the regulations of the Finance Board for depository institution applicants, which stated that a Bank ''shall obtain'' certain information from an applicant in assessing its financial condition. In the final rule, FHFA has revised that language to state that an applicant ''shall submit'' the required information, which is intended to make clear that an applicant must provide a Bank with sufficient information for the Bank to make an informed assessment of the applicant's financial condition. The final rule also adds a new requirement to this introductory language, which provides that a Bank shall consider all information provided by a member before deciding whether to approve or deny the membership application. This change relates to the standards established by § 1263.16(b)(2), which are presumptive indicators of an applicant's compliance with the requirement that it be in sufficiently sound financial condition that a Bank can safely make advances to it. Under the proposed rule, an applicant's failure to comply with one or more of the presumptive standards does not mean that the applicant cannot become a member of a Bank. Instead, it means that the applicant must overcome the presumption of noncompliance by providing the Bank with additional information demonstrating that the applicant is indeed in sufficiently sound financial condition to obtain advances from the Bank. The processes for rebutting such presumptions of noncompliance are established by § 1263.17, which applies to all types of

applicants. The new requirement added to the introductory language of § 1263.16(b)(1) is intended to ensure that a Bank does not automatically deny membership to a CDFI applicant based solely on that applicant's failure to satisfy any of the presumptive standards. It also is intended to make clear that a CDFI applicant has a right to submit additional information, beyond that required by the regulation, to demonstrate that it is in sound financial condition and to have that information considered by the Bank before it decides whether to approve the application.

The above revisions are intended to work in tandem with additional new language that the final rule adds to § 1263.16(b)(1)(iii). As proposed, that provision would have required an applicant to provide any additional information relating to its financial condition that is requested by the Bank. Because of the possibility that some CDFI applicants may not satisfy one of the presumptive standards, but may nonetheless be in sound financial condition, FHFA believes that it is important to make clear in the regulation that each CDFI applicant has the right to submit whatever information that it believes demonstrates its financial condition, regardless of whether the Bank has asked for such information. For example, if a CDFI applicant would not satisfy the net asset ratio requirement, it could submit additional information as part of its initial membership application demonstrating that its financial condition is sufficiently sound to satisfy the regulatory requirement, notwithstanding its failure to satisfy the presumptive standard. If the information in fact demonstrates that the applicant's financial condition is sufficiently sound to borrow from the Bank, FHFA expects that the Bank would approve the membership application.

The revisions described above are the only substantive amendments that the final rule makes to § 1263.16(b)(1). As to the particular financial statements that must be submitted, § 1263.16(b)(i) of the proposed rule would have required CDFIs to submit financial statements audited under generally accepted auditing standards (GAAS), as well as more recent quarterly financial statements, if those are available. An applicant also was required to submit financial statements for the two years prior to the most recent audited financial statements. At a minimum, all such financial statements must include income and expense statements, statements of activities, statements of financial position, and statements of cash flows. The financial statements for the most recent year also would have to include detailed disclosures or schedules relating to the affiliates of the CDFI applicant regarding the financial position of each affiliate, their lines of business, and the relationship between the affiliates and the applicant CDFI. There were no objections from commenters to this requirement and it is retained in the final rule. FHFA believes that in most cases a GAAS audited statement will suffice to show evidence of financial condition and anticipates that the Banks will be judicious in the amount of additional information they require CDFI applicants to submit. The proposed rule also asked whether CDFIs that do not typically obtain audited financial statements should be permitted to submit an alternative financial statement. Some commenters representing both the CDFI sector and the Banks recommended that in addition to an audited statement, a CDFI applicant be permitted to submit an alternative third party assessment, such as the CDFI Assessment and Rating System (CARS™) assessment. The final rule does not require the submission of a CARS™ statement or other similar documents. In light of the revisions made to § 1263.16(b)(1)(iii), which allows a CDFI applicant to provide the Bank with any information the applicant believes relevant to its financial condition, FHFA does not believe that the final rule needs to specify by name any other types of documents to be submitted.

The proposed rule also required any CDFI applicant that had been certified more than three years prior to applying for membership to submit to the Bank a written statement certifying that it had not undergone any material events that would adversely affect its strategic direction, mission, or business operations. Some commenters asked that the final rule be revised to require any such CDFI applicants to obtain a re-certification from the CDFI Fund in order to be admitted to membership, but FHFA has not included a re-certification requirement in the final rule. As an initial matter, the Bank Act requires only that a CDFI must have been ''certified'' by the CDFI Fund in order to be eligible for membership, and does not speak to how long ago the certification must have been obtained. Under the regulations of the CDFI Fund, a certification appears to remain effective unless the CDFI Fund rescinds the certification, such as if it finds that a CDFI no longer meets the certification requirements. 12 CFR 1805.201(a). Moreover, the regulations of the CDFI Fund do not provide a means by which an entity that has been previously certified, can routinely obtain re-certification for purposes unrelated to the CDFI Fund, such as applying for Bank membership. There does not appear to be any way for a certified CDFI to obtain routine re-certification; therefore FHFA believes that requiring submission of a written statement attesting to the absence of any material adverse events is an appropriate means of providing some assurance that an applicant has not done anything to jeopardize its standing as a CDFI. Indeed, in the absence of a means of obtaining routine re-certification from the CDFI Fund, a provision mandating re-certification as a condition of membership could effectively frustrate the intent of Congress to allow CDFIs to become Bank members.

Financial condition standards. Section 1263.16(b)(2) of the proposed rule sets out four presumptive standards that a CDFI applicant must satisfy in order to be deemed to satisfy the financial condition requirement of § 1263.6(a)(4), *i.e.,* that an applicant's condition is such that a Bank can safely make advances to it. The four presumptive standards related to an applicant's compliance are net asset ratio, earnings, loan loss reserves, and liquidity. These provisions generated a significant number of comments and suggested revisions, which FHFA has considered in developing the final rule. The final rule generally retains the standards of financial condition that were in the proposed rule, but also includes some revisions based on the suggestions of the commenters. Each of the provisions relating to the four presumptive standards is discussed separately below.

Net asset ratio. The proposed rule would have required that a CDFI applicant have a ratio of net assets to total assets of at least 20 percent, with net and total assets including restricted assets, where net assets is calculated as the residual value of assets over liabilities and is based on the information derived from the applicant's most recent financial statement. In the absence of independent regulatory examinations for this group of CDFIs, the proposed financial condition requirements for Bank membership were based on accepted prudential standards, *i.e.,* the net asset ratio mirrored the ''Financial Ratios of Minimum Prudent Standards'' used by the CDFI Fund, which prescribes a minimum net asset ratio of 20 percent (or .20). The 20 percent

standard also was subjected to peer benchmarking. A survey of 130 loan fund CDFIs conducted in 2002 found that the median net asset ratio to be .437 and the mean ratio to be .446.[2] Similarly, the CDFI Fund reported that during the period between 2003 and 2005, non-depository CDFIs had a net asset ratio of ''about 40 percent''.[3] These ratios are higher than the 20 percent net asset ratio threshold in the proposed rule.

The preponderance of CDFI sector commenters objected to the 20 percent net assets ratio in the proposed rule as too high. Several CDFI commenters called on FHFA to reduce the net asset ratio to not greater than 10 percent. These commenters argued that a 10 percent net asset ratio would be in line with the standards used by the Federal regulators for a well-capitalized federally insured credit union and suggested that FHFA adopt internal capital ratios similar to those applicable to FDIC-insured institutions.

FHFA believes that the capital composition of CDFIs and insured depositories, respectively, reflect different institutional models and are not directly comparable. The variations in CDFI sources of revenue and capital do not readily permit classifications comparable to those used by depository institutions. For example, a CDFI's assets may include: (1) Unrestricted net assets, which are assets available for use by the CDFI without encumbrance; (2) designated net assets, which have been designated by a CDFI board for a specific purpose and can become undesignated; (3) temporarily restricted net assets, which are assets that cannot be released without prior agreement from the donor but can be converted to unrestricted capital upon satisfaction of donor requirements; and (4) permanently restricted net assets that have financial covenants that cannot be removed, except, in some cases during liquidation of assets pursuant to insolvency.

The terms of grant and investor covenants also can affect the permanency of capital. In addition, the components of capital will also vary from one nonprofit CDFI to another. For example, a unique characteristic of CDFI loan funds is their use of a debt-as-equity instrument known as Equity Equivalent Investments or ''EQ2.'' The EQ2 represents a small fraction (5 percent) of the aggregate capital of all loan funds.[4] Regulated financial institutions investing in CDFIs are attracted to EQ2 investments because regulators treat EQ2 investments in a CDFI as eligible in meeting the requirements of the CRA. The EQ2 loans are deeply subordinated to all other debt; carry a rolling term; limit the rights of the investor to call the investment; and, carry interest that is independent from income. The EQ2 are included as capital in CDFI financial statements. This treatment increases capital ratios and enables a CDFI to access capital at lower rates.

FHFA recognizes that a CDFI's balance sheet and financial ratios may vary depending on the line of financial products and services that it offers. A CDFI active in lending might be more leveraged than a service-oriented CDFI and this could result in a lower net asset ratio. Such a finding does not by itself indicate declining financial performance or that the financial condition of the CDFI is not sufficiently sound to allow the Bank to safely make advances to it. Further, the CDFI specializing in lending might have more experience in asset-liability management. In fact, data show that as a CDFI grows and matures it will have lower net asset ratios than those of emerging CDFIs.[5] It is likely that these organizations have become more active lenders and less dependent on grants. More recently, however, there is evidence that financial distress among CDFI investors, such as insured depositories and grant makers, has resulted in reduced investments in CDFIs, lowering the CDFIs' equity and thus affecting their net asset ratios.[6]

Recognition of these varying conditions notwithstanding, FHFA is not inclined to accept the recommendations made by the commenters that the minimum net asset ratio should be reduced, either to equal the capital ratios of insured depositories or to some other value between 10 percent and 20 percent. In the absence of regulatory standards and comprehensive examinations of the CDFIs, there is no good way for FHFA to establish the merit of one particular numerical ratio over another. Moreover, the 20 percent net asset ratio is consistent with the experience of the CDFI Fund, and appears well below the levels documented in the peer benchmarking studies described earlier. In light of those factors, FHFA decided to retain the requirement in the proposed rule that a CDFI applicant must demonstrate a 20 percent net asset ratio in order to satisfy the presumptive standard. FHFA emphasizes, however, that the revisions to § 1263.16(b)(1) are intended to allow an applicant that does not meet any of the presumptive standards, including the 20 percent threshold, to provide additional evidence of its financial condition and have the Bank consider that information prior to acting on the application. Moreover, FHFA intends to monitor the Banks' implementation of this rule, including their assessment of additional information provided by any applicant that does not initially meet one of the presumptive standards.

Earnings. Under the proposed rule, the applicant would have been required to show a positive net income for any two of the three most recent years, where net income is calculated as gross revenues less total expenses and is based on information derived from the applicant's most recent financial statement. Most commenters supported the standard in the proposed rule as reasonable measure of a CDFI's earnings, but a number of CDFIs and CDFI trade associations proposed revising this provision to allow applicants to use a rolling three-year average to demonstrate that they have achieved a pattern of positive net income over that time. Those commenters favored this method because it recognizes fluctuations on a CDFI balance sheet resulting from newly received and expiring grants. The rolling three-year average method is also consistent with the methods used by some grantors. FHFA believes that these suggestions have merit and has amended the final rule to delete the requirement that an applicant show positive net income in two of the most recent three years and replaced it with a requirement that an applicant have positive income on a rolling three-year average basis.

Loan loss reserves. The proposed rule included a requirement that an applicant's ratio of loan loss reserves to loans and leases 90 days or more delinquent (including loans sold with full recourse) be at least 30 percent, where loan loss reserves are a specified balance sheet account that reflects the amount reserved for loans expected to

[2] Lam, Marcus *et al.* ''Recommendations for CDFI Performance Measurement.'' *See* Table 2.1 based on data obtained from the Opportunity Finance Network's CDFI Project. Unpublished document, March 2002.

[3] United States Department of the Treasury, CDFI Fund, ''*Three-year Trend Analysis of Community Investment Impact System Institutional Level Report Data FY 2003–2005*'' at 47. *See http://www.cdfifund.gov/impact_we_make/ciis/CDFI3yearTrend.pdf.*

[4] CDFI Data Project 2007.

[5] *See* CDFI Fund, *Three Year Trend Analysis* at 47.

