

**List of Subjects****7 CFR Part 360**

Imports, Plants (Agriculture), Quarantine, Reporting and recordkeeping requirements, Transportation, Weeds.

**7 CFR Part 361**

Agricultural commodities, Imports, Labeling, Quarantine, Reporting and recordkeeping requirements, Seeds, Vegetables, Weeds.

**PART 360—NOXIOUS WEED REGULATIONS****PART 361—IMPORTATION OF SEED AND SCREENINGS UNDER THE FEDERAL SEED ACT**

■ Accordingly, we are adopting as a final rule, without change, the interim rule that amended 7 CFR parts 360 and 361 and that was published at 74 FR 53397-53400 on October 19, 2009.

Done in Washington, DC, this 27<sup>th</sup> day of April 2010.

**Kevin Shea**

*Acting Administrator, Animal and Plant Health Inspection Service.*

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**FEDERAL HOUSING FINANCE BOARD****12 CFR Parts 985 and 989****FEDERAL HOUSING FINANCE AGENCY****12 CFR Parts 1273 and 1274****RIN 2590-AA30****Board of Directors of Federal Home Loan Bank System Office of Finance**

**AGENCY:** Federal Housing Finance Agency.

**ACTION:** Final Rule.

**SUMMARY:** Governed by the Federal Housing Finance Agency's (FHFA) regulations, the Federal Home Loan Bank System's (Bank System) Office of Finance issues debt ("consolidated obligations") as agent for the Federal Home Loan Banks (Banks) on which the Banks are jointly and severally liable and publishes combined financial reports on the Banks so that members of the Bank System, investors in the consolidated obligations, and other interested parties can assess the strength of the Bank System that stands behind them. The Office of Finance (OF) is governed by a board of directors, the composition and functions of which are

determined by FHFA's regulations. FHFA's experience with the Bank System and with the OF's combined financial reports during the recent period of market stress suggests that the OF and the Bank System could benefit from a reconstituted board and strengthened audit committee. This regulation is intended to achieve that end.

**DATES:** This rule is effective June 2, 2010.

**FOR FURTHER INFORMATION CONTACT:**

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**SUPPLEMENTARY INFORMATION:****I. Background****A. Creation of the Federal Housing Finance Agency and Recent Legislation**

Effective July 30, 2008, the Housing and Economic Recovery Act of 2008 (HERA), Public Law 110-289, 122 Stat. 2654, transferred the supervisory and oversight responsibilities of the Office of Federal Housing Enterprise Oversight (OFHEO) over the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac) (collectively, the Enterprises), the oversight responsibilities of the Federal Housing Finance Board (FHFB or Finance Board) over the Banks and the Office of Finance (OF) (which acts as the Banks' fiscal agent), and certain functions of the Department of Housing and Urban Development to FHFA, a new independent executive branch agency. *See id.* at section 1101, 122 Stat. 2661-62. FHFA is responsible for ensuring that the Enterprises and the Banks operate in a safe and sound manner, including that they maintain adequate capital and internal controls, that their activities foster liquid, efficient, competitive, and resilient national housing finance markets, and that they carry out their public policy missions through authorized activities. *See id.* at section 1102, 122 Stat. 2663-64. The Enterprises, the Banks, and the OF continue to operate under regulations promulgated by OFHEO and the FHFB until FHFA issues its own regulations.

*See id.* at sections 1302, 1313, 122 Stat. 2795, 2798.

**B. The Bank System Generally**

The twelve Banks are instrumentalities of the United States organized under the Federal Home Loan Bank Act (Bank Act).<sup>1</sup> *See* 12 U.S.C. 1423, 1432(a). The Banks are cooperatives; only members of a Bank may purchase the capital stock of a Bank, and only members or certain eligible housing associates (such as state housing finance agencies) may obtain access to secured loans, known as advances, or other products provided by a Bank. *See* 12 U.S.C. 1426(a)(4), 1430(a), 1430b. Each Bank is managed by its own board of directors and serves the public interest by enhancing the availability of residential mortgage and community lending credit through its member institutions. *See* 12 U.S.C. 1427. Any eligible institution (generally a federally insured depository institution or state-regulated insurance company) may become a member of a Bank if it satisfies certain criteria and purchases a specified amount of the Bank's capital stock. *See* 12 U.S.C. 1424; 12 CFR part 1263.

As government-sponsored enterprises (GSEs), the Banks are granted certain privileges under federal law. In light of those privileges and their status as GSEs, the Banks typically can borrow funds at spreads over the rates on U.S. Treasury securities of comparable maturity lower than most other entities. The Banks pass along a portion of their GSE funding advantage to their members—and ultimately to consumers—by providing advances and other financial services at rates that would not otherwise be available to their members. Consolidated obligations (COs), consisting of bonds and discount notes, are the principal funding source for the Banks. The OF issues all COs on behalf of the twelve Banks. Although each Bank is primarily liable for the portion of consolidated obligations corresponding to the proceeds received by that Bank, each Bank is also jointly and severally liable with the other eleven Banks for the payment of principal and interest on all COs. *See* 12 CFR 966.9.

**C. The OF**

The OF was one of a number of joint Bank offices established by regulation by the former Federal Home Loan Bank Board (FHLBB), a predecessor agency to

<sup>1</sup> Each Bank is generally referred to by the name of the city in which it is located. The twelve Banks are located in: Boston, New York, Pittsburgh, Atlanta, Cincinnati, Indianapolis, Chicago, Des Moines, Dallas, Topeka, San Francisco, and Seattle.

FHFA. See 65 FR 324, 326 (Jan. 4, 2000). The OF was originally formed from two other joint Bank Offices, the Office of System Finance and the Office of Fiscal Agent. Among other things, OF was assigned the duties previously vested in the Fiscal Agent which included facilitating the issuance of COs. *Id.*

In 1989, as part of the amendments made to the Bank Act by the Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA),<sup>2</sup> all joint offices of the Bank System other than the OF were abolished. The FHLBB was also abolished and its regulatory authority over the Bank System, including the OF, was transferred to the Finance Board. The FHLBB's regulations were also transferred to the Finance Board. *Id.* In 1992, the Finance Board reorganized the OF as fiscal agent of the Finance Board for issuing COs under section 11(c) of the Bank Act, and set forth other duties for OF.<sup>3</sup> See 57 FR 11429 (Apr. 3, 1992) (*adopting* 12 CFR part 941). The regulation also instituted a three-member board of directors for the oversight and management of the OF, made up of two Bank presidents and a private United States citizen with demonstrated expertise in financial markets. *Id.*

In January 2000, the Finance Board proposed changes to its regulations to alter how COs were issued under section 11 of the Bank Act, reorganize the OF and its board of directors, and expand the duties of the OF, including assigning the OF the duty to prepare the Bank System combined annual and quarterly financial reports. See 65 FR 324. As proposed, the January 2000 regulation transferred authority for issuance of the Bank COs from the Finance Board, which had been issuing debt pursuant to then-existing authority under section 11(c) of the Bank Act, to the Banks themselves pursuant to authority under section 11(a) of the Bank Act and subject to the requirement, among other things, that all such debt issued by the Banks be the joint and several obligations of all twelve Banks and be issued through the OF as their agent. *Id.* Under the proposed regulation, the Finance Board retained the option to issue COs itself under section 11(c) of the Bank Act at any point in the future.

The Finance Board also believed that “[a]s a natural and necessary adjunct to the issuance of COs, the Banks also should be responsible for the preparation of the disclosure documents that facilitate CO issuance and for the periodic combined financial statements for the Bank System.” *Id.* at 325. The Finance Board therefore proposed that the OF, as the only joint Bank System office and existing agent for CO issuance, be assigned the duty of preparing the Bank System's combined financial reports. *Id.* The Finance Board also proposed to codify disclosure standards in the regulation, many of which had been set forth in a Finance Board policy statement. Other duties related to debt issuance and management were also proposed to be assigned to the OF.

In light of the expanded duties assigned to the OF as well as amendments to the Bank Act that had recently been made by the Gramm-Leach-Bliley Act (GLB Act) of 1999,<sup>4</sup> the Finance Board also thought it was appropriate to alter both the size and composition of the OF board. *Id.* at 326. The Finance Board had two main goals in proposing its changes. First, it wanted to build on the governance structure in the Bank Act by which the Banks should be provided greater autonomy to manage their affairs. Second, it wanted to assure each Bank had representation on the OF board to help achieve operational goals and wanted to assure that the OF board itself had directors with experience and qualification to help the OF meet the evolving needs of the Bank System.

After consideration of the comments on the proposed regulation, the Finance Board adopted many of the changes including those authorizing the Banks to issue COs under section 11(a) of the Bank Act and assigning to the OF the function of preparing the Bank System's combined financial reports, along with additional duties. See 65 FR 36290 (June 7, 2000) (*adopting* among other parts 12 CFR parts 966 and 985). The Finance Board did not, however, adopt the proposed changes to the OF board structure or composition. Instead, the new regulation incorporated the prior three-person board structure. The Finance Board also specified some additional duties for the OF board consistent with the additional functions that had been assigned to the OF over the years. Since the 2000 rulemaking, no significant changes to the regulations governing the OF have been proposed.

#### D. Proposed Rule

On August 4, 2009, FHFA published a proposed rule for comment which would have altered the structure, composition and duties of the OF board of directors and its audit committee. See 74 FR 38564. As proposed, the rule also would have transferred the current OF board regulations, as well as regulations related to Banks' financial statements, respectively from parts 985 and 989 of title 12 to parts 1273 and 1274 of Title 12.

The proposal would have expanded the OF board of directors to between fifteen and seventeen members, consisting of the twelve Bank presidents and from three to five Independent Directors (as defined under the rule). The proposed rule also would have created an Audit Committee for the OF board made up of the Independent Directors. The Audit Committee would have been assigned the duty to oversee the audit of the OF and the preparation of the Bank System's combined financial report. To help ensure that information from the Banks could be combined in a meaningful and accurate fashion in the combined financial report, the proposed rule also would have empowered the OF Audit Committee to require the Banks to establish common accounting policies and procedures with regard to information submitted to the OF. As with the current regulation, the proposed rule also set forth standards for the combined financial reports. The proposed rule addressed the duties of the OF board of directors generally, although it would have carried over many of the provisions in the current regulations with regard to the OF board's duties.

Under the proposed rule, FHFA would have selected the initial Independent Directors for staggered terms of up to five years.<sup>5</sup> Each Bank was given the right to nominate one candidate for appointment. Thereafter, Independent Directors would have been elected by the full board of directors for five-year terms, subject to the right of FHFA to review and object to a particular Independent Director's election, reserving to FHFA the right to appoint Independent Directors if it thought the OF board had not elected suitably qualified persons. Under the proposed rule, FHFA also would have appointed the first chairman of the reconstituted OF board from among the Independent Directors and a vice chairman from among all directors.

<sup>5</sup> Terms would have been staggered such that no more than one Independent Director's seat would be scheduled to become vacant in any year.

<sup>2</sup> Public Law 101-73, 103 Stat. 183 (Aug. 9, 1989).

<sup>3</sup> As it existed in 1992, section 11(c) of the Bank Act provided the Finance Board authority to issue the debt on which the Banks were jointly and severally liable. 12 U.S.C. 1431(c)(1992). HERA recently amended this provision and removed authority from the regulator to issue such debt on behalf of the Banks and provided the OF as agent for the Banks with authority to issue the COs. See section 1204(3)(B), Pub. L. 110-289, 122 Stat. 2786.

