

Federal Housing Finance Board

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January 11, 2001

Mr. Harvey Simon
General Counsel
Federal Home Loan Bank of Dallas
8500 Freepoint Parkway, South
Suite 100
Irving, Texas 75063-2547

Re: Request for Supplemental Information Pursuant to Section 907.12(d) -- Petition for Case-by-Case Determination-- Membership Based on Convenience Washington Mutual Bank, FA

Dear Harvey:

The Federal Housing Finance Board (Finance Board) has received a Petition for Case-by-Case Determination from the Federal Home Loan Bank (Bank) of Dallas, dated December 8, 2000 (Petition), and received by the Finance Board on December 11, 2000. The Petition requests that the Finance Board approve the membership of Washington Mutual Bank, FA (WMBFA), currently a member of the San Francisco Bank, in the Dallas Bank upon completion of the merger of Bank United into WMBFA, under the "demanded by convenience standard" for membership in an adjoining Bank District contained in section 4(b) of the Federal Home Loan Bank Act (Bank Act) and section 925.18(a)(2) of the Finance Board's regulations. See 12 U.S.C. § 1424(b); 12 CFR § 925.18(a)(2). The effect of such an approval would be to allow WMBFA to be a member of both the San Francisco and the Dallas Banks. The Finance Board has not established any specific standards, guidelines or criteria for what constitutes "demanded by convenience" under section 4(b), and has never acted to approve single or dual membership under this provision.

After reviewing the Petition, and, pursuant to section 907.12(d) of the Finance Board's regulations, 12 C.F.R. § 907.12(d), the Finance Board is requesting that the Dallas Bank provide to the Finance Board in writing the following supplemental information (Request)

' The information requests contained in this Request should not be viewed as indicating the Finance Board's legal or policy positions on any of the specific issues raised by the Petition. For example, certain

A. Technical Questions Regarding the Proposal

1. According to the Petition, WMBFA is awaiting approval from its primary bank regulators of its proposed acquisition of Bank United, which would be merged into WMBFA and its charter cancelled. Please provide a detailed description of the organizational structure of each institution prior to the merger, and the organizational structure of the surviving institution after the merger, including all financial and non-financial subsidiaries, holding companies and affiliates. An organizational flow chart would be helpful in this regard.
2. Please describe which, if any, entities in the organizational structures of the two institutions have now or will have exempt multiple or unitary thrift holding company status, or financial holding company status, before and after the merger, and the effect on such status of: (i) merging WMBFA and Bank United; and (ii) holding Bank United as a separate subsidiary. In addition, please explain the benefits and/or restrictions associated with such status and losing such status. Include all applicable statutory and regulatory citations.
3. Does WMBFA's acquisition agreement with Bank United contain any contingencies or default provisions related to WMBFA being able to eliminate the Bank United charter and/or maintaining membership in the Dallas Bank? Does the acquisition agreement have any default provisions that are triggered if the February 1, 2001 date for closing the transaction is missed? How will WMBFA's operations be affected if the acquisition closes, but WMBFA retains the Bank United charter for some interim period of time?
4. The Petition states that, in order to maintain the status quo with regard to the economic impact of the Bank United merger on the Dallas Bank, WMBFA's ability to borrow from the Dallas Bank would be limited to the amount of advances Bank United has outstanding at the time the merger transaction closes, and such amount may be increased only by the amount required to fund "on-going operations" of the acquired Bank United entity. Please explain whether the amount that may be increased refers to the outstanding amount of advances at any given point of time, what is meant by "ongoing operations," and how this would be administered. See Question C.3. In addition, please explain why it is your belief that maintaining the economic status quo at the Dallas Bank would be an appropriate standard generally for allowing dual membership.

B. Convenience of the San Francisco Bank

The Petition states that if dual membership is not permitted for WMBFA, the advances and Affordable Housing Program (AHP) business arising from former Bank United offices necessarily will increase the demands and operational burdens placed on the San Francisco Bank and, therefore, that the convenience of the San Francisco Bank demands dual membership for WMBFA. Please demonstrate whether the San Francisco Bank concurs that dual membership should be approved, and submit any evidence you have that the San Francisco Bank could not devote additional resources necessary to meet such increased demands and operational burdens and concurs in the Dallas Bank's representations that membership of WMBFA in the Dallas Bank would be demanded by the convenience of the San Francisco Bank.

questions assume, solely for purposes of this Request, that analyzing the convenience of the Banks is relevant in determining whether membership in an adjoining Bank District is "demanded by convenience" under section 4(b) of the Bank Act.