[6] *See* Opportunity Finance Network, ''*CDFI Market Conditions Report: Fourth Quarter 2008*'', (April, 2009). *See* ''*The Economic Crisis and Community Development Finance: An Industry Assessment*'', Community Development Investment Center Working paper Series, Federal Reserve Bank of San Francisco, (May 2009).

be uncollectible and are based on information derived from the applicant's most recent financial statement. FHFA proposed the 30 percent threshold, which is half the reserve requirement that applies to depository institution applicants, in recognition of the historically low delinquency rate among CDFI-originated loans and the willingness and ability of CDFIs to work with borrowers to modify loans. Generally speaking, CDFI loans have performed as well or better than prime loans, and FHFA believed that it was appropriate for the loan loss reserve standard to recognize that difference.

Notwithstanding that, FHFA explained its rationale for the 30 percent requirement in the proposed rule, a number of commenters serving or representing depository institutions stated that the 30 percent figure was too low and recommended that it be increased to 60 percent, the same as it is for depositories. For the same reasons that were cited in the proposed rule, FHFA believes that the 30 percent figure is appropriate for CDFI applicants, and that increasing the ratio to 60 percent would not take into consideration the default experience for CDFI loans. One CDFI commenter recommended lowering the reserve ratio to 20 percent, in recognition that nonprofit institutions typically work with borrowers to modify loans. In light of current economic conditions affecting all lenders, FHFA believes that a 20 percent reserve may be too low and is not prepared to accept that suggestion, though it notes that any CDFI applicant not meeting the 30 percent requirement could provide the Bank additional information demonstrating why, in the context of the business conducted by that CDFI, its level of loan loss reserves is consistent with the concept of operating in a sound financial condition. Accordingly, the final rule adopts the loan loss reserve standard exactly as it was proposed.

Liquidity ratio. The proposed rule included a standard requiring a CDFI applicant to have an operating liquidity ratio of at least 1.0 for the current year, and for one or both of the two preceding years, where the numerator of the ratio includes unrestricted cash and cash equivalents and the denominator of the ratio is the average quarterly operating expense for the four most recent quarters. FHFA believes that this liquidity ratio provides a measure of funds available to pay creditors by requiring a CDFI to have sufficient liquidity to cover its average operating expenses for one quarter. The preponderance of commenters supported the liquidity ratio in the proposed rule, and one commenter suggested that the final rule replace the reference to ''current year'' with a reference to the ''four most recent quarters.'' FHFA agrees with that suggestion and has incorporated it into the final rule. In all other respects, the final rule is identical to the proposed rule on this topic.

Self-sufficiency or sustainability ratio. The proposed rule sought comment on whether FHFA should incorporate into the final rule a requirement that a CDFI applicant have a minimum self-sufficiency or sustainability ratio, *i.e.,* a ratio used to evaluate the extent to which a CDFI can cover its expenses from earned revenue and, by inference, the CDFI's independence from grants and loans. FHFA acknowledged in the proposed rule that self-sufficiency ratios can be affected by the type of services and grant programs operated by the CDFI, and thus may not adequately portray a CDFI's financial condition. Moreover, if a self-sufficiency ratio for Bank membership were to be too stringent, it could conflict with the service delivery requirements for a CDFI to become certified by the CDFI Fund. *See* 12 U.S.C. 4701(b). Most of the commenters addressing this issue believed that a self-sufficiency ratio was not necessary, though some commenters did advocate for its inclusion. Given the above-described concerns and the absence in the comments of any compelling reasons for adopting a self-sufficiency requirement, FHFA does not include one in the final rule.

Section 1263.17—Rebuttable Presumptions. The membership regulations of the Finance Board had long included a series of presumptive standards, under which an applicant that satisfied a particular standard would be presumed to have satisfied the underlying statutory or regulatory requirement to which the standard related. For example, those regulations presumed that an insurance company applicant that was subject to inspection and regulation by a State regulator that is accredited by the National Association of Insurance Commissioners had satisfied the statutory ''inspection and regulation'' requirement of 12 U.S.C. 1424(a)(1)(B). *See* 12 CFR 925.8. In the event that an insurance company applicant was not regulated by an accredited agency, and thus had failed to meet the presumptive standard, other provisions of the regulations allowed the applicant to rebut the presumption of non-compliance by providing the Bank with ''substantial evidence'' that it in fact could satisfy the statutory requirement notwithstanding the lack of accreditation for its regulator. *See* 12 CFR 925.17(c). In the proposed rule, FHFA retained this framework, with certain modifications to proposed § 1263.17 to accommodate CDFI applicants. In effect, the proposed rule would have applied the presumptive compliance and rebuttal provisions to CDFI applicants in the same manner that they apply to other applicants.

Certain commenters objected to this arrangement, apparently on the mistaken belief that the presumption and rebuttal structure of the regulation disadvantaged CDFI applicants by presuming that they had not satisfied one or more of the requirements for membership. In the final rule FHFA retains the presumption and rebuttal provisions as proposed. Each of the regulation's presumptive standards for Bank membership is linked to one of the statutory or regulatory requirements that each applicant must satisfy in order to become a Bank member. An applicant that satisfies a presumptive standard is presumed to have satisfied the underlying statutory or regulatory requirement and need do nothing more with respect to that requirement.

An applicant that does not satisfy a presumptive standard, however, is not conclusively determined to have failed to satisfy the underlying requirement. Instead, the regulation effectively requires an applicant to go through a somewhat more rigorous process before a Bank can determine that the applicant in fact has satisfied the underlying membership requirement. FHFA believes that this level of scrutiny is appropriate because Congress has established certain requirements for membership that each applicant must satisfy in order to become a member and FHFA has a responsibility to ensure that the Banks admit to membership only those applicants that have satisfied all applicable requirements for membership. FHFA also believes that this arrangement ultimately works to the benefit of an applicant because it provides an opportunity to present whatever additional documentation an applicant believes relevant to satisfying a particular requirement for membership. As a practical matter, FHFA also notes that the addition of the new provisions into § 1263.16(b)(1)(ii) and (b)(1)(iii), which allow CDFI applicants to submit as part of their original membership application whatever information they believe relevant to their application, and gives CDFI applicants an opportunity to address any such issues at the beginning of the application process, which should lessen the likelihood that a CDFI applicant will need to rely on the rebuttal provisions of § 1263.17.

D. Community Support Amendment—Part 944

Section 10(g) of the Bank Act requires FHFA to adopt regulations establishing standards of community investment or service for members of the Banks to maintain continued access to long-term Bank advances. That section further provides that the regulations shall take into account factors such as a member's performance under the CRA and the member's record of lending to first-time homebuyers. 12 U.S.C. 1430(g)(1) and (2). In the proposed rule, FHFA stated its belief that a CDFI member should be able to comply with the existing community support regulations but also requested comments on whether FHFA should develop an alternative community support regulation for CDFIs that recognizes their unique mission and business practices. The comments received on this issue were split, with some advocating a revision to the community support regulations to accommodate CDFI members and others expressing the view that most CDFI members should be able to satisfy the requirements of the existing community support regulations. After consideration, FHFA decided to amend the community support regulations to add provisions in the final rule that deem a CDFI member (other than a depository institution or credit union) to have satisfied the statutory community support if it is certified by the CDFI Fund. The substance of the new provisions and FHFA's rationale are set out below.

The existing Finance Board regulations implementing the community support requirement are located at 12 CFR part 944, and incorporate the two factors cited by the statute, *i.e.,* the CRA and the record of lending to first-time homebuyers. Under these provisions, a Bank member that is subject to the CRA is deemed to meet the CRA standard if its most recent CRA evaluation is ''outstanding'' or ''satisfactory.'' *See* 12 CFR 944.3(b)(1). A member also is presumed to meet the first-time homebuyer lending standard if its CRA evaluation is ''outstanding'' and there are no public comments or other information to the contrary. 12 CFR 944.3(c). Members that are not subject to the CRA, such as credit unions and insurance companies, are only required to meet the first-time homebuyer lending standard. *Id.* Because the newly-eligible CDFIs are not subject to the CRA, they too would only be subject to the first-time homebuyer lending standard if they were to be subject to the existing regulations. Section 944.3(c)(1) includes a non-exclusive list of eligible activities that meet the first-time homebuyer lending standard, such as having an established record of lending to first-time homebuyers, providing homeownership counseling programs for first-time homebuyers, providing or participating in marketing plans and related outreach programs targeted to first-time homebuyers, and providing technical assistance or financial support to organizations that assist first-time homebuyers. *See id.* at 944.3(c)(1).

When the Finance Board adopted the current community support regulations, it construed the statutory provisions narrowly and described the references to the CRA and first-time homebuyers as ''mandatory statutory factors.'' *See* 61 FR 60229, 60230 (November 27, 1996) (proposed rule). At that time, however, the Bank Act did not authorize CDFIs to become Bank members, and the Finance Board did not consider the issue of how the community support requirements should be applied to CDFIs, which are not subject to the CRA and may not be as actively involved in first-time home buyer activities as are depository institutions. In light of the HERA amendments, FHFA reconsidered that interpretation and determined that it need not construe the references to the CRA and first-time home buyers as ''mandatory factors'' for all members. FHFA believes that it has the authority under section 10(g) of the Bank Act to adopt different community support standards for particular categories of members if it believes that the circumstances warrant such a difference. With respect to certified CDFI members, FHFA believes that the circumstances warrant that they be treated differently from depository institution and insurance company members with respect to the community support requirements and is including in the final rule revisions to the community support regulations to deal with certified CDFI members.

Section 10(g) of the Bank Act mandates that FHFA adopt regulations that establish standards of community investment or service for the members of the Banks. That mandate appears clearly intended to encourage members to be engaged in providing community investments and services by making their access to long-term advances dependent on how involved they are in those activities. That approach makes eminent sense, in the case of depository institutions and insurance companies, because the principal focus of the business of such entities may well involve activities that do not have a community orientation. In the case of CDFIs, however, the principal, and in some cases the exclusive business focus is on community oriented services and investments. Indeed, in order to become certified by the CDFI Fund a CDFI must by statute have a primary mission of promoting community development, serve an investment area (which is a geographic area that meets certain criteria of economic distress), and provide development services (which are activities that promote community development and are integral to lending or investment activities) in conjunction with equity investments or loans. 12 U.S.C. 4702(5)(A). Given that a principal reason certified CDFIs exist is to promote economic revitalization and community development through investments and other services within their local communities, *see* 12 U.S.C. 4701(b), and that certification represents a determination by the CDFI Fund that the CDFI has satisfied the above described statutory requirements, FHFA believes that an entity that has been certified by the CDFI Fund may be presumed to have satisfied the community support requirements of section 10(g) of the Bank Act. Accordingly, the final rule includes several amendments to the existing community support regulations to implement that determination. The final rule also relocates the existing community support regulations from 12 CFR part 944 to 12 CFR part 1290.

Section 1290.1 of the final rule adds several definitions to those in the existing community support regulations and revises one existing definition. The newly defined terms are ''appropriate Federal banking agency,'' ''appropriate State regulator,'' ''Bank,'' ''CDFI Fund,'' ''community development financial institution,'' and ''FHFA.'' The definition of ''targeted community lending'' is revised to replace a cross-reference to a definition from the Finance Board regulations with the actual content of the cross-referenced definition, which does not alter the substance of the defined term.

Section 1290.2 of the relocated community support regulations is being revised by including in paragraph (a) (which deals with the biennial selection of members for community support review) new language saying that the review process applies ''except as otherwise provided in this section.'' That new language refers to new paragraph (e), which provides that a member that has been certified as a CDFI by the CDFI Fund shall be deemed to be in compliance with the community support requirements of section 10(g) of the Bank Act by virtue of that certification and is not subject to the biennial review under paragraph (a) of this section. This language also includes an express statement that the

exclusion for certified CDFIs does not apply to any members that are insured depository institutions or CDFI credit unions. Those institutions would continue to be evaluated under the community support requirements that apply to all other depository institutions and credit unions, notwithstanding their CDFI status. FHFA has excluded those institutions because it believes that all depository institution and credit union members should be evaluated for community support compliance under the same regulatory standards, *i.e.,* the CRA and first-time home buyer standards described above.

IV. Paperwork Reduction Act

The final rule will have no substantive or material effect on any collection of information covered by the Paperwork Reduction Act of 1995 (PRA). *See* 44 U.S.C. 3501 *et seq.* Therefore, FHFA has not submitted this final rule to the Office of Management and Budget (OMB) for review.

The currently approved information collection, entitled ''Members of the Banks,'' has been assigned control number 2590–0003 by the Office of Management and Budget (OMB). FHFA uses this information as set forth in the existing Members of the Banks regulation.

The Community Support Statement Form contained in the currently approved information collection, entitled ''Community Support Requirements,'' has been assigned the control number 2590–0005 by the OMB. FHFA uses this information as set forth in the existing Community Support Requirements Regulation.

FHFA plans to direct the Banks to use a revised version of those instructions, applications, and forms, which revised version will not materially modify the approved information collections.