<sup>4</sup> Pub. L. 106-102, 113 Stat. 1338 (Nov. 12, 1999).

Thereafter, the chairman would be elected by the full board of directors from among the Independent Directors and the vice chairman would be elected by the board from among all directors. The proposed rule also set standards for a quorum for board meetings, established a minimum number of board meetings per year, and addressed issues related to board committees and other matters such as compensation and indemnification of directors.

The proposed rule also would have readopted current regulations addressing the financial statements for the Banks, subject to technical corrections made necessary by proposed changes in the composition and duties of the OF Audit Committee. *See* 12 CFR part 989. The proposed rule also would have made changes to part 989 to reflect the fact that the Banks had registered equity securities with the Securities and Exchange Commission subsequent to the adoption of these requirements.

The proposed rule originally had a comment period of 60 days, which was set to close on October 5, 2009. This comment period was later extended for an additional 30 days. *See* 74 FR 50926 (Oct. 2, 2009). FHFA received 23 comment letters on the proposed rule. These comments are discussed below.

#### *E. Considerations of Differences Between the Banks and the Enterprises*

Section 1201 of HERA (codified at 12 U.S.C. 4513(f)) requires the Director, when promulgating regulations relating to the Banks, to consider the following differences between the Banks and the Enterprises: Cooperative ownership structure; Mission of providing liquidity to members; Affordable housing and community development mission; capital structure; and Joint and several liability. The Director also may consider any other differences that are deemed appropriate. In preparing this final regulation, FHFA considered the differences between the Banks and the Enterprises as they relate to the above factors, and determined that the rule is appropriate.

## **II. The Final Rule**

### *A. Comments*

FHFA received 23 comment letters on the proposed rule from the Banks, the OF, trade associations, and individual representing members. The OF along with eleven of the twelve Banks submitted a single joint comment letter, while the remaining Bank submitted its own comment letter. FHFA also received comments from six trade associations that represent Bank System members, as well as fifteen letters from

individuals representing member institutions. Copies of the comments are available at FHFA's Web site, <http://www.fhfa.gov>.

The comments generally supported the proposed expansion of the OF board of directors to include all twelve Bank presidents and additional independent directors. The comments were also generally supportive of the proposal to establish for the OF an Audit Committee made up of Independent Directors. The commenters opposed, however, some of the specific powers and duties assigned to the Audit Committee under the proposed rule, especially those provisions mandating the Audit Committee to require the Banks to adopt common accounting policies. A number of commenters felt that some of the duties and authority assigned to the Audit Committee should be vested in the full OF Board or were inconsistent with the role and authority of the individual Banks' boards of directors and audit committees.

Commenters also felt that the duties that would be assigned to either the OF board of directors or its Audit Committee should not be described by reference to the part 917 rules. The commenters noted that the part 917 rules addressed the duties and authority of the individual Banks' board of directors and that the relationship of the OF to the Banks was different from the relationship of a Bank to its members. A number of commenters suggested that the duties of the OF board of directors or Audit Committee be limited specifically to those enumerated in the rule. Some commenters also believed that the proposed rule gave FHFA too much authority to appoint Independent Directors and to overrule decisions of the OF board of directors and urged FHFA to change these provisions. Commenters also made specific suggestions of wording changes in a number of proposed provisions of the rule that they believed would clarify the meaning of the provision or otherwise improve the rule.

### *B. Final Rule Provisions*

FHFA has considered all the comments in developing the final rule. It has accepted a number of the suggestions made by commenters and, as discussed below, has made changes in the final rule as a result. FHFA believes, however, that the basic approach of the proposed rule remains correct, as do its underlying reasons for initially proposing the changes. FHFA views the changes in this final rule as an important step in assisting the Banks to coordinate among themselves the process of providing the OF with

information to prepare the Bank System's combined financial reports and assisting the OF otherwise to obtain information where the coordination process has not worked well. Most importantly, FHFA continues to believe that high-quality combined financial reports play an important role in the ability of the Banks to access financial markets and issue debt and that they provide financial markets with needed information about the Bank System. Therefore, much of the proposed rule is carried over into the final regulation, albeit often with some small changes in language to clarify the extent and scope of the provision in question. Comments, and the changes that FHFA has made to the rule, are discussed in more detail below in the section describing each final rule provision.

### Section 1273.1—Definitions

FHFA has adopted the definitions as proposed. FHFA did not receive any comments that addressed the proposed definitions directly, although one commenter suggested using a term other than "Independent Director" since the term is used somewhat differently under the rule than in the general corporate governance context. FHFA has considered this comment, but is continuing to use the term Independent Director. The qualifications for Independent Director are set forth in the rule. The definition of this term makes clear that the term means a party that meets such qualifications, and its use is not intended to imply any other meaning. Thus, FHFA has not made the requested change.<sup>6</sup>

### Section 1273.2—Authority of the OF

FHFA has adopted this section as proposed. The provision, as proposed, was similar to § 985.2 which had previously set forth the OF authority. The proposed provision reflected the fact that HERA amended section 11 of the Bank Act so that the regulator was no longer authorized to issue COs. *See* Public Law 110–289, Div. A, Title II, section 1204(3) (*amending* 12 U.S.C. 1431(b) and (c)). Thus, § 1273.2 as adopted, unlike former § 985.2, does not provide that the OF may act as agent for FHFA in the issuance of COs.

### Section 1273.3—Functions of the OF

FHFA has made a number of clarifying changes in the final version of § 1273.3, which describes the general functions of the OF, in response to

<sup>6</sup> Additional comments were received on the proposed qualifications for an Independent Director. These comments are discussed below in the section addressing § 1273.7, which sets out the qualifications for Independent Directors.

comments on the proposed rule. These changes do not alter the scope of the proposed provision, but FHFA believes that the changes will make its original intent more clear.

First, FHFA has altered § 1273.3(a) to provide that, in the offering, issuance and servicing of COs, the OF is acting as agent for the Banks. As originally proposed, the provision merely stated that the OF was agent. Some comments indicated that language in this provision and in § 1273.6 should make clear that the OF administers these functions on behalf of the Banks but is not the issuer of debt and does not enjoy independent authority to undertake these activities. FHFA believes that the change in the final rule, along with the description in § 1273.2 that OF acts as agent for the Banks makes clear that the OF is not acting independently of the Banks in these activities. Moreover, the language in § 1273.3(a) now closely follows the language in section 11(b) and (c) of the Bank Act, as amended by HERA, which states that “the Office of Finance as agent for the Banks may issue” consolidated Bank debentures or bonds.<sup>7</sup>

Second, FHFA has changed § 1273.3(b) to clarify that, in preparing the combined financial reports, the OF shall apply consistent accounting policies and procedures as provided under § 1273.9(b). Commenters urged that the reference to “consistent accounting policies and procedures” should be removed from this section, and from § 1273.6(b)(2), because the references were confusing and raised issues as to whether the language created a “consistency” requirement beyond or in addition to that set forth in § 1273.9(b). FHFA believes that the change in the language makes clear that language in this section is referencing § 1273.9(b) and is not creating a “consistency” requirement independent or separate from that under § 1273.9(b). The provision makes clear, however, that the OF has the duty to apply policies adopted under § 1273.9(b) in preparing the Bank System combined financial reports.<sup>8</sup>

Commenters also asked that § 1273.3 be changed to specifically limit the OF's functions to those listed in the section. FHFA sees no need for this change. As now written, the provisions clearly delineate the OF functions, and FHFA does not believe the rule as adopted is

vague or will be subject to expansive interpretation.

#### Section 1273.4—FHFA Oversight

As proposed, the provision would have carried over Finance Board regulation § 985.5 with minor technical changes. It also would have added a new paragraph (c) that provided that FHFA would determine whether a combined Bank System annual or quarterly financial report complied with the standards of the part 1273 regulations, a provision that in scope and content was basically the same as Finance Board rule § 985.6(b)(5). One commenter noted that the ramifications of this proposed section were unclear and was not sure why the section was included in the regulation. The commenter asked that the section be removed or expanded to better explain its purpose.

FHFA disagrees that the provision is unclear. As proposed, the provision described FHFA's general oversight authority with regard to the OF, and provided more specific statements about FHFA's examination of the OF and its oversight of the combined financial reports. FHFA agrees that, because of revisions made by HERA the provision needs revision from what was proposed. Prior to HERA, the Bank Act did not clearly delineate the regulator's authority over the OF. HERA, however, added provisions to the Bank Act and the Federal Housing Enterprises Financial Safety and Soundness Act of 1992<sup>9</sup> which more clearly define this authority. Paragraph (a) therefore has been changed to make specific reference to FHFA regulatory authority over the OF under these statutes.

#### Section 1273.5—Funding of the OF

As proposed, § 1273.5 set forth the Banks' responsibility for jointly funding the OF and the process for, and other requirements related to, this funding. The rule, as proposed, carried over most of the provisions that had been in Finance Board regulation § 985.5. FHFA proposed certain changes to the Finance Board requirements, however. Most significantly, the proposed rule allowed that each Bank's *pro rata* share of the OF's expenses could be calculated by any reasonable formula set by the OF Board of Directors, subject to FHFA's review and right to require the OF to make changes to that formula. By contrast, under the Finance Board's regulation, the formula was specified in the rule, although the OF board retained the right to implement an alternative

funding formula with the Finance Board's approval.

FHFA received one comment that was generally supportive of the approach in the proposed rule for establishing the method of calculating each Bank's share of the OF's funding. Another commenter believed, however, that FHFA did not need to reserve authority to require the OF board of directors to change the formula. The commenter stated that the rule required that any formula be reasonable and that FHFA maintained its general oversight and enforcement authority to enforce this requirement so that the agency could take action if the OF board of directors did not adopt a reasonable approach to calculating each Bank's share of the OF's expenses.

FHFA considered this comment asking for a change to the provision but decided not to alter the proposed approach to establishing the funding formula. FHFA believes the approach in § 1273.5 will provide greater flexibility than the approach in the Finance Board regulation while maintaining regulatory oversight to make sure any formula remains fair to all Banks and provides for adequate funding of the OF. By removing from the rule a specific formula for calculating each Bank's share of the OF expenses and the requirement that the OF Board of Directors obtain pre-approval from FHFA for any change to such formula, § 1273.5 will allow the OF board of directors to take action in response to changed conditions while allowing FHFA to intervene quickly if needed. Thus, FHFA is adopting § 1273.5 as proposed.

#### Section 1273.6—Debt Management Duties of the OF

Proposed § 1273.6 described the debt management duties of the OF, and these duties substantively remained similar to those set forth in Finance Board regulation § 985.6. As indicated in the notice of proposed rulemaking, however, FHFA proposed certain changes to the standards governing the preparation of the combined financial report. These proposed changes were needed, among other reasons, to conform the duties in this section to new responsibilities proposed for the Audit Committee with regard to ensuring consistency of information provided by the Banks for use in the combined financial reports. See 74 FR at 38566, 38567. As already discussed, FHFA received comments on certain aspects of proposed § 1273.6 and has made clarifying changes to the proposed language similar to changes made to proposed language in § 1273.3. See notes 7 and 8, *supra*.

<sup>7</sup> FHFA is adopting a similar change to wording in § 1273.6(a) for the same reasons discussed here.

<sup>8</sup> FHFA is adopting a similar change to the language in § 1273.6(b)(2) for the same reasons discussed here.

<sup>9</sup> 12 U.S.C. 4501 *et seq.*

FHFA also received comments asking that it alter § 1273.6(b)(4) so that the deadline for publication of the combined financial report be 21 days after the Banks' filing deadline with the SEC. The commenters indicated that this would give the OF sufficient time to complete the combined reports after each Bank finalized its reporting to the SEC. After considering this request, FHFA is not altering the deadline for publication of the quarterly and annual combined financial reports. The Bank System is one of the largest non-governmental issuers of debt in the world, with the level of outstanding COs approaching \$1 trillion. The combined financial report is an important and convenient source of information for investors and other parties interested in the Bank System and Bank System debt. FHFA believes that timely publication of the combined financial report is important to the Banks' continued access to financial markets. Therefore, the combined reports are as important, if not more so, than the individual Bank reports. FHFA, therefore, expects that the OF and the Banks will take whatever steps are necessary to file the combined financial reports on the schedule set forth in SEC rules for the individual Banks. Further, given the limited nature of the Banks' business lines—advances, and in some cases acquired member assets—and the limited universe of their investment activities, FHFA also thinks the deadlines set forth in the rule are reasonable.

With regard to the requirements for delivering copies of the combined reports to the Banks and Bank members also found in § 1273.6(b)(4), FHFA confirms that OF may continue to rely on Finance Board Regulatory Interpretation 2007–RI–01 (Jan. 19, 2007), which sets forth terms and conditions for the electronic distribution of these financial reports, to meet these requirements.

Other commenters suggested that FHFA modify § 1273.6 to give the OF Board of Directors authority to limit issuance of COs by any Bank or Banks to enforce OF policies. While the OF board has delegated to OF's management the authority to prohibit or redirect issuance of COs because of market reasons, the OF does not currently enjoy the power to prohibit the issuance of debt to enforce specific policies. FHFA, therefore, has carefully considered making these changes but has decided not to do so at this time because it does not believe such changes are necessary to achieve the goals of this final rule. Under rules adopted herein (and carried over from the Finance Board regulations), the Banks are

required to provide the OF with information in form and timeframes set forth by the OF to facilitate the preparation of the combined financial reports. *See* 12 CFR 1274.3 (as adopted herein). Under the assessment formula approved by FHFA in February 2009, a Bank that fails to meet a deadline for the submission of information to OF can be subject to a special assessment. Thus, the Banks could be subject to enforcement and other actions if they fail to comply with OF policies with regard to submission of information.

Commenters also suggested that § 1273.6 be modified to give the OF authority to impose appropriate limits on any Bank's or the Bank System's exposure to risk as necessary to facilitate the issuance of COs. Assigning the OF risk management duties of the type suggested would go beyond the current scope of the OF's duties, and FHFA does not wish to take such a step at this time.

FHFA, however, intends to monitor how the OF board, and its Audit Committee, implement the changes being adopted at this time, and may consider proposing changes along the lines suggested in these comments if it believes this type of authority needs to be granted to the OF board to achieve the goals of this final rule.

#### Section 1273.7—Structure of the OF Board of Directors

Commenters generally supported the basic structure of having an OF board of directors made up of the twelve Bank presidents and some Independent Directors, but provided a number of comments about specific aspects of this section. As discussed below, FHFA made a number of changes to the provisions as a result of these comments and made some other changes to clarify the meaning of some provisions in this section.

In response to comments, FHFA clarified language in § 1273.7(a)(1) to state that if a Bank presidency becomes vacant, the person designated by the Bank's board of directors to fill temporarily the duties of president shall serve on the OF board of directors until the presidency is filled permanently. The language in the proposed rule created some unintended ambiguity on this point, by stating that a person appointed to temporarily fill the duties of president may serve on the OF board of directors. The change will assure that a Bank has representation on the board as soon as the Bank's board designates a temporary or interim president.

Given that the proposed rule provided that from three to five Independent Directors would serve on the OF board

of directors, commenters also requested that the final rule clarify how the final number of Independent Directors should be determined within the authorized range. They suggested that the OF board of directors be given authority to make this determination. FHFA agrees that some certainty on this point is needed, and has decided to change § 1273.7(a)(2) to specify that five Independent Directors shall serve on the OF board of directors. FHFA believes that five Independent Directors will better help assure a diversity of perspective and experience on the board and the Audit Committee and provide better representation with regard to the public interest than would having as few as three Independent Directors.

FHFA also received a number of comments concerning the qualifications proposed in § 1273.7(a)(2) for Independent Directors. First, commenters felt that the criteria limiting an Independent Director's financial interest in a Bank member or a consolidated obligation dealer or seller group should be eliminated because the requirement could prevent many qualified individuals serving as Independent Directors, especially given the large number of Bank members. Commenters also urged FHFA to adopt criteria closer to those used by the New York Stock Exchange to determine independence of board members, which would include a requirement that the board of directors affirmatively determine that the Independent Director had no material relationship with the Bank System. Commenters also indicated that the rule should make clear that only current officers, directors, or employees of a Bank or a Bank System member were prohibited from serving as Independent Directors and that this prohibition did not apply to former officers, directors, or employees.

FHFA has considered these comments and has modified the qualifications for Independent Directors. Under the final rule, a director, to be considered independent, must not have any material relationship with a Bank or the OF (either directly or as the partner, shareholder, or officer of an organization with a material relationship) as determined under criteria set forth in a policy adopted by the OF board of directors. This policy should address when a financial interest in, or other relationship with, a Bank System member would constitute a material relationship with a Bank or the OF. This approach would give the board more flexibility to look at the nature of an individual's financial interests in a member and determine whether the

interest would constitute a material relationship with a particular Bank that gives rise to a disqualifying conflict (or the appearance of such a conflict). The policy should also consider and address issues such as when a family member's professional or financial interest may create a conflict that should disqualify an individual from serving as an Independent Director, or whether other direct or indirect relationships of an individual with the Bank System (which can include business or advisory relationships) should disqualify such individual from serving. FHFA expects that the OF board of directors will refer to rules of the New York Stock Exchange and similar organizations in developing the policy, but recognizes that the cooperative nature and other unique aspects of the Bank System may not allow such criteria to be adopted without appropriate modification.

The final rule also sets forth minimum criteria that the "independence" policy must meet. First, such policy must provide that an Independent Director may not be an officer, director or employee of any Bank, or member of a Bank. This requirement basically carries over previously proposed criteria. After considering the comments, FHFA also believes that recent employment or service as a director at a Bank or Bank member may also create at least an appearance that a director is not independent. Therefore, the OF board of directors' policy must disqualify an individual who was an officer, director or employee of any Bank, or member of a Bank at any time in the past three years from serving as an Independent Director. The final rule also states that the policy must provide that a current officer or employee of the OF, or a person who was an officer or employee of the OF at any time during the past three years, cannot serve as an Independent Director.

Second, the OF board policy must prohibit from serving as an Independent Director, a person who is affiliated with any consolidated obligations selling or dealer group under contract with the OF, or who has a financial interest in such group that exceeds the lesser of \$250,000 or 0.01% of the group's market capitalization. This final provision basically carries over the proposed financial interest limits for consolidated obligation seller or dealer groups. The final rule also adopts the proposed criteria as to when a financial interest in a holding company of a consolidated obligations seller or dealer group would disqualify a person from serving as an Independent Director. FHFA has further altered the final rule so that a person

who has combined financial interests of more than \$1,000,000 in more than one consolidated obligation seller or dealer groups under contract with the OF must also be disqualified by the OF board policy from serving as an Independent Director. FHFA continues to believe that, given the OF role in issuing COs, an Independent Director's possessing such a financial interest in a consolidated obligation seller or dealer group or groups would create a conflict, or an appearance of conflict, that would prevent such a director from being considered independent, and is therefore adopting this provision as part of the final rule.

As in the proposed rule, the final rule requires that Independent Directors be United States citizens and, as a group, have substantial experience in financial and accounting matters. With regard to this latter requirement, some commenters asked that FHFA verify that the reference to "as a group" meant that the requirement could be met when considering the collective expertise of the Independent Directors and did not have to be met by each Director. FHFA confirms that this was its intent. Commenters also requested confirmation that the experience can be derived from a variety of sources including past experience as an attorney, government official, or business executive that was involved in financial and accounting matters. Again, FHFA confirms that this was its intent as long as such involvement qualified as substantive experience and not merely tangential involvement in these areas.

As proposed, § 1273.7(b) of the final rule provides that Independent Directors will serve for five-year terms which will be staggered so that no more than one Independent Director seat is scheduled for election in any one year. The final provision also provides, as in the proposed rule, that when an Independent Director seat becomes vacant prior to the end of a scheduled term, any individual will be elected (or appointed by FHFA) only for the remainder of the term associated with that seat. In response to comments, FHFA has clarified in the final rule that where a director is elected or appointed to fill an Independent Director seat that has become vacant before the end of the term, the partial term does not count for purposes of the prohibition on an Independent Director's serving for more than two full terms.

The final rule also continues to provide for FHFA to appoint the initial Independent Directors, the initial chairman of the reconstituted board from among the Independent Directors, and the initial vice chairman from

among all directors, even though some commenters urged that these positions initially be filled through election by the board as a whole. FHFA believes that it has an important role to play in the initial selection of the board members to ensure that the overall goals of the rule are met, and thus has not altered the proposal on this point.

To enable the current OF board of directors and the Banks to play an important role in nominating candidates for initial selection, however, FHFA has changed the process for nominating the initial slate of Independent Directors. Under § 1273.7(c)(2) of the final rule, the current OF board of directors, in consultation with the Banks, should nominate within 45 days of publication date of this final rule in the **Federal Register** a slate of at least five candidates for the Independent Directorships that FHFA can consider for appointment. This slate of candidates can include the private citizen member of the current OF board. This is a change from the proposed rule which provided that each Bank individually nominate one person and which did not give the current OF board a role in the nominating process. FHFA believes that the change will allow the current OF board and the Banks to propose a slate of candidates whose collective experience will be more appropriate and better suited to the duties of the board than if each Bank nominated a candidate individually. Overall, this should improve the chances that FHFA will find suitable candidates among the nominees. Under the final rule, FHFA will be able to appoint the Independent Directors from among the candidates nominated by the OF board, from among other persons identified by FHFA itself, or from some combination of these two groups.

FHFA recognizes that at the time the current OF board will need to nominate a slate of candidates for consideration by FHFA as Independent Directors, the new board will not have had an opportunity to develop and approve the policy identifying additional criteria for "independence" required by § 1273.7(a)(2)(iii). Therefore, FHFA expects that the current board in choosing its slate of nominees for appointment as Independent Directors will assure that the candidates meet at least the minimum criteria for independence set forth in the final rule. In making its appointments, FHFA also will consider whether any relationships that a candidate may have with a Bank or the Bank System could, in its view, compromise the candidate's ability to act independently and will make its decisions accordingly.

The final rule generally adopts the provisions dealing with election of independent directors as proposed. In this respect, the final rule requires the OF board to provide FHFA with relevant biographic and background information about an elected Independent Director at least 20 business days before that Director assumes any duties. This requirement applies whether the person is newly elected or is being re-elected; for directors that are re-elected, FHFA would expect to receive relevant biographic and background information at least 20 business days before the new term begins. The final rule also retains FHFA's right to object to a particular Independent Director and to appoint an Independent Director if FHFA believes in its judgment that the OF board failed to elect a qualified person. Some commenters objected to FHFA retaining the right of objection to, and appointment of, Independent Directors, but FHFA believes that this right of review is legitimate for the regulator and will help assure that the requirements and goals of this rule are met. In response to comments, the final rule does clarify, however, that FHFA will exercise its right to object to a particular Director prior to the time that the Independent Director is to assume his or her duties (or for a Director that has been re-elected, prior to when the new term is to begin). The rule also provides that in any notice of objection, FHFA will inform the OF board if FHFA will appoint someone to fill the seat in question or if the OF board should hold a new election to do so.