V. Regulatory Flexibility Act

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

List of Subjects

12 CFR Parts 925 and 1263

Federal home loan banks, Reporting and recordkeeping requirements.

12 CFR Parts 944 and 1290

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

■ For the reasons stated in the preamble, FHFA hereby amends chapters IX and XII, of title 12 of the Code of Federal Regulations as follows:

CHAPTER IX—FEDERAL HOUSING FINANCE BOARD

PART 925—[REDESIGNATED AS PART 1263]

■ 1. Transfer 12 CFR part 925 from chapter IX, subchapter D, to chapter XII, subchapter D and redesignate as 12 CFR part 1263.

■ 2. Revise the newly redesignated part 1263 to read as follows:

PART 1263—MEMBERS OF THE BANKS

Subpart A—Definitions

Sec.
1263.1 Definitions.

Subpart B—Membership Application Process

1263.2 Membership application requirements.
1263.3 Decision on application.
1263.4 Automatic membership.
1263.5 Appeals.

Subpart C—Eligibility Requirements

1263.6 General eligibility requirements.
1263.7 Duly organized requirement.
1263.8 Subject to inspection and regulation requirement.
1263.9 Makes long-term home mortgage loans requirement.
1263.10 Ten percent requirement for certain insured depository institution applicants.
1263.11 Financial condition requirement for depository institutions and CDFI credit unions.
1263.12 Character of management requirement.
1263.13 Home financing policy requirement.
1263.14 De novo insured depository institution applicants.
1263.15 Recent merger or acquisition applicants.
1263.16 Financial condition requirement for insurance company and certain CDFI applicants.
1263.17 Rebuttable presumptions.
1263.18 Determination of appropriate Bank district for membership.

Subpart D—Stock Requirements

1263.19 Par value and price of stock.
1263.20 Stock purchase.
1263.21 Issuance and form of stock.
1263.22 Adjustments in stock holdings.
1263.23 Excess stock.

Subpart E—Consolidations Involving Members

1263.24 Consolidations involving members.

Subpart F—Withdrawal and Removal from Membership

1263.25 Reserved.
1263.26 Voluntary withdrawal from membership.
1263.27 Involuntary termination of membership.
1263.28 Reserved.

Subpart G—Orderly Liquidation of Advances and Redemption of Stock

1263.29 Disposition of claims.

Subpart H—Reacquisition of Membership

1263.30 Readmission to membership.

Subpart I—Bank Access to Information

1263.31 Reports and examinations.

Subpart J—Membership Insignia

1263.32 Official membership insignia.

Authority: 12 U.S.C. 1422, 1423, 1424, 1426, 1430, 1442, 4511, 4513.

Subpart A—Definitions

§ 1263.1 Definitions.

For purposes of this part:

Adjusted net income means net income, excluding extraordinary items such as income received from, or expense incurred in, sales of securities or fixed assets, reported on a regulatory financial report.

Aggregate unpaid loan principal means the aggregate unpaid principal of a subscriber's or member's home mortgage loans, home-purchase contracts and similar obligations.

Allowance for loan and lease losses means a specified balance-sheet account held to fund potential losses on loans or leases, which is reported on a regulatory financial report.

Appropriate regulator means:

(1) In the case of an insured depository institution or CDFI credit union, the Federal Deposit Insurance Corporation, Board of Governors of the Federal Reserve System, National Credit Union Administration, Office of the Comptroller of the Currency, Office of Thrift Supervision, or appropriate State regulator that has regulatory authority over, or is empowered to institute enforcement action against, the institution, as applicable, and

(2) In the case of an insurance company, an appropriate State regulator accredited by the National Association of Insurance Commissioners.

Bank Act means the Federal Home Loan Bank Act, as amended (12 U.S.C. 1421 through 1449).

CDFI credit union means a State-chartered credit union that has been certified as a CDFI by the CDFI Fund and that does not have Federal share insurance.

CDFI Fund means the Community Development Financial Institutions

Fund established under section 104(a) of the Community Development Banking and Financial Institutions Act of 1994 (12 U.S.C. 4703(a)).

CFI asset cap means $1 billion, as adjusted annually by FHFA, beginning in 2009, to reflect any percentage increase in the preceding year's Consumer Price Index (CPI) for all urban consumers, as published by the U.S. Department of Labor.

Class A stock means capital stock issued by a Bank, including subclasses, that has the characteristics specified in section 6(a)(4)(A)(i) of the Bank Act (12 U.S.C. 1426(a)(4)(A)(i)) and applicable FHFA regulations.

Class B stock means capital stock issued by a Bank, including subclasses, that has the characteristics specified in section 6(a)(4)(A)(ii) of the Bank Act (12 U.S.C. 1426(a)(4)(A)(ii)) and applicable FHFA regulations.

Combination business or farm property means real property for which the total appraised value is attributable to residential, and business or farm uses.

Community development financial institution or CDFI means an institution that is certified as a community development financial institution by the CDFI Fund under the Community Development Banking and Financial Institutions Act of 1994 (12 U.S.C. 4701 *et seq.*), other than a bank or savings association insured under the Federal Deposit Insurance Act (12 U.S.C. 1811 *et seq.*), a holding company for such a bank or savings association, or a credit union insured under the Federal Credit Union Act (12 U.S.C. 1751 *et seq.*).

Community financial institution or CFI means an institution:

(1) The deposits of which are insured under the Federal Deposit Insurance Act (12 U.S.C. 1811 *et seq.*); and

(2) The total assets of which, as of the date of a particular transaction, are less than the CFI asset cap, with total assets being calculated as an average of total assets over three years, with such average being based on the institution's regulatory financial reports filed with its appropriate regulator for the most recent calendar quarter and the immediately preceding 11 calendar quarters.

Composite regulatory examination rating means a composite rating assigned to an institution following the guidelines of the Uniform Financial Institutions Rating System (issued by the Federal Financial Institutions Examination Council), including a CAMELS rating or other similar rating, contained in a written regulatory examination report.

Consolidation includes a consolidation, a merger, or a purchase of all of the assets and assumption of all of the liabilities of an entity by another entity.

Director means the Director of FHFA or his or her designee.

Dwelling unit means a single room or a unified combination of rooms designed for residential use.

Enforcement action means any written notice, directive, order, or agreement initiated by an applicant for Bank membership or by its appropriate regulator to address any operational, financial, managerial or other deficiencies of the applicant identified by such regulator. An ''enforcement action'' does not include a board of directors' resolution adopted by the applicant in response to examination weaknesses identified by such regulator.

Funded residential construction loan means the portion of a loan secured by real property made to finance the on-site construction of dwelling units on one-to-four family property or multifamily property disbursed to the borrower.

Gross revenues means, in the case of a CDFI applicant, total revenues received from all sources, including grants and other donor contributions and earnings from operations.

Home mortgage loan means:

(1) A loan, whether or not fully amortizing, or an interest in such a loan, which is secured by a mortgage, deed of trust, or other security agreement that creates a first lien on one of the following interests in property:

(i) One-to-four family property or multifamily property, in fee simple;

(ii) A leasehold on one-to-four family property or multifamily property under a lease of not less than 99 years that is renewable, or under a lease having a period of not less than 50 years to run from the date the mortgage was executed; or

(iii) Combination business or farm property where at least 50 percent of the total appraised value of the combined property is attributable to the residential portion of the property, or in the case of any community financial institution, combination business or farm property, on which is located a permanent structure actually used as a residence (other than for temporary or seasonal housing), where the residence constitutes an integral part of the property; or

(2) A mortgage pass-through security that represents an undivided ownership interest in:

(i) Long-term loans, provided that, at the time of issuance of the security, all of the loans meet the requirements of paragraph (1) of this definition; or

(ii) A security that represents an undivided ownership interest in long-term loans, provided that, at the time of issuance of the security, all of the loans meet the requirements of paragraph (1) of this definition.

Insured depository institution means an insured depository institution as defined in section 2(9) of the Bank Act, as amended (12 U.S.C. 1422(9)).

Long-term means a term to maturity of five years or greater.

Manufactured housing means a manufactured home as defined in section 603(6) of the National Manufactured Housing Construction and Safety Standards Act of 1974, as amended (42 U.S.C. 5402(6)).

Multifamily property means:

(1) Real property that is solely residential and includes five or more dwelling units;

(2) Real property that includes five or more dwelling units combined with commercial units, provided that the property is primarily residential; or

(3) Nursing homes, dormitories, or homes for the elderly.

Nonperforming loans and leases means the sum of the following, reported on a regulatory financial report:

(1) Loans and leases that have been past due for 90 days (60 days, in the case of credit union applicants) or longer but are still accruing;

(2) Loans and leases on a nonaccrual basis; and

(3) Restructured loans and leases (not already reported as nonperforming).

Nonresidential real property means real property that is not used for residential purposes, including business or industrial property, hotels, motels, churches, hospitals, educational and charitable institution buildings or facilities, clubs, lodges, association buildings, golf courses, recreational facilities, farm property not containing a dwelling unit, or similar types of property.

One-to-four family property means:

(1) Real property that is solely residential, including one-to-four family dwelling units or more than four family dwelling units if each dwelling unit is separated from the other dwelling units by dividing walls that extend from ground to roof, such as row houses, townhouses or similar types of property;

(2) Manufactured housing if applicable State law defines the purchase or holding of manufactured housing as the purchase or holding of real property;

(3) Individual condominium dwelling units or interests in individual cooperative housing dwelling units that are part of a condominium or cooperative building without regard to the number of total dwelling units therein; or

(4) Real property which includes one-to-four family dwelling units combined with commercial units, provided the property is primarily residential.

Operating expenses means, in the case of a CDFI applicant, expenses for business operations, including, but not limited to, staff salaries and benefits, professional fees, interest, loan loss provision, and depreciation, contained in the applicant's audited financial statements.

Other real estate owned means all other real estate owned (*i.e.,* foreclosed and repossessed real estate), reported on a regulatory financial report, and does not include direct and indirect investments in real estate ventures.

Regulatory examination report means a written report of examination prepared by the applicant's appropriate regulator, containing, in the case of insured depository institution applicants, a composite rating assigned to the institution following the guidelines of the Uniform Financial Institutions Rating System, including a CAMELS rating or other similar rating.

Regulatory financial report means a financial report that an applicant is required to file with its appropriate regulator on a specific periodic basis, including the quarterly call report for commercial banks, thrift financial report for savings associations, quarterly or semi-annual call report for credit unions, the National Association of Insurance Commissioners' annual or quarterly report for insurance companies, or other similar report, including such report maintained by the appropriate regulator on a computer on-line database.

Residential mortgage loan means any one of the following types of loans, whether or not fully amortizing:

(1) Home mortgage loans;

(2) Funded residential construction loans;

(3) Loans secured by manufactured housing whether or not defined by State law as secured by an interest in real property;

(4) Loans secured by junior liens on one-to-four family property or multifamily property;

(5) Mortgage pass-through securities representing an undivided ownership interest in–

(i) Loans that meet the requirements of paragraphs (1) through (4) of this definition at the time of issuance of the security;

(ii) Securities representing an undivided ownership interest in loans, provided that, at the time of issuance of the security, all of the loans meet the requirements of paragraphs (1) through (4) of this definition; or

(iii) Mortgage debt securities as defined in paragraph (6) of this definition;

(6) Mortgage debt securities secured by–

(i) Loans, provided that, at the time of issuance of the security, substantially all of the loans meet the requirements of paragraphs (1) through (4) of this definition;

(ii) Securities that meet the requirements of paragraph (5) of this definition; or

(iii) Securities secured by assets, provided that, at the time of issuance of the security, all of the assets meet the requirements of paragraphs (1) through (5) of this definition;

(7) Home mortgage loans secured by a leasehold interest, as defined in paragraph (1)(ii) of the definition of ''home mortgage loan,'' except that the period of the lease term may be for any duration; or

(8) Loans that finance properties or activities that, if made by a member, would satisfy the statutory requirements for the Community Investment Program established under section 10(i) of the Bank Act (12 U.S.C. 1430(i)), or the regulatory requirements established for any CICA program.

Restricted assets means both permanently restricted assets and temporarily restricted assets, as those terms are used in Financial Accounting Standard No. 117, or any successor publication.

Total assets means the total assets reported on a regulatory financial report or, in the case of a CDFI applicant, the total assets contained in the applicant's audited financial statements.

Unrestricted cash and cash equivalents means, in the case of a CDFI applicant, cash and highly liquid assets that can be easily converted into cash that are not restricted in a manner that prevents their use in paying expenses, as contained in the applicant's audited financial statements.

Subpart B—Membership Application Process

§ 1263.2 Membership application requirements.

(a) *Application.* An applicant for membership in a Bank shall submit to that Bank an application that satisfies the requirements of this part. The application shall include a written resolution or certification duly adopted by the applicant's board of directors, or by an individual with authority to act on behalf of the applicant's board of directors, of the following:

(1) *Applicant review.* Applicant has reviewed the requirements of this part and, as required by this part, has provided to the best of applicant's knowledge the most recent, accurate, and complete information available; and

(2) *Duty to supplement.* Applicant will promptly supplement the application with any relevant information that comes to applicant's attention prior to the Bank's decision on whether to approve or deny the application, and if the Bank's decision is appealed pursuant to § 1263.5, prior to resolution of any appeal by FHFA.

(b) *Digest.* The Bank shall prepare a written digest for each applicant stating whether or not the applicant meets each of the requirements in §§ 1263.6 to 1263.18, the Bank's findings, and the reasons therefor.

(c) *File.* The Bank shall maintain a membership file for each applicant for at least three years after the Bank decides whether to approve or deny membership or, in the case of an appeal to FHFA, for three years after the resolution of the appeal. The membership file shall contain at a minimum:

(1) *Digest.* The digest required by paragraph (b) of this section.

(2) *Required documents.* All documents required by §§ 1263.6 to 1263.18, including those documents required to establish or rebut a presumption under this part, shall be described in and attached to the digest. The Bank may retain in the file only the relevant portions of the regulatory financial reports required by this part. If an applicant's appropriate regulator requires return or destruction of a regulatory examination report, the date that the report is returned or destroyed shall be noted in the file.

(3) *Additional documents.* Any additional document submitted by the applicant, or otherwise obtained or generated by the Bank, concerning the applicant.

(4) *Decision resolution.* The decision resolution described in § 1263.3(b).

§ 1263.3 Decision on application.

(a) *Authority.* FHFA hereby authorizes the Banks to approve or deny all applications for membership, subject to the requirements of this part. The authority to approve membership applications may be exercised only by a committee of the Bank's board of directors, the Bank president, or a senior officer who reports directly to the Bank president, other than an officer with responsibility for business development.

(b) *Decision resolution.* For each applicant, the Bank shall prepare a written resolution duly adopted by the Bank's board of directors, by a committee of the board of directors, or

by an officer with delegated authority to approve membership applications. The decision resolution shall state:

(1) That the statements in the digest are accurate to the best of the Bank's knowledge, and are based on a diligent and comprehensive review of all available information identified in the digest; and

(2) The Bank's decision and the reasons therefor. Decisions to approve an application should state specifically that:

(i) The applicant is authorized under the laws of the United States and the laws of the appropriate State to become a member of, purchase stock in, do business with, and maintain deposits in, the Bank to which the applicant has applied; and

(ii) The applicant meets all of the membership eligibility criteria of the Bank Act and this part.

(c) *Action on applications.* The Bank shall act on an application within 60 calendar days of the date the Bank deems the application to be complete. An application is ''complete'' when a Bank has obtained all the information required by this part, and any other information the Bank deems necessary, to process the application. If an application that was deemed complete subsequently is deemed incomplete because the Bank determines during the review process that additional information is necessary to process the application, the Bank may stop the 60-day clock until the application again is deemed complete, and then resume the clock where it left off. The Bank shall notify an applicant in writing when its application is deemed by the Bank to be complete, and shall maintain a copy of such letter in the applicant's membership file. The Bank shall notify an applicant if the 60-day clock is stopped, and when the clock is resumed, and shall maintain a written record of such notifications in the applicant's membership file. Within three business days of a Bank's decision on an application, the Bank shall provide the applicant and FHFA with a copy of the Bank's decision resolution.

§ 1263.4 Automatic membership.

(a) *Automatic membership for certain charter conversions.* An insured depository institution member that converts from one charter type to another automatically shall become a member of the Bank of which the converting institution was a member on the effective date of such conversion, provided that the converting institution continues to be an insured depository institution and the assets of the institution immediately before and immediately after the conversion are not materially different. In such case, all relationships existing between the member and the Bank at the time of such conversion may continue.

(b) *Automatic membership for transfers.* Any member whose membership is transferred pursuant to § 1263.18(d) automatically shall become a member of the Bank to which it transfers.

(c) *Automatic membership, in the Bank's discretion, for certain consolidations.*—(1) If a member institution (or institutions) and a nonmember institution are consolidated, and the consolidated institution has its principal place of business in a State in the same Bank district as the disappearing institution (or institutions), and the consolidated institution will operate under the charter of the nonmember institution, on the effective date of the consolidation, the consolidated institution may, in the discretion of the Bank of which the disappearing institution (or institutions) was a member immediately prior to the effective date of the consolidation, automatically become a member of such Bank upon the purchase of the minimum amount of Bank stock required for membership in that Bank, as required by § 1263.20, provided that:

(i) 90 percent or more of the consolidated institution's total assets are derived from the total assets of the disappearing member institution (or institutions); and

(ii) The consolidated institution provides written notice to such Bank, within 60 calendar days after the effective date of the consolidation, that it desires to be a member of the Bank.

(2) The provisions of § 1263.24(b)(4)(i) shall apply, and upon approval of automatic membership by the Bank, the provisions of § 1263.24(c) and (d) shall apply.

§ 1263.5 Appeals.

(a) *Appeals by applicants.*—(1) *Filing procedure.* Within 90 calendar days of the date of a Bank's decision to deny an application for membership, the applicant may file a written appeal of the decision with FHFA.

(2) *Documents.* The applicant's appeal shall be addressed to the Deputy Director for Federal Home Loan Bank Regulation, Federal Housing Finance Agency, 1625 Eye Street, NW., Washington, DC 20006, with a copy to the Bank, and shall include the following documents:

(i) *Bank's decision resolution.* A copy of the Bank's decision resolution; and

(ii) *Basis for appeal.* An applicant must provide a statement of the basis for the appeal with sufficient facts, information, analysis, and explanation to rebut any applicable presumptions, or otherwise to support the applicant's position.

(b) *Record for appeal.*—(1) *Copy of membership file.* Upon receiving a copy of an appeal, the Bank whose action has been appealed (appellee Bank) shall provide FHFA with a copy of the applicant's complete membership file. Until FHFA resolves the appeal, the appellee Bank shall supplement the materials provided to FHFA as any new materials are received.

(2) *Additional information.* FHFA may request additional information or further supporting arguments from the appellant, the appellee Bank, or any other party that FHFA deems appropriate.

(c) *Deciding appeals.* FHFA shall consider the record for appeal described in paragraph (b) of this section and shall resolve the appeal based on the requirements of the Bank Act and this part within 90 calendar days of the date the appeal is filed with FHFA. In deciding the appeal, FHFA shall apply the presumptions in this part, unless the appellant or appellee Bank presents evidence to rebut a presumption as provided in § 1263.17.

Subpart C—Eligibility Requirements

§ 1263.6 General eligibility requirements.

(a) *Requirements.* Any building and loan association, savings and loan association, cooperative bank, homestead association, insurance company, savings bank, community development financial institution (including a CDFI credit union), or insured depository institution, upon submission of an application satisfying all of the requirements of the Bank Act and this part, shall be eligible to become a member of a Bank if:

(1) It is duly organized under Tribal law, or under the laws of any State or of the United States;

(2) It is subject to inspection and regulation under the banking laws, or under similar laws, of any State or of the United States or, in the case of a CDFI, is certified by the CDFI Fund;

(3) It makes long-term home mortgage loans;

(4) Its financial condition is such that advances may be safely made to it;

(5) The character of its management is consistent with sound and economical home financing; and

(6) Its home financing policy is consistent with sound and economical home financing.

(b) *Additional eligibility requirement for insured depository institutions other than community financial institutions.* In order to be eligible to become a member of a Bank, an insured depository institution applicant other than a community financial institution also must have at least 10 percent of its total assets in residential mortgage loans.

(c) *Additional eligibility requirement for applicants that are not insured depository institutions.* In order to be eligible to become a member of a Bank, an applicant that is not an insured depository institution also must have mortgage-related assets that reflect a commitment to housing finance, as determined by the Bank in its discretion.

(d) *Ineligibility.* Except as otherwise provided in this part, if an applicant does not satisfy the requirements of this part, the applicant is ineligible for membership.

§ 1263.7 Duly organized requirement.

An applicant shall be deemed to be duly organized, as required by section 4(a)(1)(A) of the Bank Act (12 U.S.C. 1424(a)(1)(A)) and § 1263.6(a)(1), if it is chartered by a State or Federal agency as a building and loan association, savings and loan association, cooperative bank, homestead association, insurance company, savings bank, or insured depository institution or, in the case of a CDFI applicant, is incorporated under State or Tribal law.

§ 1263.8 Subject to inspection and regulation requirement.

An applicant shall be deemed to be subject to inspection and regulation, as required by section 4(a)(1)(B) of the Bank Act (12 U.S.C. 1424 (a)(1)(B)) and § 1263.6(a)(2) if, in the case of an insured depository institution or insurance company applicant, it is subject to inspection and regulation by its appropriate regulator. A CDFI applicant that is certified by the CDFI Fund is not subject to this requirement.

§ 1263.9 Makes long-term home mortgage loans requirement.

An applicant shall be deemed to make long-term home mortgage loans, as required by section 4(a)(1)(C) of the Bank Act (12 U.S.C. 1424(a)(1)(C)) and § 1263.6(a)(3), if, based on the applicant's most recent regulatory financial report filed with its appropriate regulator, or other documentation provided to the Bank, in the case of a CDFI applicant that does not file such reports, the applicant originates or purchases long-term home mortgage loans.

§ 1263.10 Ten percent requirement for certain insured depository institution applicants.

An insured depository institution applicant that is subject to the 10 percent requirement of section 4(a)(2)(A) of the Bank Act (12 U.S.C. 1424(a)(2)(A)) and § 1263.6(b) shall be deemed to be in compliance with such requirement if, based on the applicant's most recent regulatory financial report filed with its appropriate regulator, the applicant has at least 10 percent of its total assets in residential mortgage loans, except that any assets used to secure mortgage debt securities as described in paragraph (6) of the definition of ''residential mortgage loan'' set forth in § 1263.1 shall not be used to meet this requirement.

§ 1263.11 Financial condition requirement for depository institutions and CDFI credit unions.

(a) *Review requirement.* In determining whether a building and loan association, savings and loan association, cooperative bank, homestead association, savings bank, insured depository institution, or CDFI credit union has complied with the financial condition requirements of section 4(a)(2)(B) of the Bank Act (12 U.S.C. 1424(a)(2)(B)) and § 1263.6(a)(4), the Bank shall obtain as a part of the membership application and review each of the following documents:

(1) *Regulatory financial reports.* The regulatory financial reports filed by the applicant with its appropriate regulator for the last six calendar quarters and three year-ends preceding the date the Bank receives the application;

(2) *Financial statement.* In order of preference—

(i) The most recent independent audit of the applicant conducted in accordance with generally accepted auditing standards by a certified public accounting firm which submits a report on the applicant;

(ii) The most recent independent audit of the applicant's parent holding company conducted in accordance with generally accepted auditing standards by a certified public accounting firm which submits a report on the consolidated holding company but not on the applicant separately;

(iii) The most recent directors' examination of the applicant conducted in accordance with generally accepted auditing standards by a certified public accounting firm;

(iv) The most recent directors' examination of the applicant performed by other external auditors;

(v) The most recent review of the applicant's financial statements by external auditors;

(vi) The most recent compilation of the applicant's financial statements by external auditors; or

(vii) The most recent audit of other procedures of the applicant.

(3) *Regulatory examination report.* The applicant's most recent available regulatory examination report prepared by its appropriate regulator, a summary prepared by the Bank of the applicant's strengths and weaknesses as cited in the regulatory examination report, and a summary prepared by the Bank or applicant of actions taken by the applicant to respond to examination weaknesses;

(4) *Enforcement actions.* A description prepared by the Bank or applicant of any outstanding enforcement actions against the applicant, responses by the applicant, reports as required by the enforcement action, and verbal or written indications, if available, from the appropriate regulator of how the applicant is complying with the terms of the enforcement action; and

(5) *Additional information.* Any other relevant document or information concerning the applicant that comes to the Bank's attention in reviewing the applicant's financial condition.