In response to comments, the final rule modifies the proposed provisions subjecting the charters of any committees established by the board to FHFA's review and approval, although the final rule continues to provide that the by-laws of the board of directors and the charter of the Audit Committee shall be subject to review and approval by FHFA. The final rule also no longer specifically reserves to FHFA the right to require the OF board of directors to withdraw or change the scope of any delegation made by it. These changes, however, do not alter or diminish FHFA's general oversight, examination, or enforcement authority with regard to such actions by the OF board of directors.

With regard to these proposed provisions, some commenters felt that it was inappropriate for FHFA to reserve to itself such direct involvement in the internal affairs of the OF board and that the provisions were contrary to the devolution of authority from the regulator to the Banks that began with

the passage of the Gramm-Leach-Bliley Act of 1999. Commenters pointed out that this was especially true because, even without these provisions, all aspects of the OF's activities would remain subject to FHFA's general oversight and examination authority. Similar comments were made with regard to the proposed provision reserving to FHFA the right to require the OF board to withdraw or change the scope of any delegation made by it.

FHFA believes that, in light of the changes to duties and responsibilities of the board of directors and the Audit Committee made by this regulation, FHFA has a legitimate need to review and approve the by-laws of the board of directors and the charter of the Audit Committee to assure that these documents are consistent with, and meet, the goals and requirements of this rulemaking. FHFA also believes that such review and approval is a proper exercise of its supervisory authority. Thus, the final rule continues to provide that the by-laws of the board of directors and the charter of the Audit Committee shall be subject to review and approval by FHFA. FHFA believes that that supervisory need is less prominent with respect to the charters of other committees and delegations made by the board, and therefore has deleted the requirement that those charters and delegations also be subject to FHFA review and approval.

FHFA also adopted as final the proposed provision that provided that the OF shall pay reasonable compensation and expenses to the Independent Directors in accordance with the payment of compensation and expenses to Bank directors. Commenters urged FHFA to change this provision so that the OF board could compensate and pay expenses of Independent Directors as would be reasonable under the circumstances rather than limiting compensation and reimbursement by reference to provision applicable to Bank directors. In fact, the rule provides that OF director compensation must comply with the same standard as that of Bank directors—a standard of reasonableness—and not that OF director compensation be the same as that of Bank directors.

In response to urging by commenters, FHFA changed in the final rule the provision dealing with indemnification so that the OF board can choose the body of law that would govern corporate governance practice and procedure, including indemnification, from among the law of the jurisdiction in which the OF is located, Delaware Corporation law, or the Revised Model Business Corporation Act. As commenters

pointed out, this approach would be similar to rules previously adopted by OFHEO with regard to the Enterprises.<sup>10</sup> The change will allow the OF board to have more specific guidance as to what legal standards should apply to their corporate governance and indemnification practices than did the proposed provision, which was silent on this point. The final rule requires the OF board to make this choice of law decision within 90 calendar days from the date of its initial organizational meeting required under § 1273.10. The final rule also makes clear that the OF shall indemnify its directors, officers (including the Chief Executive Officer), and employees under such terms and conditions as are determined by the board, and that the board may maintain insurance with respect to such persons.

#### Section 1273.8—General Duties of the OF Board of Directors

Proposed § 1273.8 sets out the general duties of the OF board of directors. Most of the specific provisions in this section as proposed were carried over from existing Finance Board regulation § 985.8. Nevertheless, FHFA received a number of comments on this section.

First, commenters urged FHFA not to describe the OF board's general duties by reference to the regulations in 12 CFR part 917, as such references could create confusion. Commenters noted that the part 917 regulations address the duty of a Bank's board of directors to a Bank's members, and that the duties owed by the OF board of directors to the Banks and the Bank System may differ fundamentally from those owed by a Bank's board to its member institutions. FHFA agrees, and has changed proposed § 1273.8(a) accordingly. As adopted, § 1273.8(a) now provides that an OF director should carry out his or her duties in good faith in a manner that the director believes to be in the best interests of the OF and the Bank System, with such care, including a duty of reasonable inquiry, as an ordinary prudent person in a like position would use under similar circumstances. It also provides that the OF directors should administer the affairs of the OF fairly and impartially without discrimination in favor of or against any Bank. It also requires directors to develop a familiarity with the basic business, finance, and accounting practices of the Banks, to be able to understand the Banks' combined financial statements, and to make substantive inquiries of management and of the internal and external auditors with regard to the combined financial statements and the

<sup>10</sup> See 12 CFR 1710.10.

OF's individual financial statement. FHFA also removed other references to the part 917 regulations where it felt the reference could be confusing or inappropriate.

Commenters also suggested that FHFA alter the proposed quorum requirements so that the requirement for a quorum could be set in the OF by-laws rather than in the rule, or that the quorum be set at a majority of sitting directors rather than ten directors as proposed. FHFA has considered these comments but believes that the quorum requirements should be set in the rule to assure that there is adequate representation of all parties, including Independent Directors, at each meeting. Thus, FHFA has adopted a final provision that states that a quorum requires at least a majority of sitting directors, which must include a majority of Independent Directors.<sup>11</sup> The OF board may adopt in its by-laws more stringent quorum requirements than those adopted in the rule.

Commenters argued that the requirement for at least six in-person board meetings per year should be dropped, and that the number of required meetings should instead be established in the by-laws. FHFA believes that, given the duties assigned to the OF board, a requirement of six in-person board meetings is reasonable and necessary to assure that those duties are carried out. Thus, it has not changed this requirement.

FHFA also received comments asking that the proposal be changed to allow the OF board, rather than FHFA, to assign additional duties to the Chief Executive Officer of the OF. Proposed § 1273.8(d)(4), however, already clearly provided that the OF board (and not FHFA) select, employ, determine the compensation for, and assign the duties and functions of the Chief Executive Officer, subject to certain minimum responsibilities.<sup>12</sup> Thus, no change was made in the final rule in response to this comment.

#### Section 1273.9—Audit Committee

Proposed § 1273.9 set out the duties and function of the OF Audit Committee. Under the proposed rule, the Audit Committee would assume the OF board's previous responsibility for overseeing the OF's preparation of the

combined financial reports, and duties related to overseeing the audit of these reports and of the OF itself. As part of these responsibilities, the proposed rule would have required the Audit Committee to ensure that the Banks adopt consistent accounting policies and procedures so that the combined financial reports continue to be accurate and meaningful. Where the Banks were unable to agree to such policies, the proposed rule would have authorized the Audit Committee, in consultation with FHFA, to prescribe them.

A large number of the comments made on the proposed rule addressed § 1273.9. In particular, commenters addressed the proposed provisions assigning to the Audit Committee the duty and authority to require the Banks to adopt consistent accounting policies and procedures so that information submitted by them may be combined to create accurate and meaningful combined financial reports. In general, commenters felt these provisions were inappropriate in that the power to adopt accounting policies and procedures should be vested in the board of directors or audit committees of the individual Banks. They also felt that the rule failed to recognize the role of the individual Banks in establishing their own accounting policies, and felt that consistency can only be achieved through cooperation, not by mandate of the OF's Audit Committee.

Alternatively, commenters suggested that the Audit Committee's role be that of making recommendations to the full OF board of directors. One commenter suggested that the Audit Committee be required only to assure that Banks' accounting policies and procedures be only "sufficiently" consistent to assure that information can be combined in an accurate and meaningful way. Some commenters also questioned whether the regulator-imposed limitation under the rule on a Bank's right to make accounting policy choices otherwise acceptable under generally accepted accounting principles (GAAP) would itself be a violation of GAAP. Other commenters urged that the proposed rule be refined to reflect the appropriate discretion that is accorded to the Banks as independent entities to apply GAAP.

Commenters also questioned the use of the phrase "accurate and meaningful" stating that it had no well-understood meaning in law. Commenters said the proposed provision also appeared to impose on the OF Audit Committee the duty to ensure accuracy of the underlying financial information submitted by the Banks, a task that they did not believe could be accomplished by the Audit Committee. They urged

that the rule be recast to make clear that the OF Audit Committee was only responsible for the acts related to the combining of information and not for the accuracy of the information reported by the Banks.

FHFA has carefully considered these comments. It continues to believe that the OF Audit Committee, made up of the Independent Directors, remains the appropriate body for overseeing the preparation of the combined financial reports, and it must have all appropriate authority needed to be successful in this task. As Independent Directors, members of the Audit Committee will have a lesser incentive and less of a vested interest than any Bank president to represent the view of any particular Bank or Banks, and will be in the best position to ensure that, given the information presented by the Banks, the combined financial reports presents an accurate and meaningful picture of the Bank System's financial condition. FHFA agrees that as an initial matter, it is the duty of the Banks themselves to coordinate accounting policies and procedures to assure that information is presented in a uniform manner so that it can be combined in an accurate and meaningful fashion. FHFA also recognizes, however, that the Banks have not always been able to agree on such presentation and that it is appropriate to give the Audit Committee authority, in consultation with FHFA, to require consistent accounting policies and procedures where needed so that it can carry out its duties with regard to the preparation of the combined financial reports. FHFA does not believe that it is inconsistent with GAAP for the Audit Committee to require particular accounting principles to be used in submitting information for the combined reports from among the range of principles that may be available under GAAP; nor does FHFA believe that this is inconsistent with the independent identities and reporting responsibilities of the twelve Banks, given that they retain their authority to issue their own separate financial statements, which are not required to be consistent across all twelve Banks, in their SEC filings.

FHFA also believes that its overall approach is consistent with its authority to supervise the safety and soundness of the Bank System. The goal of the rule is to improve the disclosure now provided by the combined financial reports. Combined financial reports are necessary and useful to the market because a Bank does not issue debt in its own name but as a Bank System. Thus, the need for the rule is driven by the unique funding mechanism of the

<sup>11</sup> Thus, if all board seats were filled, a quorum would require the presence of at least nine board members, of whom at least three would have to be Independent Directors.

<sup>12</sup> By contrast, the proposed rule also provided that the OF board of directors should assume such additional duties as might be assigned to it by FHFA. This provision was proposed and adopted as § 1273.8(d)(6).

Bank System, including the joint and several nature of Bank COs.

Given the comments just discussed, FHFA also realizes that the wording of the proposed provisions may not have fully reflected its intent and thus has made some changes to the language of the final rule. First, it has changed the language in § 1273.9(b)(1) to state that the Audit Committee will be responsible for “overseeing the audit function of the OF and the preparation and the accurate and meaningful combination of the information submitted by the Banks in the Bank System’s combined financial reports.” FHFA believes that this wording more accurately reflects the Audit Committee’s oversight of the preparation of the combined financial reports especially, with regard to the basis and approach to combining information received from the Banks, but that the OF Audit Committee is not responsible for overseeing the reliability and integrity of the accounting policies and financial reporting and disclosure policies of the individual Banks, or the accuracy of the information that they submit. FHFA has also adopted new language in § 1273.9(b)(2) which now states that the “Audit Committee shall ensure that the Banks adopt consistent accounting policies and procedures to the extent necessary for information submitted by the Banks to the OF to be combined to create accurate and meaningful combined financial reports.” This change makes it clear that the Audit Committee’s authority to require consistent accounting policies and procedures is not meant to be unlimited in nature, but to assure it can fulfill its duties with regard to the combined financial reports.