(b) *Standards.* An applicant of the type described in paragraph (a) of this section shall be deemed to be in compliance with the financial condition requirement of section 4(a)(2)(B) of the Bank Act (12 U.S.C. 1424(a)(2)(B)) and § 1263.6(a)(4), if:

(1) *Recent composite regulatory examination rating.* The applicant has received a composite regulatory examination rating from its appropriate regulator within two years preceding the date the Bank receives the application;

(2) *Capital requirement.* The applicant meets all of its minimum statutory and regulatory capital requirements as reported in its most recent quarter-end regulatory financial report filed with its appropriate regulator; and

(3) *Minimum performance standard*—(i) Except as provided in paragraph (b)(3)(iii) of this section, the applicant's most recent composite regulatory examination rating from its appropriate regulator within the past two years was ''1'', or the most recent rating was ''2'' or ''3'' and, based on the applicant's most recent regulatory financial report filed with its appropriate regulator, the applicant satisfied all of the following performance trend criteria—

(A) *Earnings.* The applicant's adjusted net income was positive in four of the six most recent calendar quarters;

(B) *Nonperforming assets.* The applicant's nonperforming loans and leases plus other real estate owned, did

not exceed 10 percent of its total loans and leases plus other real estate owned, in the most recent calendar quarter; and

(C) *Allowance for loan and lease losses.* The applicant's ratio of its allowance for loan and lease losses plus the allocated transfer risk reserve to nonperforming loans and leases was 60 percent or greater during four of the six most recent calendar quarters.

(ii) For applicants that are not required to report financial data to their appropriate regulator on a quarterly basis, the information required in paragraph (b)(3)(i) of this section may be reported on a semi-annual basis.

(iii) A CDFI credit union applicant must meet the performance trend criteria in paragraph (b)(3)(i) of this section irrespective of its composite regulatory examination rating.

(c) *Eligible collateral not considered.* The availability of sufficient eligible collateral to secure advances to the applicant is presumed and shall not be considered in determining whether an applicant is in the financial condition required by section 4(a)(2)(B) of the Bank Act (12 U.S.C. 1424(a)(2)(B)) and § 1263.6(a)(4).

§ 1263.12 Character of management requirement.

(a) *General.* A building and loan association, savings and loan association, cooperative bank, homestead association, savings bank, insured depository institution, insurance company, and CDFI credit union shall be deemed to be in compliance with the character of management requirements of section 4(a)(2)(C) of the Bank Act (12 U.S.C. 1424(a)(2)(C)) and § 1263.6(a)(5) if the applicant provides to the Bank an unqualified written certification duly adopted by the applicant's board of directors, or by an individual with authority to act on behalf of the applicant's board of directors, that:

(1) *Enforcement actions.* Neither the applicant nor any of its directors or senior officers is subject to, or operating under, any enforcement action instituted by its appropriate regulator;

(2) *Criminal, civil or administrative proceedings.* Neither the applicant nor any of its directors or senior officers has been the subject of any criminal, civil or administrative proceedings reflecting upon creditworthiness, business judgment, or moral turpitude since the most recent regulatory examination report; and

(3) *Criminal, civil or administrative monetary liabilities, lawsuits or judgments.* There are no known potential criminal, civil or administrative monetary liabilities, material pending lawsuits, or unsatisfied judgments against the applicant or any of its directors or senior officers since the most recent regulatory examination report, that are significant to the applicant's operations.

(b) *CDFIs other than CDFI credit unions.* A CDFI applicant, other than a CDFI credit union, shall be deemed to be in compliance with the character of management requirement of § 1263.6(a)(5), if the applicant provides an unqualified written certification duly adopted by the applicant's board of directors, or by an individual with authority to act on behalf of the applicant's board of directors, that:

(1) *Criminal, civil or administrative proceedings.* Neither the applicant nor any of its directors or senior officers has been the subject of any criminal, civil or administrative proceedings reflecting upon creditworthiness, business judgment, or moral turpitude in the past three years; and

(2) *Criminal, civil or administrative monetary liabilities, lawsuits or judgments.* There are no known potential criminal, civil or administrative monetary liabilities, material pending lawsuits, or unsatisfied judgments against the applicant or any of its directors or senior officers arising within the past three years that are significant to the applicant's operations.

§ 1263.13 Home financing policy requirement.

(a) *Standard.* An applicant shall be deemed to be in compliance with the home financing policy requirements of section 4(a)(2)(C) of the Bank Act (12 U.S.C. 1424(a)(2)(C)) and § 1263.6(a)(6), if the applicant has received a Community Reinvestment Act (CRA) rating of ''Satisfactory'' or better on its most recent formal, or if unavailable, informal or preliminary, CRA performance evaluation.

(b) *Written justification required.* An applicant that is not subject to the CRA shall file, as part of its application for membership, a written justification acceptable to the Bank of how and why the applicant's home financing policy is consistent with the Bank System's housing finance mission.

§ 1263.14 De novo insured depository institution applicants.

(a) *Duly organized, subject to inspection and regulation, financial condition and character of management requirements.* An insured depository institution applicant whose date of charter approval is within three years prior to the date the Bank receives the applicant's application for membership in the Bank (*de novo* applicant) is deemed to meet the requirements of §§ 1263.7, 1263.8, 1263.11 and 1263.12.

(b) *Makes long-term home mortgage loans requirement.* A de novo applicant shall be deemed to make long-term home mortgage loans as required by § 1263.9, if it has filed as part of its application for membership, a written justification acceptable to the Bank of how its home financing credit policy and lending practices will include originating or purchasing long-term home mortgage loans.

(c) *10 percent requirement*—(1) *One-year requirement.* A de novo applicant subject to the 10 percent requirement of section 4(a)(2)(A) of the Bank Act (12 U.S.C. 1424(a)(2)(A)) and § 1263.6(b) shall have until one year after commencing its initial business operations to meet the 10 percent requirement of § 1263.10.

(2) *Conditional approval.* A de novo applicant shall be conditionally deemed to be in compliance with the 10 percent requirement of section 4(a)(2)(A) of the Bank Act (12 U.S.C. 1424(a)(2)(A)) and § 1263.6(b). A de novo applicant that receives such conditional membership approval is subject to the stock purchase requirements established by FHFA regulation or the Bank's capital plan, as applicable, as well as FHFA regulations governing advances to members.

(3) *Approval.* A de novo applicant shall be deemed to be in compliance with the 10 percent requirement of section 4(a)(2)(A) of the Bank Act (12 U.S.C. 1424(a)(2)(A)) and § 1263.6(b) upon receipt by the Bank from the applicant, within one year after commencement of the applicant's initial business operations, of evidence acceptable to the Bank that the applicant satisfies the 10 percent requirement.

(4) *Conditional approval deemed null and void.* If the requirements of paragraph (c)(3) of this section are not satisfied, a de novo applicant shall be deemed to be in noncompliance with the 10 percent requirement of section 4(a)(2)(A) of the Bank Act (12 U.S.C. 1424(a)(2)(A)) and § 1263.6(b), and its conditional membership approval is deemed null and void.

(5) *Treatment of outstanding advances and Bank stock.* If a de novo applicant's conditional membership approval is deemed null and void pursuant to paragraph (c)(4) of this section, the liquidation of any outstanding indebtedness owed by the applicant to the Bank and redemption of stock of such Bank shall be carried out in accordance with § 1263.29.

(d) *Home financing policy requirement*—(1) *Conditional approval.*

A de novo applicant that has not received its first formal, or, if unavailable, informal or preliminary, CRA performance evaluation, shall be conditionally deemed to be in compliance with the home financing policy requirement of section 4(a)(2)(C) of the Bank Act (12 U.S.C. 1424(a)(2)(C)) and § 1263.6(a)(6), if the applicant has filed, as part of its application for membership, a written justification acceptable to the Bank of how and why its home financing credit policy and lending practices will meet the credit needs of its community. An applicant that receives such conditional membership approval is subject to the stock purchase requirements established by FHFA regulation or the Bank's capital plan, as applicable, as well as FHFA regulations governing advances to members.

(2) *Approval.* A de novo applicant that has been granted conditional approval under paragraph (d)(1) of this section shall be deemed to be in compliance with the home financing policy requirement of section 4(a)(2)(C) of the Bank Act (12 U.S.C. 1424(a)(2)(C)) and § 1263.6(a)(6) upon receipt by the Bank of evidence from the applicant that it received a CRA rating of ''Satisfactory'' or better on its first formal, or if unavailable, informal or preliminary, CRA performance evaluation.

(3) *Conditional approval deemed null and void.* If the de novo applicant's first such CRA rating is ''Needs to Improve'' or ''Substantial Non-Compliance,'' the applicant shall be deemed to be in noncompliance with the home financing policy requirement of section 4(a)(2)(C) of the Bank Act (12 U.S.C. 1424(a)(2)(C)) and § 1263.6(a)(6), subject to rebuttal by the applicant under § 1263.17(f), and its conditional membership approval is deemed null and void.

(4) *Treatment of outstanding advances and Bank stock.* If the applicant's conditional membership approval is deemed null and void pursuant to paragraph (d)(3) of this section, the liquidation of any outstanding indebtedness owed by the applicant to the Bank and redemption of stock of such Bank shall be carried out in accordance with § 1263.29.

§ 1263.15 Recent merger or acquisition applicants.

An applicant that merged with or acquired another institution prior to the date the Bank receives its application for membership is subject to the requirements of §§ 1263.7 to 1263.13 except as provided in this section.

(a) *Financial condition requirement*—(1) *Regulatory financial reports.* For purposes of § 1263.11(a)(1), an applicant that, as a result of a merger or acquisition preceding the date the Bank receives its application for membership, has not yet filed regulatory financial reports with its appropriate regulator for the last six calendar quarters and three year-ends preceding such date, shall provide any regulatory financial reports that the applicant has filed with its appropriate regulator.

(2) *Performance trend criteria.* For purposes of § 1263.11(b)(3)(i)(A) to (C), an applicant that, as a result of a merger or acquisition preceding the date the Bank receives its application for membership, has not yet filed combined regulatory financial reports with its appropriate regulator for the last six calendar quarters preceding such date, shall provide pro forma combined financial statements for those calendar quarters in which actual combined regulatory financial reports are unavailable.

(b) *Home financing policy requirement.* For purposes of § 1263.13, an applicant that, as a result of a merger or acquisition preceding the date the Bank receives its application for membership, has not received its first formal, or if unavailable, informal or preliminary, CRA performance evaluation, shall file as part of its application, a written justification acceptable to the Bank of how and why the applicant's home financing credit policy and lending practices will meet the credit needs of its community.

(c) *Makes long-term home mortgage loans requirement; 10 percent requirement.* For purposes of determining compliance with §§ 1263.9 and 1263.10, a Bank may, in its discretion, permit an applicant that, as a result of a merger or acquisition preceding the date the Bank receives its application for membership, has not yet filed a consolidated regulatory financial report as a combined entity with its appropriate regulator, to provide the combined pro forma financial statement for the combined entity filed with the regulator that approved the merger or acquisition.

§ 1263.16 Financial condition requirement for insurance company and certain CDFI applicants.

(a) *Insurance companies.* An insurance company applicant shall be deemed to meet the financial condition requirement of § 1263.6(a)(4) if, based on the information contained in the applicant's most recent regulatory financial report filed with its appropriate regulator, the applicant meets all of its minimum statutory and regulatory capital requirements and the capital standards established by the National Association of Insurance Commissioners.

(b) *CDFIs other than CDFI credit unions*—(1) *Review requirement.* In order for a Bank to determine whether a CDFI applicant, other than a CDFI credit union, has complied with the financial condition requirement of § 1263.6(a)(4), the applicant shall submit, as a part of its membership application, each of the following documents, and the Bank shall consider all such information prior to acting on the application for membership:

(i) *Financial statements.* An independent audit conducted within the prior year in accordance with generally accepted auditing standards by a certified public accounting firm, plus more recent quarterly statements, if available, and financial statements for the two years prior to the most recent audited financial statement. At a minimum, all such financial statements must include income and expense statements, statements of activities, statements of financial position, and statements of cash flows. The financial statement for the most recent year must include separate schedules or disclosures of the financial position of each of the applicant's affiliates, descriptions of their lines of business, detailed financial disclosures of the relationship between the applicant and its affiliates (such as indebtedness or subordinate debt obligations), disclosures of interlocking directorships with each affiliate, and identification of temporary and permanently restricted funds and the requirements of these restrictions;

(ii) *CDFI Fund certification.* The certification that the applicant has received from the CDFI Fund. If the certification is more than three years old, the applicant must also submit a written statement attesting that there have been no material events or occurrences since the date of certification that would adversely affect its strategic direction, mission, or business operations; and

(iii) *Additional information.* Any other relevant document or information a Bank requests concerning the applicant's financial condition that is not contained in the applicant's financial statements, as well as any other information that the applicant believes demonstrates that it satisfies the financial condition requirement of § 1263.6(a)(4), notwithstanding its failure to meet any of the financial condition standards of paragraph (b)(2) of this section.

(2) *Standards.* A CDFI applicant, other than a CDFI credit union, shall be

deemed to be in compliance with the financial condition requirement of § 1263.6(a)(4) if it meets all of the following minimum financial standards—

(i) *Net asset ratio.* The applicant's ratio of net assets to total assets is at least 20 percent, with net and total assets including restricted assets, where net assets is calculated as the residual value of assets over liabilities and is based on information derived from the applicant's most recent financial statements;

(ii) *Earnings.* The applicant has shown positive net income, where net income is calculated as gross revenues less total expenses, is based on information derived from the applicant's most recent financial statements, and is measured as a rolling three-year average;

(iii) *Loan loss reserves.* The applicant's ratio of loan loss reserves to loans and leases 90 days or more delinquent (including loans sold with full recourse) is at least 30 percent, where loan loss reserves are a specified balance sheet account that reflects the amount reserved for loans expected to be uncollectible and are based on information derived from the applicant's most recent financial statements;

(iv) *Liquidity.* The applicant has an operating liquidity ratio of at least 1.0 for the four most recent quarters, and for one or both of the two preceding years, where the numerator of the ratio includes unrestricted cash and cash equivalents and the denominator of the ratio is the average quarterly operating expense.

§ 1263.17 Rebuttable presumptions.

(a) *Rebutting presumptive compliance.* The presumption that an applicant meeting the requirements of §§ 1263.7 to 1263.16 is in compliance with section 4(a) of the Bank Act (12 U.S.C. 1424(a)) and § 1263.6(a) and (b), may be rebutted, and the Bank may deny membership to the applicant, if the Bank obtains substantial evidence to overcome the presumption of compliance.

(b) *Rebutting presumptive noncompliance.* The presumption that an applicant not meeting a particular requirement of §§ 1263.8, 1263.11, 1263.12, 1263.13, or 1263.16, is in noncompliance with section 4(a) of the Bank Act (12 U.S.C. 1424(a)), and § 1263.6(a)(2), (4), (5), or (6) may be rebutted. The applicant shall be deemed to meet such requirement, if the applicable requirements in this section are satisfied.

(c) *Presumptive noncompliance by insurance company applicant with ''subject to inspection and regulation'' requirement of § 1263.8.* If an insurance company applicant is not subject to inspection and regulation by an appropriate State regulator accredited by the National Association of Insurance Commissioners (NAIC), as required by § 1263.8, the applicant or the Bank shall prepare a written justification that provides substantial evidence acceptable to the Bank that the applicant is subject to inspection and regulation as required by § 1263.6(a)(2), notwithstanding the lack of NAIC accreditation.

(d) *Presumptive noncompliance with financial condition requirements of §§ 1263.11 and 1263.16*—(1) *Applicants subject to § 1263.11.* For applicants subject to § 1263.11, in the case of an applicant's lack of a composite regulatory examination rating within the two-year period required by § 1263.11(b)(1), a variance from the rating required by § 1263.11(b)(3)(i), or a variance from a performance trend criterion required by § 1263.11(b)(3)(i), the applicant or the Bank shall prepare a written justification pertaining to such requirement that provides substantial evidence acceptable to the Bank that the applicant is in the financial condition required by § 1263.6(a)(4), notwithstanding the lack of rating or variance.

(2) *Applicants subject to § 1263.16.* For applicants subject to § 1263.16, in the case of an insurance company applicant's variance from a capital requirement or standard of § 1263.16(a) or, in the case of a CDFI applicant's variance from the standards of § 1263.16(b), the applicant or the Bank shall prepare a written justification pertaining to such requirement or standard that provides substantial evidence acceptable to the Bank that the applicant is in the financial condition required by § 1263.6(a)(4), notwithstanding the variance.

(e) *Presumptive noncompliance with character of management requirement of § 1263.12*—(1) *Enforcement actions.* If an applicant or any of its directors or senior officers is subject to, or operating under, any enforcement action instituted by its appropriate regulator, the applicant shall provide or the Bank shall obtain:

(i) *Regulator confirmation.* Written or verbal confirmation from the applicant's appropriate regulator that the applicant or its directors or senior officers are in substantial compliance with all aspects of the enforcement action; or

(ii) *Written analysis.* A written analysis acceptable to the Bank indicating that the applicant or its directors or senior officers are in substantial compliance with all aspects of the enforcement action. The written analysis shall state each action the applicant or its directors or senior officers are required to take by the enforcement action, the actions actually taken by the applicant or its directors or senior officers, and whether the applicant regards this as substantial compliance with all aspects of the enforcement action.

(2) *Criminal, civil or administrative proceedings.* If an applicant or any of its directors or senior officers has been the subject of any criminal, civil or administrative proceedings reflecting upon creditworthiness, business judgment, or moral turpitude since the most recent regulatory examination report or, in the case of a CDFI applicant, during the past three years, the applicant shall provide or the Bank shall obtain—

(i) *Regulator confirmation.* Written or verbal confirmation from the applicant's appropriate regulator that the proceedings will not likely result in enforcement action; or

(ii) *Written analysis.* A written analysis acceptable to the Bank indicating that the proceedings will not likely result in enforcement action or, in the case of a CDFI applicant, that the proceedings will not likely have a significantly deleterious effect on the applicant's operations. The written analysis shall state the severity of the charges, and any mitigating action taken by the applicant or its directors or senior officers.

(3) *Criminal, civil or administrative monetary liabilities, lawsuits or judgments.* If there are any known potential criminal, civil or administrative monetary liabilities, material pending lawsuits, or unsatisfied judgments against the applicant or any of its directors or senior officers since the most recent regulatory examination report or, in the case of a CDFI applicant, occurring within the past three years, that are significant to the applicant's operations, the applicant shall provide or the Bank shall obtain—

(i) *Regulator confirmation.* Written or verbal confirmation from the applicant's appropriate regulator that the liabilities, lawsuits or judgments will not likely cause the applicant to fall below its applicable capital requirements set forth in §§ 1263.11(b)(2) and 1263.16(a); or

(ii) *Written analysis.* A written analysis acceptable to the Bank indicating that the liabilities, lawsuits or judgments will not likely cause the applicant to fall below its applicable

capital requirements set forth in § 1263.11(b)(2) or § 1263.16(a), or the net asset ratio set forth in § 1263.16(b)(2)(i). The written analysis shall state the likelihood of the applicant or its directors or senior officers prevailing, and the financial consequences if the applicant or its directors or senior officers do not prevail.

(f) *Presumptive noncompliance with home financing policy requirements of §§ 1263.13 and 1263.14(d).* If an applicant received a ''Substantial Non-Compliance'' rating on its most recent formal, or if unavailable, informal or preliminary, CRA performance evaluation, or a ''Needs to Improve'' CRA rating on its most recent formal, or if unavailable, informal or preliminary, CRA performance evaluation and a CRA rating of ''Needs to Improve'' or better on any immediately preceding CRA performance evaluation, the applicant shall provide or the Bank shall obtain:

(1) *Regulator confirmation.* Written or verbal confirmation from the applicant's appropriate regulator of the applicant's recent satisfactory CRA performance, including any corrective action that substantially improved upon the deficiencies cited in the most recent CRA performance evaluation(s); or

(2) *Written analysis.* A written analysis acceptable to the Bank demonstrating that the CRA rating is unrelated to home financing, and providing substantial evidence of how and why the applicant's home financing credit policy and lending practices meet the credit needs of its community.

§ 1263.18 Determination of appropriate Bank district for membership.

(a) *Eligibility.* (1) An institution eligible to become a member of a Bank under the Bank Act and this part may become a member only of the Bank of the district in which the institution's principal place of business is located, except as provided in paragraph (a)(2) of this section. A member shall promptly notify its Bank in writing whenever it relocates its principal place of business to another State and the Bank shall inform FHFA in writing of any such relocation.

(2) An institution eligible to become a member of a Bank under the Bank Act and this part may become a member of the Bank of a district adjoining the district in which the institution's principal place of business is located, if demanded by convenience and then only with the approval of FHFA.

(b) *Principal place of business.* Except as otherwise designated in accordance with this section, the principal place of business of an institution is the State in which the institution maintains its home office established as such in conformity with the laws under which the institution is organized.

(c) *Designation of principal place of business.* (1) A member or an applicant for membership may request in writing to the Bank in the district where the institution maintains its home office that a State other than the State in which it maintains its home office be designated as its principal place of business. Within 90 calendar days of receipt of such written request, the board of directors of the Bank in the district where the institution maintains its home office shall designate a State other than the State where the institution maintains its home office as the institution's principal place of business, provided that all of the following criteria are satisfied:

(i) At least 80 percent of the institution's accounting books, records, and ledgers are maintained, located or held in such designated State;

(ii) A majority of meetings of the institution's board of directors and constituent committees are conducted in such designated State; and

(iii) A majority of the institution's five highest paid officers have their place of employment located in such designated State.

(2) Written notice of a designation made pursuant to paragraph (c)(1) of this section shall be sent to the Bank in the district containing the designated State, FHFA, and the institution.

(3) The notice of designation made pursuant to paragraph (c)(1) of this section shall include the State designated as the principal place of business and the resulting Bank to which membership will be transferred.

(4) If the board of directors of the Bank in the district where the institution maintains its home office fails to make the designation requested by the member or applicant pursuant to paragraph (c)(1) of this section, then the member or applicant may request in writing that FHFA make the designation.

(d) *Transfer of membership.* (1) No transfer of membership from one Bank to another Bank shall take effect until the Banks involved reach an agreement on a method of orderly transfer.

(2) In the event that the Banks involved fail to agree on a method of orderly transfer, FHFA shall determine the conditions under which the transfer shall take place.

(e) *Effect of transfer.* A transfer of membership pursuant to this section shall be effective for all purposes, but shall not affect voting rights in the year of the transfer and shall not be subject to the provisions on termination of membership set forth in section 6 of the Bank Act (12 U.S.C. 1426) or §§ 1263.26 and 1263.27, nor the restriction on reacquiring Bank membership set forth in § 1263.30.

Subpart D—Stock Requirements

§ 1263.19 Par value and price of stock.

The capital stock of each Bank shall be sold at par, unless the Director has fixed a higher price.

§ 1263.20 Stock purchase.

(a) *Minimum stock purchase.* Each member shall purchase stock in the Bank of which it is a member in an amount specified by the Bank's capital plan, except that each member of a Bank that has not converted to the capital structure authorized by the Gramm-Leach-Bliley Act (GLB Act) shall purchase stock in the Bank in an amount equal to the greater of:

(1) $500;

(2) 1 percent of the member's aggregate unpaid loan principal; or

(3) 5 percent of the member's aggregate amount of outstanding advances.

(b) *Timing of minimum stock purchase.* (1) Within 60 calendar days after an institution is approved for membership in a Bank, the institution shall purchase its minimum stock requirement as set forth in paragraph (a) of this section.

(2) In the case of a Bank that has not converted to the capital structure authorized by the GLB Act, an institution that has been approved for membership may elect to purchase its minimum stock requirement in installments, provided that not less than one-fourth of the total amount shall be purchased within 60 calendar days of the date of approval of membership, and that a further sum of not less than one-fourth of such total shall be purchased at the end of each succeeding period of four months from the date of approval of membership.

(c) *Commencement of membership.* An institution that has been approved for membership shall become a member at the time it purchases its minimum stock requirement or the first installment thereof pursuant to this section.

(d) *Failure to purchase minimum stock requirement.* If an institution that has submitted an application and been approved for membership fails to purchase its minimum stock requirement or its first installment within 60 calendar days of the date of its approval for membership, such approval shall be null and void and the

institution, if it wants to become a member, shall be required to submit a new application for membership.

(e) *Reports.* The Bank shall make reports to FHFA setting forth purchases by institutions approved for membership of their minimum stock requirement pursuant to this section and in accordance with the instructions provided in the Data Reporting Manual issued by FHFA, as amended from time to time.

§ 1263.21 Issuance and form of stock.

(a) A Bank shall issue to each new member, as of the effective date of membership, stock in the member's name for the amount of stock purchased and paid for in full.

(b) If the member purchases stock in installments, the stock shall be issued in installments with the appropriate number of shares issued after each payment is made.

(c) A Bank that has not converted to the capital structure authorized by the GLB Act may issue stock in certificated or uncertificated form at the discretion of the Bank.

(d) A Bank that has not converted to the capital structure authorized by the GLB Act may convert all outstanding certificated stock to uncertificated form at its discretion.

§ 1263.22 Adjustments in stock holdings.

(a) *Adjustment in general.* A Bank may from time to time increase or decrease the amount of stock any member is required to hold.

(b)(1) *Annual adjustment.* A Bank shall calculate annually, in the manner set forth in § 1263.20(a), each member's required minimum holdings of stock in the Bank in which it is a member using calendar year-end financial data provided by the member to the Bank, pursuant to § 1263.31(d), and shall notify each member of the adjustment. The notice shall clearly state that the Bank's calculation of each member's minimum stock holdings is to be used to determine the number of votes that the member may cast in that year's election of directors and shall identify the State within the district in which the member will vote. A member that does not agree with the Bank's calculation of the minimum stock requirement or with the identification of its voting State may request FHFA to review the Bank's determination. FHFA shall promptly determine the member's minimum required holdings and its proper voting State, which determination shall be final.