While FHFA has made some changes, it has kept the phrase “accurate and meaningful” even though some commenters felt it lacked precision and had no clear meaning under law. FHFA believes the words themselves have a well understood plain meaning and can be applied accordingly. In using the term “accurate”, FHFA contemplates that the combination of the several Banks’ financial statements and quantitative disclosures is correctly presented, that the overall presentation complies with GAAP, relevant interpretative materials put forth by accounting and audit standard setters, and with this and other applicable regulations and guidance issued by FHFA. In using the term “meaningful”, FHFA contemplates that the combined statements will present, in an understandable and transparent manner, robust disclosures and discussion that will enhance the readers’ understanding of the Banks’ combined financial

conditions, changes in this financial condition, and the combined results of their operations.

FHFA also notes that under this rule both as proposed and adopted, the Audit Committee is responsible for selecting the external auditor for the combined financial statements. Historically, the Banks have selected a common auditor for the individual Bank and combined financial statements audits. Engaging a common external auditor may promote more consistent accounting practices, would avoid subjecting the Banks and the OF to inter-firm disagreements on accounting matters, and has been found by the Banks to be more cost-effective than using multiple auditors. FHFA recognizes that as a practical matter the auditor for the combined financial reports is likely to be the same firm that audits the individual Banks.

Based on comments, the final rule does not define the Audit Committee duties in § 1273.9(c) by reference to § 917.7 of this title, which addresses the duties of a Bank’s audit committee. FHFA agrees that this reference is confusing given the differences between the Banks and the OF. Instead, FHFA added descriptions of relevant duties that should be carried out by the Audit Committee in the final rule as paragraphs (c)(7) through (c)(15) of § 1273.9. This list of duties is based on those in § 917.7, although they have been modified to reflect differences between the Banks and the OF. The duties assigned to the Audit Committee under these provisions include overseeing the preparation and audit of the OF’s own financial statements and the OF’s internal controls. The Audit Committee is also responsible for providing an independent direct channel of communication between the OF board of directors and OF’s internal and external auditors. The Audit Committee also must periodically report findings to the full board and must keep written minutes of its meetings. The final rule also requires that the Audit Committee adopt and the full board approve, a written charter that specifies the scope of the Audit Committee’s powers and responsibilities, consistent with the duties and authority set forth in § 1273.9. The Audit Committee and the board also must review and assess the adequacy of the charter on an annual basis, and where appropriate make changes, and re-adopt and re-approve the charter not less often than every three years. The final rule makes clear that the charter of the Audit Committee is subject to review and approval by FHFA.

Some commenters also requested that FHFA recast the duties of the Audit Committee based on language contained in the Securities Exchange Act of 1934 (1934 Act).<sup>13</sup> Along these lines commenters also asked that the rule should make clear that the Audit Committee is part of the board of directors as a whole and is not acting separate or apart from the board’s general oversight responsibility for the OF. FHFA has not made specific changes in response to these comments. FHFA believes that § 1273.9 as adopted is consistent with the audit committee provisions of the 1934 Act, although FHFA notes that, because the OF is not a reporting company or a company at all, those provisions do not apply to it.

FHFA also received comments that the OF board of directors should be able to establish an Audit Committee made up of less than all of the Independent Directors. Commenters felt this would allow the board to find Independent Directors whose skills may not fit with those required for the Audit Committee but could provide important insights on other areas of interest. As already noted, FHFA believes that having five Independent Directors sit on the Audit Committee will better assure a diversity of perspective and experience than would a smaller number, and will thereby help the Committee better carry out its duties under this rule. FHFA also believes that the skill sets required of the Independent Directors under the rule are not narrowly tailored and that the board will be able to find Independent Directors with a wide range of knowledge and experience that will prove valuable to the board in carrying out its duties. FHFA therefore is not adopting this suggestion.

Section 1273.9(a) of the final rule also now clarifies that the Audit Committee shall elect its chairperson from among its members. The provision makes clear that nothing prevents the Audit Committee from choosing the OF Chairperson also to serve as chair of the Audit Committee if the Committee so decides. This is not a requirement, however, and any Independent Director

<sup>13</sup> Section 10A(m)(2) of the 1934 Act states in relevant part that:

The audit committee \* \* \*, in its capacity as a committee of the board of directors, shall be directly responsible for the appointment, compensation and oversight of the work of any registered public accounting firm employed \* \* \* (including resolution of disagreements between management and the auditor regarding financial reporting) for purposes of preparing or issuing an audit report or related work, and each registered public accounting firm shall report directly to the audit committee.

15 U.S.C. 78j-1(m).

may be elected chair of the Audit Committee.

#### Section 1273.10—Transition

Commenters suggested that the final rule should require that an organizational meeting of the new OF board of directors be held within a set time of the effective date of the rule and that the new OF board of directors be deemed to be reconstituted as of that date. FHFA agrees that it is important to set out in the rule more specific details of how the transition should occur between the current OF board of directors and the new board of directors required under this part 1273. As such, FHFA is adopting, as part of the final rule, § 1273.10, which lays out a transition provision.

Under this section, the new OF board of directors will be required to hold an organizational meeting within 45 calendar days of the date that FHFA first appoints an Independent Director under § 1273.7(c). The board shall be deemed to be reconstituted as of the date of the organizational meeting. The rule provides that the person appointed chairman of the new board shall have authority to set the date of the organizational meeting. The transition provision also makes clear that until the date of the organizational meeting, the current OF board of directors and its audit committee shall continue to have power and authority to act in these capacities.

The transition provision also provides that the audit committee as in existence immediately prior to the effective date of the rule may continue to have responsibility and oversight authority with regard to the preparation and publication of any combined financial report that covers a reporting period that ends prior to July 1, 2010. This provision will avoid requiring the members of the reconstituted Audit Committee to review and approve any combined financial statements for a period during which the new Committee was not in existence. The rule, however, would allow the new board of directors to determine that the new Audit Committee of Independent Directors may take over the responsibility for a combined financial report that covers a period prior to July 1, 2010. This provision is meant to provide flexibility in when responsibility for the combined financial reports is handed over, given that it is difficult to predict the exact date of the organizational meeting and therefore hard to predict how much time a new Audit Committee would have before it had to take its first actions with respect to a combined financial

report. Thus, if the board believes the Independent Directors have sufficient time to familiarize themselves with relevant issues prior to the completion of the preparation and publication of a combined financial report, it can allow the new Audit Committee to take over this duty with respect to a report that covers a period prior to the third quarter of 2010.

#### Appendix A to Part 1273 and Part 1274

FHFA did not receive any specific comments on the proposed Appendix A to Part 1273 or to the proposed Part 1274 rules. FHFA is adopting these provisions substantively as proposed. FHFA notes that as adopted, Appendix A to Part 1273 would require biographical information about the Bank presidents to appear only once in the combined financial report and not twice, even though the Bank presidents also serve as OF board members. The combined report should make clear that the Bank presidents serve as OF board members and provide an appropriate cross reference to where the biographical information appears.

#### III. Paperwork Reduction Act

The final rule does not contain any collections of information pursuant to the Paperwork Reduction Act of 1995 (44 U.S.C. 3501 *et seq.*). Therefore, FHFA has not submitted any information to the Office of Management and Budget for review.

#### IV. Regulatory Flexibility Act

The final rule applies only to the Banks and the OF (which is a joint office of 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), FHFA certifies that this final rule will not have significant economic impact on a substantial number of small entities.

#### List of Subjects

##### 12 CFR Part 985

Federal home loan bank, Securities.

##### 12 CFR Part 989

Accounting, Federal home loan banks, Financial disclosure.

##### 12 CFR Part 1273

Federal home loan banks, Securities.

##### 12 CFR Part 1274

Accounting, Federal home loan banks, Financial disclosure.

■ Accordingly, for reasons stated in the preamble, under the authority of 12 U.S.C. 4526(a), FHFA amends chapters

IX and XII of title 12 of the Code of Federal Regulations as follows:

#### CHAPTER IX—FEDERAL HOUSING FINANCE BOARD

##### Subchapter K—Office of Finance

#### PART 985—[REMOVED]

■ 1. Remove 12 CFR part 985.

#### PART 989—[REMOVED]

■ 2. Remove 12 CFR part 989.

#### CHAPTER XII—FEDERAL HOUSING FINANCE AGENCY

##### Subchapter D—Federal Home Loan Banks

■ 3. Add part 1273 to subchapter D to read as follows:

#### PART 1273—OFFICE OF FINANCE

##### Sec.

- 1273.1 Definitions.
  - 1273.2 Authority of the OF.
  - 1273.3 Functions of the OF.
  - 1273.4 FHFA oversight.
  - 1273.5 Funding of the OF.
  - 1273.6 Debt management duties of the OF.
  - 1273.7 Structure of the OF board of directors.
  - 1273.8 General duties of the OF board of directors.
  - 1273.9 Audit Committee.
  - 1273.10 Transition.
- Appendix A to Part 1273—Exceptions to the General Disclosure Standards

**Authority:** 12 U.S.C. 1431, 1440, 4511(b), 4513, 4514(a), 4526(a).

##### § 1273.1 Definitions.

For purposes of this part: *Audit Committee* means the OF Independent Directors acting as the committee established in accordance with § 1273.9 of this part.

*Bank* written in title case, means a Federal Home Loan Bank established under section 12 of the Bank Act (12 U.S.C. 1432).

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

*Bank System* means the Federal Home Loan Bank System, consisting of the twelve Banks and the Office of Finance.

*Chair* means the chairperson of the board of directors of the Office of Finance.

*Chief Executive Officer* or *CEO* means the chief executive officer of the Office of Finance.

*Consolidated obligations* means any bond, debenture or note on which the Banks are jointly and severally liable and which was issued under section 11 of the Bank Act (12 U.S.C. 1431) and any implementing regulations, whether or not such instrument was originally issued jointly by the Banks or by the Federal Housing Finance Board on behalf of the Banks.

*FHFA* means the Federal Housing Finance Agency.

*Financing Corporation* or *FICO* means the Financing Corporation established and supervised by FHFA under section 21 of the Bank Act (12 U.S.C. 1441).

*Generally accepted accounting principles* or *GAAP* means accounting principles generally accepted in the United States.

*Independent Director* means a member of the OF board of directors who meets the qualifications set forth in § 1273.7(a)(2) of this part.

*NRSRO* means a credit rating organization registered as a Nationally Recognized Statistical Rating Organization with the Securities and Exchange Commission.

*Office of Finance* or *OF* means the Office of Finance, a joint office of the Banks established under this part 1273 and referenced in the Bank Act and the Safety and Soundness Act.

*Resolution Funding Corporation* or *REFCORP* means the Resolution Funding Corporation established by section 21B of the Bank Act (12 U.S.C. 1441b).

*Safety and Soundness Act* means the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (12 U.S.C. 4501 *et seq.*), as amended.

#### § 1273.2 Authority of the OF.

(a) *General.* The OF shall enjoy such incidental powers under section 12(a) of the Bank Act (12 U.S.C. 1432(a)), as are necessary, convenient and proper to accomplish the efficient execution of its duties and functions pursuant to this part, including the authority to contract with a Bank or Banks for the use of Bank facilities or personnel in order to perform its functions or duties.