(2) *Redemption of excess shares.* If, in the case of a Bank that has not converted to the capital structure authorized by the GLB Act and after the annual adjustment required by paragraph (b)(1) of this section is made, the amount of stock that a member is required to hold is decreased, the Bank may, in its discretion and upon proper application of the member, retire such excess stock, and the Bank shall pay for each share upon surrender of the stock an amount equal to the par value thereof (except that if at any time FHFA finds that the paid-in capital of a Bank is or is likely to be impaired as a result of losses in or depreciation of the assets held, the Bank shall on the order of FHFA withhold from the amount to be paid in retirement of the stock a *pro rata* share of the amount of such impairment as determined by FHFA) or, at its election, the Bank may credit any part of such payment against the member's debt to the Bank. The Bank's authority to retire such excess stock shall be further subject to the limitations of section 6(f) of the Bank Act (12 U.S.C. 1426(f)).

(c) A member's stock holdings shall not be reduced under this section to an amount less than required by sections 6(b) and 10(c) of the Bank Act (12 U.S.C. 1426(b), 1430(c)).

§ 1263.23 Excess stock.

(a) *Sale of excess stock.* Subject to the restriction in paragraph (b) of this section, a member may purchase excess stock as long as the purchase is approved by the member's Bank and is permitted by the laws under which the member operates.

(b) *Restriction.* Any Bank with excess stock greater than 1 percent of its total assets shall not declare or pay any dividends in the form of additional shares of Bank stock or otherwise issue any excess stock. A Bank shall not issue excess stock, as a dividend or otherwise, if after the issuance, the outstanding excess stock at the Bank would be greater than 1 percent of its total assets.

Subpart E—Consolidations Involving Members

§ 1263.24 Consolidations involving members.

(a) *Consolidation of members.* Upon the consolidation of two or more institutions that are members of the same Bank into one institution operating under the charter of one of the consolidating institutions, the membership of the surviving institution shall continue and the membership of each disappearing institution shall terminate on the cancellation of its charter. Upon the consolidation of two or more institutions, at least two of which are members of different Banks, into one institution operating under the charter of one of the consolidating institutions, the membership of the surviving institution shall continue and the membership of each disappearing institution shall terminate upon cancellation of its charter, provided, however, that if more than 80 percent of the assets of the consolidated institution are derived from the assets of a disappearing institution, then the consolidated institution shall continue to be a member of the Bank of which that disappearing institution was a member prior to the consolidation, and the membership of the other institutions shall terminate upon the effective date of the consolidation.

(b) *Consolidation into nonmember*—(1) *In general.* Upon the consolidation of a member into an institution that is not a member of a Bank, where the consolidated institution operates under the charter of the nonmember institution, the membership of the disappearing institution shall terminate upon the cancellation of its charter.

(2) *Notification.* If a member has consolidated into a nonmember that has its principal place of business in a State in the same Bank district as the former member, the consolidated institution shall have 60 calendar days after the cancellation of the charter of the former member within which to notify the Bank of the former member that the consolidated institution intends to apply for membership in such Bank. If the consolidated institution does not so notify the Bank by the end of the period, the Bank shall require the liquidation of any outstanding indebtedness owed by the former member, shall settle all outstanding business transactions with the former member, and shall redeem or repurchase the Bank stock owned by the former member in accordance with § 1263.29.

(3) *Application.* If such a consolidated institution has notified the appropriate Bank of its intent to apply for membership, the consolidated institution shall submit an application for membership within 60 calendar days of so notifying the Bank. If the consolidated institution does not submit an application for membership by the end of the period, the Bank shall require the liquidation of any outstanding indebtedness owed by the former member, shall settle all outstanding business transactions with the former member, and shall redeem or repurchase the Bank stock owned by the former member in accordance with § 1263.29.

(4) *Outstanding indebtedness.* If a member has consolidated into a nonmember institution, the Bank need

not require the former member or its successor to liquidate any outstanding indebtedness owed to the Bank or to redeem its Bank stock, as otherwise may be required under § 1263.29, during:

(i) The initial 60 calendar-day notification period;

(ii) The 60 calendar-day period following receipt of a notification that the consolidated institution intends to apply for membership; and

(iii) The period of time during which the Bank processes the application for membership.

(5) *Approval of membership.* If the application of such a consolidated institution is approved, the consolidated institution shall become a member of that Bank upon the purchase of the amount of Bank stock required by section 6 of the Bank Act (12 U.S.C. 1426). If a Bank's capital plan has not taken effect, the amount of stock that the consolidated institution is required to own shall be as provided in §§ 1263.20 and 1263.22. If the capital plan for the Bank has taken effect, the amount of stock that the consolidated institution is required to own shall be equal to the minimum investment established by the capital plan for that Bank.

(6) *Disapproval of membership.* If the Bank disapproves the application for membership of the consolidated institution, the Bank shall require the liquidation of any outstanding indebtedness owed by, and the settlement of all other outstanding business transactions with, the former member, and shall redeem or repurchase the Bank stock owned by the former member in accordance with § 1263.29.

(c) *Dividends on acquired Bank stock.* A consolidated institution shall be entitled to receive dividends on the Bank stock that it acquires as a result of a consolidation with a member in accordance with applicable FHFA regulations.

(d) *Stock transfers.* With regard to any transfer of Bank stock from a disappearing member to the surviving or consolidated member, as appropriate, for which the approval of FHFA is required pursuant to section 6(f) of the Bank Act (12 U.S.C. 1426(f)), as in effect prior to November 12, 1999, such transfer shall be deemed to be approved by FHFA by compliance in all applicable respects with the requirements of this section.

Subpart F—Withdrawal and Removal From Membership

§ 1263.25 [Reserved]

§ 1263.26 Voluntary withdrawal from membership.

(a) *In general.* (1) Any institution may withdraw from membership by providing to the Bank written notice of its intent to withdraw from membership. A member that has so notified its Bank shall be entitled to have continued access to the benefits of membership until the effective date of its withdrawal. The Bank need not commit to providing any further services, including advances, to a withdrawing member that would mature or otherwise terminate subsequent to the effective date of the withdrawal. A member may cancel its notice of withdrawal at any time prior to its effective date by providing a written cancellation notice to the Bank. A Bank may impose a fee on a member that cancels a notice of withdrawal, provided that the fee or the manner of its calculation is specified in the Bank's capital plan.

(2) A Bank shall notify FHFA within 10 calendar days of receipt of any notice of withdrawal or notice of cancellation of withdrawal from membership.

(b) *Effective date of withdrawal.* The membership of an institution that has submitted a notice of withdrawal shall terminate as of the date on which the last of the applicable stock redemption periods ends for the stock that the member is required to hold, as of the date that the notice of withdrawal is submitted, under the terms of a Bank's capital plan as a condition of membership, unless the institution has cancelled its notice of withdrawal prior to the effective date of the termination of its membership.

(c) *Stock redemption periods.* The receipt by a Bank of a notice of withdrawal shall commence the applicable 6-month and 5-year stock redemption periods, respectively, for all of the Class A and Class B stock held by that member that is not already subject to a pending request for redemption. In the case of an institution, the membership of which has been terminated as a result of a merger or other consolidation into a nonmember or into a member of another Bank, the applicable stock redemption periods for any stock that is not subject to a pending notice of redemption shall be deemed to commence on the date on which the charter of the former member is cancelled.

(d) *Certification.* No institution may withdraw from membership unless, on the date that the membership is to terminate, there is in effect a certification from FHFA that the withdrawal of a member will not cause the Bank System to fail to satisfy its requirements under section 21B(f)(2)(C) of the Bank Act (12 U.S.C. 1441b(f)(2)(C)) to contribute toward the interest payments owed on obligations issued by the Resolution Funding Corporation.

§ 1263.27 Involuntary termination of membership.

(a) *Grounds.* The board of directors of a Bank may terminate the membership of any institution that:

(1) Fails to comply with any requirement of the Bank Act, any regulation adopted by FHFA, or any requirement of the Bank's capital plan;

(2) Becomes insolvent or otherwise subject to the appointment of a conservator, receiver, or other legal custodian under Federal or State law; or

(3) Would jeopardize the safety or soundness of the Bank if it were to remain a member.

(b) *Stock redemption periods.* The applicable 6-month and 5-year stock redemption periods, respectively, for all of the Class A and Class B stock owned by a member and not already subject to a pending request for redemption, shall commence on the date that the Bank terminates the institution's membership.

(c) *Membership rights.* An institution whose membership is terminated involuntarily under this section shall cease being a member as of the date on which the board of directors of the Bank acts to terminate the membership, and the institution shall have no right to obtain any of the benefits of membership after that date, but shall be entitled to receive any dividends declared on its stock until the stock is redeemed or repurchased by the Bank.

§ 1263.28 [Reserved]

Subpart G—Orderly Liquidation of Advances and Redemption of Stock

§ 1263.29 Disposition of claims.

(a) *In general.* If an institution withdraws from membership or its membership is otherwise terminated, the Bank shall determine an orderly manner for liquidating all outstanding indebtedness owed by that member to the Bank and for settling all other claims against the member. After all such obligations and claims have been extinguished or settled, the Bank shall return to the member all collateral pledged by the member to the Bank to secure its obligations to the Bank.

(b) *Bank stock.* If an institution that has withdrawn from membership or that

otherwise has had its membership terminated remains indebted to the Bank or has outstanding any business transactions with the Bank after the effective date of its termination of membership, the Bank shall not redeem or repurchase any Bank stock that is required to support the indebtedness or the business transactions until after all such indebtedness and business transactions have been extinguished or settled.

Subpart H—Reacquisition of Membership

§ 1263.30 Readmission to membership.

(a) *In general.* An institution that has withdrawn from membership or otherwise has had its membership terminated and which has divested all of its shares of Bank stock, may not be readmitted to membership in any Bank, or acquire any capital stock of any Bank, for a period of 5 years from the date on which its membership terminated and it divested all of its shares of Bank stock.

(b) *Exceptions.* An institution that transfers membership between two Banks without interruption shall not be deemed to have withdrawn from Bank membership or had its membership terminated.

Subpart I—Bank Access to Information

§ 1263.31 Reports and examinations.

As a condition precedent to Bank membership, each member:

(a) Consents to such examinations as the Bank or FHFA may require for purposes of the Bank Act;

(b) Agrees that reports of examinations by local, State or Federal agencies or institutions may be furnished by such authorities to the Bank or FHFA upon request;

(c) Agrees to give the Bank or the appropriate Federal banking agency, upon request, such information as the Bank or the appropriate Federal banking agency may need to compile and publish cost of funds indices and to publish other reports or statistical summaries pertaining to the activities of Bank members;

(d) Agrees to provide the Bank with calendar year-end financial data each year, for purposes of making the calculation described in § 1263.22(b)(1); and

(e) Agrees to provide the Bank with copies of reports of condition and operations required to be filed with the member's appropriate Federal banking agency, if applicable, within 20 calendar days of filing, as well as copies of any annual report of condition and operations required to be filed.

Subpart J—Membership Insignia

§ 1263.32 Official membership insignia.

Members may display the approved insignia of membership on their documents, advertising and quarters, and likewise use the words ''Member Federal Home Loan Bank System.''

CHAPTER IX—FEDERAL HOUSING FINANCE BOARD

PART 944—[REDESIGNATED AS PART 1290]

■ 3. Transfer 12 CFR part 944 from chapter IX, subchapter F, to chapter XII subchapter E and redesignate as 12 CFR part 1290.

■ 4. Revise the newly redesignated part 1290 to read as follows:

PART 1290—COMMUNITY SUPPORT REQUIREMENTS

Sec.

1290.1 Definitions.
1290.2 Community support requirement.
1290.3 Community support standards.
1290.4 Decision on community support statements.
1290.5 Restrictions on access to long-term advances.
1290.6 Bank community support programs.
1290.7 Reports.

Authority: 12 U.S.C. 1430(g), 4511, 4513.

§ 1290.1 Definitions.

For purposes of this part:

Advisory Council means the Advisory Council each Bank is required to establish pursuant to section 10(j)(11) of the Federal Home Loan Bank Act (12 U.S.C. 1430(j)(11)) and part 1291 of this chapter.

Appropriate Federal banking agency has the meaning set forth in section 3(q) of the Federal Deposit Insurance Act (12 U.S.C. 1813(q)) and, for federally insured credit unions, means the National Credit Union Administration.

Appropriate State regulator means any State officer, agency, supervisor, or other entity that has regulatory authority over, or is empowered to institute enforcement action against, a particular institution.

Bank means a Federal Home Loan Bank established under section 12 of the Federal Home Loan Bank Act (12 U.S.C. 1432).

CDFI Fund means the Community Development Financial Institutions Fund established under section 104(a) of the Community Development Banking and Financial Institutions Act of 1994 (12 U.S.C. 4703(a)).

Community development financial institution or CDFI means an institution that is certified as a community development financial institution by the CDFI Fund under the Community Development Banking and Financial Institutions Act of 1994 (12 U.S.C. 4701 *et seq.*).

CRA means the Community Reinvestment Act of 1977, as amended (12 U.S.C. 2901, *et seq.*).

CRA evaluation means the public disclosure portion of the CRA performance evaluation provided by a member's appropriate Federal banking agency.

Displaced homemaker means an adult who has not worked full-time, full-year in the labor force for a number of years, and during that period, worked primarily without remuneration to care for a home and family, and currently is unemployed or underemployed and is experiencing difficulty in obtaining or upgrading employment.

FHFA means Federal Housing Finance Agency.

First-time homebuyer means:

(1) An individual and his or her spouse, if any, who has had no present ownership interest in a principal residence during the three-year period prior to purchase of a principal residence.

(2) A displaced homemaker who, except for owning a residence with his or her spouse or residing in a residence owned by his or her spouse, meets the requirements of paragraph (1) of this definition.

(3) A single parent who, except for owning a residence with his or her spouse or residing in a residence owned by his or her spouse, meets the requirements of paragraph (1) of this definition.

Long-term advance means an advance with a term to maturity greater than one year.

Restriction on access to long-term advances means a member may not borrow long-term advances or renew any maturing advance for a term to maturity greater than one year.

Single parent means an individual who is unmarried or legally separated from a spouse and has custody or joint custody of one or more minor children or is pregnant.

Targeted community lending means providing financing for economic development projects for targeted beneficiaries.

§ 1290.2 Community support requirement.

(a) *Selection for community support review.* Except as otherwise provided in this section, FHFA shall select a member for community support review approximately once every two years.

(b) *Notice*—(1) *By the FHFA.* FHFA concurrently shall:

(i) Notify each Bank of the members within its district that have to submit

community support statements during the calendar quarter; and

(ii) Publish a notice in the **Federal Register** that includes the name and address of each member required to submit a community support statement during the calendar quarter, and the deadline for submission of the community support statement to FHFA. The deadline for submission of a community support statement shall be no earlier than 45 calendar days after the date of publication of the notice in the **Federal Register**.

(2) *By the Banks.* Within 15 calendar days of the date of publication in the **Federal Register** of the notice required by paragraph (b)(1)(ii) of this section, a Bank shall provide written notice to—

(i) Each member within its district that is named in the **Federal Register** notice, that the member has to submit a community support statement to FHFA by the deadline stated in the **Federal Register** notice; and

(ii) Its Advisory Council and nonprofit housing developers, community groups, and other interested parties in its district of the name and address of each member within its district that has to submit a community support statement during the calendar quarter.

(c) *Required documents.* Each member selected for community support review must submit a completed Community Support Statement Form executed by an appropriate senior officer to FHFA and any other information FHFA may require to determine whether a member meets the community support standards.

(d) *Public comments.* In reviewing a member for compliance with the community support requirement, FHFA shall take into consideration any public comments it has received concerning the member.

(e) *Community Development Financial Institutions.* A member that has been certified as a community development financial institution by the CDFI Fund, other than a member that also is an insured depository institution or a CDFI credit union (as defined in § 1263.1), shall be deemed to be in compliance with the community support requirements of section 10(g) of the Federal Home Loan Bank Act (Bank Act), 12 U.S.C. 1430(g), by virtue of that certification and is not subject to periodic review under paragraph (a) of this section.

§ 1290.3 Community support standards.

(a) *In general.* In reviewing a community support statement, FHFA shall take into account a member's performance under the CRA if the member is subject to the requirements of the CRA, and the member's record of lending to first-time homebuyers.

(b) *CRA standard*—(1) *Adequate performance.* A member that is subject to the requirements of the CRA shall be deemed to meet the CRA standard if the rating in the member's most recent CRA evaluation is ''outstanding'' or ''satisfactory.''

(2) *Probationary performance.* A member that is subject to the requirements of the CRA shall be subject to a probationary period if the rating in the member's most recent CRA evaluation is ''Needs to Improve.'' The probationary period shall extend until the member's appropriate Federal banking agency completes its next CRA evaluation and issues a rating. The member will be eligible to receive long-term advances during the probationary period. If the member does not meet the CRA standard at the end of the probationary period, FHFA will restrict the member's access to long-term advances in accordance with § 1290.5.

(3) *Inadequate performance.* FHFA will restrict a member's access to long-term advances in accordance with § 1290.5 if the rating in the member's most recent CRA evaluation is ''Substantial Non-Compliance.''

(c) *First-time homebuyer standard*—(1) *Adequate performance.* In the absence of public comments or other information to the contrary, FHFA will presume that a member meets the first-time homebuyer standard if the member is subject to the requirements of the CRA and the rating in the member's most recent CRA evaluation is ''outstanding.'' In determining whether other members meet the first-time homebuyer standard, FHFA will consider a member's description of its efforts to assist first-time or potential first-time homebuyers or its explanation of factors that affect its ability to assist first-time or potential first-time homebuyers. A member shall be deemed to meet the first-time homebuyer standard if the member otherwise demonstrates to the satisfaction of FHFA that it:

(i) Has an established record of lending to first-time homebuyers;

(ii) Has a program whereby it actively seeks to lend or support lending to first-time homebuyers, including, but not limited to, the following—

(A) Providing special credit products with flexible underwriting standards for first-time homebuyers;

(B) Participating in Federal, State, or local government, or nationwide homeownership lending programs that benefit, serve, or are targeted to, first-time homebuyers; or

(C) Participating in loan consortia for first-time homebuyer loans or loans that serve predominantly low- or moderate-income borrowers;

(iii) Has a program whereby it actively seeks to assist or support organizations that assist potential first-time homebuyers to qualify for mortgage loans, including, but not limited to, the following—

(A) Providing, participating in, or supporting special counseling programs or other homeownership education activities that benefit, serve, or are targeted to, first-time homebuyers;

(B) Providing or participating in marketing plans and related outreach programs targeted to first-time homebuyers;

(C) Providing technical assistance of financial support to organizations that assist first-time homebuyers;

(D) Participating with or financially supporting community or nonprofit groups that assist first-time homebuyers;

(E) Holding investments or making loans that support first-time homebuyer programs;

(F) Holding mortgage-backed securities that may include a pool of loans to low- and moderate-income homebuyers;

(G) Participating or investing in service organizations that assist credit unions in providing mortgages; or

(H) Participating in Bank targeted community lending programs; or

(iv) Has any combination of the elements described in paragraphs (c)(1)(i), (ii), or (iii) of this section.

(2) *Probationary performance.* If FHFA deems the evidence of first-time homebuyer performance to be unsatisfactory, the member will be subject to a one-year probationary period. The member will be eligible to receive long-term advances during the probationary period. If the member does not demonstrate compliance with the first-time homebuyer standard before the probationary period ends, FHFA will restrict the member's access to long-term advances in accordance with § 1290.5.

(3) *Inadequate performance.* FHFA will restrict a member's access to long-term advances in accordance with § 1290.5 if the member provides no evidence of first-time homebuyer performance.

§ 1290.4 Decision on community support statements.

(a) *Action on community support statements.* FHFA will act on each community support statement in accordance with the requirements of § 1290.3 within 75 calendar days of the date FHFA deems the community

support statement to be complete. FHFA will deem a community support statement complete when it has obtained all of the information required by this part and any other information it deems necessary to process the community support statement. If FHFA determines during the review process that additional information is necessary to process the community support statement, FHFA may deem the community support statement incomplete and stop the 75-day time period by providing written notice to the member. When FHFA receives the additional information, it shall again deem the community support statement complete and resume the 75-day time period where it stopped. FHFA will have 10 calendar days in addition to the 75-day time period to act on a community support statement if FHFA receives the additional information on or after the seventieth day of the 75-day time period.

(b) *Decision on community support statements.* FHFA will provide written notice to the member and the member's Bank of its determination regarding the community support statement submitted by the member. The notice will identify the reasons for FHFA's determination.

§ 1290.5 Restrictions on access to long-term advances.

(a) *Requirement.* FHFA will restrict a member's access to long-term advances if the member:

(1) Failed to comply with the requirements of this part;

(2) Submitted a community support statement that was not approved by FHFA;

(3) Did not receive a rating in a CRA evaluation of ''outstanding'' or ''satisfactory'' at the end of the probationary period described in § 1290.3(b)(2); or

(4) Failed to provide evidence satisfactory to FHFA of its first-time homebuyer performance before the end of the probationary period described in § 1290.3(c)(2).

(b) *Notice.* FHFA will provide written notice to a member and the member's Bank of its determination to restrict the member's access to long-term advances.

(c) *Effective date.* Restrictions on access to long-term advances will take effect 30 days after the date the notices required under paragraph (b) of this section are sent unless the member complies with the requirements of this part before the end of the 30-day period.

(d) *Removing restrictions.* (1) FHFA may remove restrictions on a member's access to long-term advances imposed under this section:

(i) If FHFA determines that application of the restriction may adversely affect the safety and soundness of the member. A member may submit a written request to FHFA to remove a restriction on access to long-term advances under this paragraph (d)(1)(i). The written request must include a clear and concise statement of the basis for the request, and a statement that application of the restriction may adversely affect the safety and soundness of the member from the member's appropriate Federal banking agency, or the member's appropriate State regulator for a member that is not subject to regulation or supervision by a Federal regulator. FHFA will consider each written request within 30 calendar days of receipt.

(ii) If FHFA determines that the member subsequently has complied with the requirements of this part. A member may submit a written request to FHFA to remove a restriction on access to long-term advances under this paragraph (d)(1)(ii). The written request must state with specificity how the member has complied with the requirements of this part. FHFA will consider each written request within 30 calendar days of receipt.

(2) FHFA will place a member on probation in accordance with § 1290.3(b)(2), if—

(i) The member's access to long-term advances was restricted on the basis of the member's inadequate performance under the CRA standard, as described in § 1290.3(b)(3);

(ii) The rating in the member's subsequent CRA evaluation is ''Needs to Improve;'' and

(iii) The member did not receive either a ''Substantial Non-Compliance'' CRA rating or a ''Needs to Improve'' CRA rating immediately preceding the CRA rating on which the member's inadequate performance under the CRA standard was based.

(3) FHFA will provide written notice to the member and the member's Bank of its determination under this paragraph (d). FHFA's determination takes effect on the date the notices are sent.

(e) *Community Investment Cash Advance (CICA) Programs.* A member that is subject to a restriction on access to long-term advances under this part is not eligible to participate in a CICA program offered under part 952 of this title and 1291 of this chapter. The restriction in this paragraph (e), does not apply to CICA applications or funding approved before the date the restriction is imposed.

§ 1290.6 Bank community support programs.

(a) *Requirement.* Consistent with the safe and sound operation of the Bank, each Bank shall establish and maintain a community support program. A Bank's community support program shall:

(1) Provide technical assistance to members;

(2) Promote and expand affordable housing finance;

(3) Identify opportunities for members to expand financial and credit services in underserved neighborhoods and communities;

(4) Encourage members to increase their targeted community lending and affordable housing finance activities by providing incentives such as awards or technical assistance to nonprofit housing developers or community groups with outstanding records of participation in targeted community lending or affordable housing finance partnerships with members; and

(5) Include an annual Targeted Community Lending Plan, approved by the Bank's board of directors and subject to modification, which shall require the Bank to—(i) Conduct market research in the Bank's district;

(ii) Describe how the Bank will address identified credit needs and market opportunities in the Bank's district for targeted community lending;

(iii) Consult with its Advisory Council and with members, housing associates, and public and private economic development organizations in the Bank's district in developing and implementing its Targeted Community Lending Plan; and

(iv) Establish quantitative targeted community lending performance goals.

(b) *Notice.* A Bank shall provide annually to each of its members a written notice:

(1) Identifying CICA programs and other Bank activities that may provide opportunities for a member to meet the community support requirements and to engage in targeted community lending; and

(2) Summarizing targeted community lending and affordable housing activities undertaken by members, housing associates, nonprofit housing developers, community groups, or other entities in the Bank's district, that may provide opportunities for a member to meet the community support requirements and to engage in targeted community lending.

§ 1290.7 Reports.

Each Advisory Council annual report submitted to FHFA pursuant to section 10(j)(11) of the Bank Act (12 U.S.C. 1430(j)(11)) must include an analysis of the Bank's targeted community lending and affordable housing activities.

Dated: December 23, 2009.

Edward J. DeMarco,

Acting Director, Federal Housing Finance Agency.

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