(b) *Agent.* The OF, in the performance of its duties, shall have the power to act on behalf of the Banks in issuing consolidated obligations and in paying principal and interest due on the consolidated obligations, or other obligations of the Banks.

(c) *Assessments.* The OF shall have authority to assess the Banks for the funding of its operations in accordance with § 1273.5 of this part.

#### § 1273.3 Functions of the OF.

(a) *Joint debt issuance.* Subject to parts 965 and 966 of this title, and this part, the OF, as agent for the Banks, shall offer, issue, and service (including making timely payments on principal and interest due) consolidated obligations.

(b) *Preparation of combined financial reports.* The OF shall prepare and issue the combined annual and quarterly financial reports for the Bank System in

accordance with the requirements of § 1273.6(b) and Appendix A of this part, using consistent accounting policies and procedures as provided in § 1273.9(b) of this part.

(c) *Fiscal agent.* The OF shall function as the fiscal agent of the Banks.

(d) *Financing Corporation and Resolution Funding Corporation.* The OF shall perform such duties and responsibilities for FICO as may be required under part 995 of this title, or for REFCORP as may be required under part 996 of this title or authorized by FHFA pursuant to section 21B(c)(6)(B) of the Bank Act (12 U.S.C. 1441b(c)(6)(B)).

#### § 1273.4 FHFA oversight.

(a) *Oversight and enforcement actions.* FHFA shall have such oversight authority over the OF, the OF board of directors, the officers, employees, agents, attorneys, accountants, or other OF staff as set forth in the Bank Act, the Safety and Soundness Act, and FHFA regulations issued thereunder.

(b) *Examinations.* Pursuant to section 20 of the Bank Act (12 U.S.C. 1440), FHFA shall examine the OF, all funds and accounts that may be established pursuant to this part 1273, and the operations and activities of the OF, as provided for in the Bank Act, the Safety and Soundness Act, or any regulations promulgated pursuant thereto.

(c) *Combined financial reports.* FHFA shall determine whether a combined Bank System annual or quarterly financial report complies with the standards of this part.

#### § 1273.5 Funding of the OF.

(a) *Generally.* The Banks are responsible for jointly funding all the expenses of the OF, including the costs of indemnifying the members of the OF board of directors, the Chief Executive Officer, and other officers and employees of the OF, as provided for in this part.

(b) *Funding policies.*—(1) At the direction of and pursuant to policies and procedures adopted by the OF board of directors, the Banks shall periodically reimburse the OF in order to maintain sufficient operating funds under the budget approved by the OF board of directors. The OF operating funds shall be:

(i) Available for expenses of the OF and the OF board of directors, according to their approved budgets; and

(ii) Subject to withdrawal by check, wire transfer or draft signed by the Chief Executive Officer or other persons designated by the OF board of directors.

(2) Each Bank's respective *pro rata* share of the reimbursement described in

paragraph (b)(1) of this section shall be based on a reasonable formula approved by the OF board of directors. Such formula shall be subject to the review of FHFA, and the OF board of directors shall make any changes to the formula as may be ordered by FHFA from time to time.

(c) *Alternative funding method.* With the prior approval of FHFA, the OF board of directors may, by contract with a Bank or Banks, choose to be reimbursed through a fee structure, in lieu of or in addition to assessment, for services provided to the Bank or Banks.

(d) *Prompt reimbursement.* Each Bank from time to time shall promptly forward funds to the OF in an amount representing its share of the reimbursement described in paragraph (b) of this section when directed to do so by the Chief Executive Officer pursuant to the procedures of the OF board of directors.

(e) *Indemnification expenses.* All expenses incident to indemnification of the members of the OF board of directors, the Chief Executive Officer, and other officers and employees of the OF shall be treated as an expense of the OF to be reimbursed by the Banks under the provisions of this part.

(f) *Operating funds segregated.* Any funds received by the OF from the Banks pursuant to this section for OF operating expenses promptly shall be deposited into one or more accounts and shall not be commingled with any proceeds from the sale of consolidated obligations in any manner.

#### § 1273.6 Debt management duties of the OF.

(a) *Issuing and servicing of consolidated obligations.* The OF, as agent for the Banks, shall issue and service (including making timely payments on principal and interest due, subject to §§ 966.8 and 966.9 of this title) consolidated obligations pursuant to and in accordance with the policies and procedures established by the OF board of directors under this part.

(b) *Combined financial reports requirements.* The OF, under the oversight of the Audit Committee, shall prepare and distribute the combined annual and quarterly financial reports for the Bank System in accordance with the following requirements:

(1) The scope, form, and content of the disclosure generally shall be consistent with the requirements of the Securities and Exchange Commission Regulations S–K and S–X (17 CFR parts 229 and 210).

(2) Information about each Bank shall be presented as a segment of the Bank System as if generally accepted

accounting principles regarding business segment disclosure applied to the combined annual and quarterly financial reports of the Bank System, and shall be presented using consistent accounting policies and procedures as provided in § 1273.9(b) of this part.

(3) The standards set forth in paragraphs (b)(1) and (b)(2) of this section are subject to the exceptions set forth in Appendix A to this part.

(4) The combined Bank System annual financial reports shall be filed with FHFA and distributed to each Bank and Bank member within 90 days after the end of the fiscal year. The combined Bank System quarterly financial reports shall be filed with FHFA and distributed to each Bank and Bank member within 45 days after the end of the of the first three fiscal quarters of each year.

(5) The Audit Committee shall ensure that the combined Bank System annual or quarterly financial reports comply with the standards of this part.

(6) The OF and the OF board of directors, including the Audit Committee, shall comply promptly with any directive of FHFA regarding the preparation, filing, amendment, or distribution of the combined Bank System annual or quarterly financial reports.

(7) Nothing in this section shall create or be deemed to create any rights in any third party.

(c) *Capital markets data.* The OF shall provide capital markets information concerning debt to the Banks.

(d) *NRSROs.* The OF shall manage the relationships with NRSROs in connection with their rating of consolidated obligations.

(e) *Research.* The OF shall conduct research reasonably related to the issuance or servicing of consolidated obligations.

(f) *Monitor Banks' credit exposure.* The OF shall timely monitor, and compile relevant data on, each Bank's and the Bank System's unsecured credit exposure to individual counterparties.

#### § 1273.7 Structure of the OF board of directors.

(a) *Membership.* The OF board of directors shall consist of seventeen part-time members as follows:

(1) The twelve Bank presidents, *ex officio*, provided that if the presidency of any Bank becomes vacant, the person designated by the Bank's board of directors to temporarily fulfill the duties of president of that Bank shall serve on the OF board of directors until the presidency is filled permanently; and

(2) Five Independent Directors who—

(i) Each shall be a citizen of the United States;

(ii) As a group, shall have substantial experience in financial and accounting matters; and

(iii) Shall not have any material relationship with a Bank, or the OF (directly or as a partner, shareholder or officer of an organization), as determined under criteria set forth in a policy adopted by the OF board of directors. At a minimum, such policy shall provide that an Independent Director may not:

(A) Be an officer, director, or employee of any Bank or member of a Bank, or have been an officer director or employee of a Bank or member of a Bank during the previous three years;

(B) Be an officer or employee of the OF, or have been an officer or employee of the OF during the previous three years; or

(C) Be affiliated with any consolidated obligations selling or dealer group under contract with OF, or hold shares or any other financial interest in any entity that is part of a consolidated obligations seller or dealer group in an amount greater than the lesser of \$250,000 or 0.01% of the market capitalization of the seller or dealer group; or in an amount that exceeds \$1,000,000 for all entities that are part of any consolidated obligations seller dealer group, combined. For purposes of this paragraph (a)(2)(iii)(C), a holding company of an entity that is part of a consolidated obligations seller or dealer group shall be deemed to be part of the consolidated obligations selling or dealer group if the assets of the holding company's subsidiaries that are part of a consolidated obligation seller or dealer group constitute 35% or more of the consolidated assets of the holding company.

(b) *Terms.*—(1) Except as provided in paragraphs (b)(2) and (c)(1) of this section, each Independent Director shall serve for five-year terms (which shall be staggered so that no more than one Independent Director seat would be scheduled to become vacant in any one year), and shall be subject to removal or suspension in accordance with § 1273.4(a) of this part. An Independent Director may not serve more than two full, consecutive terms, provided that any partial term served by an Independent Director pursuant to paragraph (b)(2) of this section, or time served by a private citizen member of the OF Board pursuant to an appointment made prior to the effective date of this part, shall not count as a term for purposes of this restriction.

(2) The OF board of directors shall fill any vacancy among the Independent Directors occurring prior to the scheduled end of a term by majority

vote, subject to FHFA's review of, and non-objection to, the new Independent Director. The OF board of directors shall provide FHFA with the same biographic and background information about the new Independent Director required under paragraph (d) of this section, and FHFA shall have the same rights of non-objection to the Independent Director (and to appoint a different Independent Director) as set forth in paragraph (d) of this section. A person shall be elected (or otherwise appointed by FHFA) under this paragraph to serve only for the remainder of the term associated with the vacant directorship.

(c) *Initial selection of Independent Directors.*—(1) As soon as practicable after the effective date of this regulation, FHFA shall fill the initial Independent Director positions by appointment. The Independent Directors shall be appointed for such periods of time, not to exceed five years, to assure the terms are staggered in accordance with paragraph (b)(1) of this section.

(2) The two Bank presidents and the private citizen member who constituted the OF board of directors immediately prior to the effective date of this rule shall, in consultation with the Banks, agree on a slate of at least five persons and nominate such persons for consideration for appointment as Independent Directors by FHFA under this paragraph (c). The nominations shall be submitted to FHFA on or before June 17, 2010. FHFA may appoint persons nominated under this paragraph or other persons identified by it and meeting the requirements of paragraph (a)(2) of this section, or some combination.

(d) *Election of Independent Directors after the initial terms.* Once the terms of the Independent Directors initially appointed by FHFA expire or the positions otherwise become vacant, the Independent Directors subsequently shall be elected by majority vote of the OF board of directors, subject to FHFA's review of, and non-objection to, each Independent Director. The OF board of directors shall provide FHFA with relevant biographic and background information, including information demonstrating that the new Independent Director meets the requirements of paragraph (a)(2) of this section, at least 20 business days before the person assumes any duties as a member of the OF board of directors. If the OF board of directors, in FHFA's judgment, fails to elect a suitably qualified person, FHFA may appoint some other person who meets the requirements of paragraph (a)(2) of this section. FHFA will provide notice of its objection to a particular Independent

Director prior to the date that such Director is to assume duties as a member of the OF board of directors. Such notice shall indicate whether, given FHFA's objection, FHFA intends to fill the seat through appointment or a new election should be held by the OF board of directors.

(e) *Initial Selection of Chair and Vice-Chair.* The first Chair and Vice-Chair of the OF board of directors after the effective date of this regulation shall be appointed by FHFA. The Chair shall be selected from among the Independent Directors appointed under paragraph (c)(1) of this section. The Vice-Chair shall be selected from among all OF board directors.

(f) *Subsequent Election of Chair and Vice-Chair.* After the terms of the persons selected under paragraph (e) of this section expire or the positions otherwise become vacant:

(1) Subsequent Chairs shall be elected by majority vote of the OF board of directors from among the Independent Directors then serving on the OF board of directors; and

(2) Subsequent Vice-Chairs shall be elected by majority vote of the OF board of directors from among all directors.

(3) The OF board of directors shall promptly inform FHFA of the election of a Chair or Vice-Chair. If FHFA objects to any Chair or Vice-Chair elected by the OF board of directors, FHFA shall provide written notice of its objection within 20 business days of the date that FHFA first receives the notice of the election of the Chair and or Vice-Chair, and the OF board of directors must then promptly elect a new Chair or Vice-Chair, as appropriate.

(g) *By-laws and Committees.*—(1) The OF board of directors shall adopt by-laws governing the manner in which the board conducts its affairs, which shall be consistent with the requirements of this part and other applicable laws and regulations as administered by FHFA. The by-laws of the board of directors shall be subject to review and approval by FHFA.

(2) In addition to the Audit Committee required under § 1273.9 of this part, the OF board of directors may establish other committees, including an Executive Committee. The duties and powers of such committee, including any powers delegated by the OF board of directors, shall be specified in the by-laws of the board of directors or the charter of the committee.

(h) *Compensation.*—(1) The Bank presidents shall not receive any additional compensation or reimbursement as a result of their service as a director of the OF board.

(2) The OF shall pay reasonable compensation and expenses to the Independent Directors in accordance with the requirements for payment of compensation and expenses to Bank directors as set forth in part 1261 of this title.

(i) *Corporate Governance and Indemnification.*—(1) *General.* The corporate governance practices and procedures of the OF, and practices and procedures related to indemnification (including advancement of expenses) shall comply with applicable Federal law rules and regulations.

(2) *Election and designation of body of law.* To the extent not inconsistent with paragraph (i)(1) of this section, the OF shall elect to follow the corporate governance and indemnification practices and procedures set forth in one of the following: (i) The law of the jurisdiction in which the principal office of the OF is located, as amended; (ii) the Delaware General Corporation Law (Del. Code Ann. Title 8, as amended); or (iii) the Revised Model Business Corporation Act, as amended. The OF board of directors, as constituted under this part, shall designate in its by-laws the body of law elected pursuant to this paragraph (i)(2) within 90 calendar days from the date that it holds the organizational meeting required under § 1273.10(a) of this part.

(3) *Indemnification.* Subject to paragraphs (i)(1) and (i)(2) of this section, to the extent applicable, the OF shall indemnify (and advance the expenses of) its directors, officers and employees under such terms and conditions as are determined by the OF board of directors. The OF shall be authorized to maintain insurance for its directors, the CEO, and any other officer or employee of the OF. Nothing in this paragraph shall affect any rights to indemnification (including the advancement of expenses) that a director, the CEO, or any other officer or employee of the OF had with respect to any actions, omissions, transactions, or facts occurring prior to the effective date of this paragraph (i).

(j) *Delegation.* In addition to any delegation to a committee allowed under paragraph (g) of this section, the OF board of directors may delegate any of its authority or duties to any employee of the OF in order to enable OF to carry out its functions.

(k) *Outside staff and consultants.* In carrying out its duties and responsibilities, the OF board of directors, or any committee thereof, shall have authority to retain staff and outside counsel, independent accountants, or other outside consultants at the expense of the OF.

### § 1273.8 General duties of the OF board of directors.

(a) *General.* Each director shall have the duty to:

(1) Carry out his or her duties as director in good faith, in a manner such director believes to be in the best interests of the OF and the Bank System, and with such care, including reasonable inquiry, as an ordinarily prudent person in a like position would use under similar circumstances;

(2) Administer the affairs of the OF fairly and impartially and without discrimination in favor of or against any Bank;

(3) At the time of appointment or election, or within a reasonable time thereafter, have a working familiarity with basic finance and accounting practices, including the ability to read and understand the Banks' combined balance sheets and income statements and the relevant financial statements of the OF and to ask substantive questions of management and the internal and external auditors with regard to both the combined financial statements of the Bank System and the operations and financial statements of the OF, as appropriate; and

(4) Direct the operations of the OF in conformity with the requirements set forth in the Bank Act, Safety and Soundness Act, and this chapter.

(b) *Meetings and quorum.* The OF board of directors shall conduct its business by majority vote of its members at meetings convened in accordance with its by-laws, and shall hold no fewer than six in-person meetings annually. Due notice shall be given to FHFA by the Chair prior to each meeting. A quorum, for purposes of meetings of the OF board of directors, shall require a majority of sitting board members, which must include a majority of sitting Independent Directors.

(c) *Duties regarding COs.* The OF board of directors shall oversee the establishment of policies regarding COs that shall:

(1) Govern the frequency and timing of issuance, issue size, minimum denomination, CO concessions, underwriter qualifications, currency of issuance, interest-rate change or conversion features, call features, principal indexing features, selection and retention of outside counsel, selection of clearing organizations, and the selection and compensation of underwriters for consolidated obligations, which shall be in accordance with the requirements and limitations set forth in paragraph (c)(4) of this section;

(2) Prohibit the issuance of COs intended to be privately placed with or sold without the participation of an underwriter to retail investors, or issued with a concession structure designed to facilitate the placement of the COs in retail accounts, unless the OF has given notice to the board of directors of each Bank describing a policy permitting such issuances, soliciting comments from each Bank's board of directors, and considering the comments received before adopting a policy permitting such issuance activities;

(3) Require all broker-dealers or underwriters under contract to the OF to have and maintain adequate suitability sales practices and policies, which shall be acceptable to, and subject to review by, the OF;

(4) Require that COs shall be issued efficiently and at the lowest all-in funding costs over time, consistent with—

(i) Prudent risk-management practices, prudential debt parameters, short and long-term market conditions, and the Banks' role as GSEs;

(ii) Maintaining reliable access to the short-term and long-term capital markets; and

(iii) Positioning the issuance of debt to take advantage of current and future capital market opportunities.

(d) *Other duties.* The OF board of directors shall:

(1) Set policies for management and operation of the OF;

(2) Approve a strategic business plan for the OF in accordance with the provisions of § 917.5 of this title, as appropriate;

(3) Review, adopt and monitor annual operating and capital budgets of the OF in accordance with the provisions of § 917.8 of this title, as appropriate;

(4) Select, employ, determine the compensation for, and assign the duties and functions of a Chief Executive Officer of the OF who shall—

(i) Be head of the OF and direct the implementation of the OF board of directors' policies;

(ii) Serve as a member of the Directorate of the FICO, pursuant to section 21(b)(1)(A) of the Bank Act (12 U.S.C. 1441(b)(1)(A)); and

(iii) Serve as a member of the Directorate of the REFCORP, pursuant to section 21B(c)(1)(A) of the Bank Act (12 U.S.C. 1441b(c)(1)(A)).

(5) Review and approve all contracts of the OF, except for contracts for which exclusive authority is provided to the Audit Committee by paragraphs (b)(5) and (b)(6) of § 1273.9; and

(6) Assume any other responsibilities that may from time to time be assigned to it by FHFA.

(e) *No rights created.* Nothing in this part shall create or be deemed to create any rights in any third party.

#### § 1273.9 Audit Committee.

(a) *Composition.* The Independent Directors shall serve as the Audit Committee. The Audit Committee shall elect its chairperson from among its members. The Chairperson of the OF may also serve as chairperson of the Audit Committee, if the Audit Committee members so decide.

(b) *Responsibilities.*—(1) The Audit Committee shall be responsible for overseeing the audit function of the OF and the preparation and the accurate and meaningful combination of information submitted by the Banks in the Bank System's combined financial reports.

(2) For purposes of the combined financial reports, the Audit Committee shall ensure that the Banks adopt consistent accounting policies and procedures to the extent necessary for information submitted by the Banks to the OF to be combined to create accurate and meaningful combined financial reports.

(3) The Audit Committee, in consultation with FHFA, may establish common accounting policies and procedures for the information submitted by the Banks to the OF for the combined financial reports where the Committee determines such information provided by the several Banks is inconsistent and that consistent policies and procedures regarding that information are necessary to create accurate and meaningful combined financial reports.

(4) To the extent possible the Audit Committee shall operate consistent with the requirements pertaining to audit committee reports set forth in Item 407(d)(3) of Regulation S-K promulgated by the Securities and Exchange Commission.

(5) The Audit Committee shall oversee internal audit activities, including the selection, evaluation, compensation and, where appropriate, replacement of the internal auditor. The internal auditor shall report directly to the Audit Committee and administratively to executive management.

(6) The Audit Committee shall have the exclusive authority to employ and contract for the services of an independent, external auditor for the Banks' annual and quarterly combined financial statements and of an independent, external auditor for OF.

(7) The Audit Committee shall direct senior management to maintain the reliability and integrity of the

accounting policies and financial reporting of the OF.

(8) The Audit Committee shall review the basis for the OF's financial statements and the external auditor's opinion rendered with respect to such financial statements.

(9) The Audit Committee shall ensure that senior management has established and is maintaining an adequate internal control system within the OF by:

(i) Reviewing the OF's internal control system and the resolution of identified material weaknesses and reportable conditions in the internal control system, including the prevention or detection of management override or compromise of the internal control system; and

(ii) Reviewing the programs and policies of the OF designed to ensure compliance with applicable laws, regulations, and policies and monitoring the results of these compliance efforts.

(10) The Audit Committee shall review the policies and procedures established by senior management to assess and monitor implementation of the OF strategic business plan and the operating goals and objectives contained therein.

(11) The Audit Committee shall provide an independent, direct channel of communication between the OF's board of directors and the internal and external auditors.

(12) The Audit Committee shall conduct or authorize investigations into any matters within the Audit Committee's scope of responsibilities.

(13) The Audit Committee shall report periodically its findings to the OF's board of directors.

(14) The Audit Committee shall prepare written minutes of each Audit Committee meeting.

(c) *Charter.*—(1) The Audit Committee shall adopt, and the OF board of directors shall approve, a formal written charter, consistent with the duties and authority set forth in this section, that specifies the scope of the Audit Committee's powers and responsibilities. The Audit Committee and the OF board of directors shall:

(i) Review, and assess the adequacy of and, where appropriate, amend the Audit Committee charter on an annual basis; and

(ii) Re-adopt and re-approve, respectively, the Audit Committee charter not less often than every three years.

(2) The charter of the Audit Committee shall be subject to review and approval by FHFA.

(d) *No delegation.* The Audit Committee may not delegate the responsibilities assigned to it under this

section to any person, or to any other committee or sub-committee of the OF board of directors.

#### § 1273.10 Transition.

(a) Within 45 calendar days of the date on which FHFA first appoints an Independent Director pursuant to § 1273.7(c) of this part, the OF board of directors as structured under this part shall hold an organizational meeting. At the time of such meeting, the OF board of directors and its Audit Committee shall be deemed to be reconstituted in accordance with this part, and, except as set forth in paragraph (c) of this section, shall thereafter operate in accordance with this part. The date of this organizational meeting shall be set by the Independent Director that has been appointed as Chairman of the OF board of directors by FHFA pursuant to § 1273.7(e) of this part.

(b) Until the date of the organizational meeting required by paragraph (a) of this section, the board of directors of OF, and audit committee thereof, as in existence immediately prior to the effective date of this rule, shall continue to have power and authority to act as the OF board of directors or audit committee thereof, as applicable. Further, the board members who served as Chair and Vice-Chair of the OF board immediately prior to the effective date of this rule shall continue also to serve in these capacities until the date of the organizational meeting required under paragraph (a).

(c) Further, the audit committee as in existence immediately prior to the effective date of this rule shall continue to have responsibility and oversight authority with regard to the preparation and publication of the combined financial report for any reporting period that ends prior to July 1, 2010, unless the board of directors established under this part determines that the Audit Committee as established under this part should be given such responsibility.

#### Appendix A to Part 1273—Exceptions to the General Disclosure Standards

*A. Related-party transactions.* Item 404 of Regulation S–K, 17 CFR 229.404, requires the disclosure of certain relationships and related party transactions. In light of the cooperative nature of the Bank System, related-party transactions are to be expected, and a disclosure of all related-party transactions that meet the threshold would not be meaningful. Instead, the combined annual report will disclose the percent of advances to members an officer of which serves as a Bank director, and list the top ten holders of advances in the Bank System and the top five holders of advances by Bank, with a further disclosure indicating which of

these members had an officer that served as a Bank director. The combined financial report will also disclose the top ten holders of advances in the Bank System by holding company, where the advances of all affiliates within a holding company are aggregated.

*B. Biographical information.* The biographical information required by Items 401 and 405 of Regulation S–K, 17 CFR 229.401 and 405, will be provided only for members of the OF board of directors, including the Bank presidents, the Chair and Vice-Chair of the board of directors of each Bank, and the Chief Executive Officer of OF.

*C. Compensation.* The information on compensation required by Item 402 of Regulation S–K, 17 CFR 229.402, will be provided only for Bank presidents and the CEO of the OF. Since stock in each Bank trades at par, the OF will not include the performance graph specified in Item 402(1) of Regulation S–K, 17 CFR 229.402(1).

*D. Submission of matters to a vote of stockholders.* No information will be presented on matters submitted to shareholders for a vote, as otherwise required by Item 4 of the SEC's form 10–K, 17 CFR 249.310. The only item shareholders vote upon is the annual election of directors.

*E. Exhibits.* The exhibits required by Item 601 of Regulation S–K, 17 CFR 229.601, are not applicable and will not be provided.

*F. Per share information.* The statement of financial information required by Items 301 and 302 of Rule S–K, 17 CFR 229.301 and 302, is inapplicable because the shares of the Banks are subscription capital that trades at par, and the shares expand or contract with changes in member assets or advance levels.

*G. Beneficial ownership.* Item 403 of Rule S–K, 17 CFR 229.403, requires the disclosure of security ownership of certain beneficial owners and management. The combined financial report will provide a listing of the ten largest holders of capital stock in the Bank System and a listing of the five largest holders of capital stock by Bank. This listing will also indicate which members had an officer that served as a director of a Bank. The combined financial report will also disclose the top ten holders of Bank stock in the Bank System by holding company, where the Bank stock of all affiliates within a holding company is aggregated.

■ 4. Add part 1274 to subchapter D to read as follows:

#### PART 1274—FINANCIAL STATEMENTS OF THE BANKS

Sec.

1274.1 Definitions.

1274.2 Audit requirements.

1274.3 Requirements to provide financial and other information to FHFA and the OF.

**Authority:** 12 U.S.C. 1426, 1431, 4511(b), 4513, 4526(a).

##### § 1274.1 Definitions.

For purposes of this part:

*Audit* means an examination of the financial statements by an independent accountant in accordance with generally accepted auditing standards for the

purpose of expressing an opinion thereon.

*Audit report* means a document in which an independent accountant indicates the scope the audit made and sets forth an opinion regarding the financial statement taken as a whole, or an assertion to the effect that an overall opinion cannot be expressed. When an overall opinion cannot be expressed, the reasons therefor shall be stated.

*Bank* written in title case, means a Federal Home Loan Bank established under section 12 of the Bank Act (12 U.S.C. 1432).

*Bank System* means the Federal Home Loan Bank System, consisting of the twelve Banks and the Office of Finance.

*FHFA* means the Federal Housing Finance Agency.

*Financing Corporation* or *FICO* means the Financing Corporation established and supervised by FHFA under section 21 of the Bank Act (12 U.S.C. 1441).

*Office of Finance* or *OF* has the same meaning as set forth in § 1273.1 of this chapter.

##### § 1274.2 Audit requirements.

(a) Each Bank, the OF, and the FICO shall obtain annually an independent external audit of and an audit report on its individual financial statement.

(b) The OF audit committee shall obtain an audit and an audit report on the combined annual financial statements for the Bank System.

(c) All audits must be conducted in accordance with generally accepted auditing standards and in accordance with the most current government auditing standards issued by the Office of the Comptroller General of the United States.

(d) An independent, external auditor must meet at least twice each year with the audit committee of each Bank, the audit committee of OF, and the FICO Directorate.

(e) FHFA examiners shall have unrestricted access to all auditors' work papers and to the auditors to address substantive accounting issues that may arise during the course of any audit.

##### § 1274.3 Requirements to provide financial and other information to FHFA and the OF.

In order to facilitate the preparation by the OF of combined Bank System annual and quarterly reports, each Bank shall provide to the OF in such form and within such timeframes as FHFA or the OF shall specify, all financial and other information and assistance that the OF shall request for that purpose. Nothing in this section shall contravene or be deemed to circumscribe in any manner the authority of FHFA to obtain any information from any Bank related

to the preparation or review of any financial report.

Dated: April 26, 2010.

**Edward J. DeMarco,**

*Acting Director, Federal Housing Finance Agency.*

[FR Doc. 2010-10075 Filed 4-30-10; 8:45 am]

**BILLING CODE P**

## ENVIRONMENTAL PROTECTION AGENCY

### 40 CFR Part 52

[EPA-R06-OAR-2007-0993; FRL-9144-4]

#### Approval and Promulgation of Implementation Plans; New Mexico; Interstate Transport of Pollution

**AGENCY:** Environmental Protection Agency (EPA).

**ACTION:** Withdrawal of direct final rule.

**SUMMARY:** On April 8, 2010 (75 FR 17868), EPA published a direct final rule approving New Mexico State Implementation Plan (SIP) revisions that addressed one element of the “good neighbor” provisions of the Clean Air Act (CAA) for the 1997 ozone standards and the 1997 PM<sub>2.5</sub> standards. The direct final action was published without prior proposal because EPA anticipated no adverse comments. EPA stated in the direct final rule that if EPA received adverse comments by May 10, 2010, EPA would publish a timely withdrawal in the **Federal Register**. EPA subsequently received timely adverse comments on the direct final rule. Therefore, EPA is withdrawing the direct final approval. EPA will address the comments in a subsequent final action based on the parallel proposal also published on April 8, 2010 (75 FR 17894). As stated in the parallel proposal, EPA will not institute a second comment period on this action.

**DATES:** The direct final rule published on April 8, 2010 (75 FR 17868), is withdrawn as of May 3, 2010.

**FOR FURTHER INFORMATION CONTACT:** Emad Shahin, Air Planning Section (6PD-L), Environmental Protection Agency, Region 6, 1445 Ross Avenue, Suite 700, Dallas, Texas 75202-2733, telephone 214-665-6717; fax number 214-665-7263; e-mail address [shahin.emad@epa.gov](mailto:shahin.emad@epa.gov).

#### List of Subjects in 40 CFR Part 52

Environmental protection, Air pollution control, Incorporation by reference, Intergovernmental relations, Ozone, Particulate matter, Reporting and recordkeeping requirements, Volatile organic compounds.

Dated: April 24, 2010.

**Al Armendariz,**

*Regional Administrator, Region 6.*

■ Accordingly, the amendments to 40 CFR 52.1620 published in the **Federal Register** on April 8, 2010 (75 FR 17868), which were to become effective on June 7, 2010, are withdrawn.

[FR Doc. 2010-10233 Filed 4-30-10; 8:45 am]

**BILLING CODE 6560-50-P**

## ENVIRONMENTAL PROTECTION AGENCY

### 40 CFR Part 82

[EPA-HQ-OAR-2009-0351; FRL-9144-5]

RIN 2060-AP62

#### Protection of Stratospheric Ozone: The 2010 Critical Use Exemption From the Phaseout of Methyl Bromide

**AGENCY:** Environmental Protection Agency (EPA).

**ACTION:** Final rule.

**SUMMARY:** This final rule authorizes uses of methyl bromide that qualify for the 2010 critical use exemption and the amount of methyl bromide that may be produced, imported, or supplied from existing pre-phaseout inventory for those uses in 2010. EPA is taking action under the authority of the Clean Air Act to reflect a recent consensus decision taken by the Parties to the Montreal Protocol on Substances that Deplete the Ozone Layer at the Twentieth Meeting of the Parties.

**DATES:** This rule is effective on May 3, 2010.

**ADDRESSES:** EPA has established a docket for this action identified under EPA-HQ-OAR-2009-0351. All documents in the docket are listed on the <http://www.regulations.gov> site. Although listed in the index, some information is not publicly available, e.g., CBI or other information whose disclosure is restricted by statute. Certain other material, such as copyrighted material, is not placed on the Internet and will be publicly available only in hard copy form. Publicly available docket materials are available only through <http://www.regulations.gov> or in hard copy. To obtain copies of materials in hard copy, please call the EPA Docket Center at (202) 564-1744 between the hours of 8:30 a.m.–4:30 p.m. E.S.T., Monday–Friday, excluding legal holidays, to schedule an appointment. The EPA Docket Center’s Public Reading Room address is EPA/DC, EPA West, Room 3334, 1301 Constitution Ave., NW., Washington, DC.

#### FOR FURTHER INFORMATION CONTACT:

Jeremy Arling by telephone at (202) 343-9055, or by e-mail at [arling.jeremy@epa.gov](mailto:arling.jeremy@epa.gov) or by mail at U.S. Environmental Protection Agency, Stratospheric Protection Division, Stratospheric Program Implementation Branch (6205), 1200 Pennsylvania Avenue, NW., Washington, DC, 20460. You may also visit the Ozone Depletion Web site of EPA’s Stratospheric Protection Division at <http://www.epa.gov/ozone/strathome.html> for further information about EPA’s Stratospheric Ozone Protection regulations, the science of ozone layer depletion, and related topics.

**SUPPLEMENTARY INFORMATION:** This final rule concerns Clean Air Act (CAA) restrictions on the consumption, production, and use of methyl bromide (a Class I, Group VI controlled substance) for critical uses during calendar year 2010. Under the Clean Air Act, methyl bromide consumption (consumption is defined under the CAA as production plus imports minus exports) and production was phased out on January 1, 2005, apart from allowable exemptions, such as the critical use exemption and the quarantine and preshipment (QPS) exemption. With this action, EPA is authorizing the uses that qualify for the 2010 critical use exemption as well as specific amounts of methyl bromide that may be produced, imported, or supplied from pre-phaseout inventory for critical uses in 2010.

Section 553(d) of the Administrative Procedure Act (APA), 5 U.S.C. Chapter 5, generally provides that rules may not take effect earlier than 30 days after they are published in the **Federal Register**. EPA is issuing this final rule under section 307(d)(1) of the Clean Air Act, which states: “The provisions of section 553 through 557 \* \* \* of Title 5 shall not, except as expressly provided in this section, apply to actions to which this subsection applies.” Thus, section 553(d) of the APA does not apply to this rule. EPA is nevertheless acting consistently with the policies underlying APA section 553(d) in making this rule effective on May 3, 2010. APA section 553(d) provides an exception for any action that grants or recognizes an exemption or relieves a restriction. This final rule grants an exemption from the phaseout of methyl bromide.

#### Table of Contents

- I. General Information
  - Regulated Entities
- II. What is methyl bromide?