C. Convenience of the Dallas Bank

1. The Petition states that, in Bank Districts whose members disproportionately disappear in mergers, "[t]he ability of [such] Banks . . . to advance the housing needs of the residents of the District, such as affordable housing goals, will become increasingly difficult." Please explain why, after its merger with Bank United, WMBFA would not be able to continue to provide funding, using advances from the San Francisco Bank, to further the housing needs of the residents of the Dallas Bank District.
2. The Petition states that dual membership "will protect the Dallas [Bank's] strength." Please describe the effect on the Dallas Bank's financial condition, including assets, earnings and contributions to the AHP, if WMBFA were not permitted to become a member of the Dallas Bank after the merger, and provide a copy of the portion of the Dallas Bank's Strategic Plan that describes the Dallas Bank's plan for dealing with the loss of this member.
3. The Petition states that merging Bank United into WMBFA, rather than holding Bank United as a separate subsidiary, would result in "administrative simplification and operational efficiencies." Elsewhere, the Petition states that membership of WMBFA in the Dallas Bank would allow WMBFA "seamlessly to step into the place of Bank United." Please reconcile these two statements, explaining in greater detail the administrative simplification and operational efficiencies expected after the merger.

D. Convenience of the Bank System

Dual or multiple membership would affect all of the Banks, each of which has large members with branch offices in multiple states. At least one member has branch offices in 15 different states and 6 different Bank Districts. Please provide a brief analysis of the consequences of multiple Bank membership on a System-wide basis, particularly with respect to the following factors:

1. The Petition states that permitting simultaneous membership in two adjoining Banks "is necessary to prevent interstate expansion and consolidation from causing distortions and imbalances in the Bank System that would impede the expansion of home finance." Please describe briefly the types of distortions and imbalances contemplated, how such distortions and imbalances would impede the expansion of home finance, and how allowing simultaneous membership in different Bank Districts would prevent such distortions and imbalances. Provide the evidence that shows that housing finance will decrease if dual membership is denied. Does WMBFA intend to curtail its mortgage lending in the Dallas Bank District without dual membership? See Question C. 1.
2. Please explain why the Finance Board's statutory power to realign Bank Districts would be insufficient to address any such imbalances, should they prove to be a problem. See 12 U.S.C. §§ 1423, 1446.
3. Please describe briefly the effect multiple Bank membership could have on large interstate member control or influence over the Banks of which it would be a member, as compared to the current structure, and whether that change would disrupt or enhance the cooperative nature of the Bank System.

4. Please describe briefly the effect multiple Bank membership would have on a large interstate member's ability to "District shop" among the Banks to obtain services, credit products pricing and dividend rates on more favorable terms than would be available to members that have no interstate branch offices, as compared to the current structure. Discuss briefly the implications of such forum shopping, including whether this would tend to destabilize or enhance the cooperative nature of the Bank System. Describe what actions the Dallas Bank will take to protect itself from such possibilities. Is WMBFA committing to fund mortgage lending in the Dallas Bank District with Dallas Bank advances only?

5. Under the existing capital stock purchase requirements of the Bank Act, which remain in effect until a Bank implements its new capital structure plan under the Gramm-Leach-Bliley Act, a member is required to purchase capital stock in a Bank equal to the greater of 1 percent of its residential mortgage assets or 5 percent of advances outstanding to such member. If WMBFA, after the merger with Bank United, were to be a member of both the Dallas and San Francisco Banks, how would the 1 percent capital stock purchase requirement be implemented? Would WMBFA be required to hold capital stock in each Bank that equaled or exceeded 1 percent of WMBFA's residential mortgage assets? If so, would this amount exceed 5 percent of the advances outstanding from the Dallas Bank? If so, what plans does the Dallas Bank have to employ this additional capital? What statutory or regulatory bases, if any, would allow the Dallas Bank to ignore the 1 percent capital stock purchase requirement?

6. Please describe briefly how introducing the volatility of multiple Bank membership at this time would affect the ability of the Banks to create capital structure plans pursuant to the capital provisions of the Gramm-Leach-Bailey Act.

Legal Arguments

Our preliminary research has revealed significantly more legislative history regarding the issues of multiple Bank membership and adjoining Bank District membership under the Bank Act than is referenced in the November 28, 2000 Legal Memorandum (Exhibit C) (Legal Memorandum) accompanying the Petition. We would appreciate your analysis of the following issues raised by our research:

1. The Legal Memorandum argues that the first usage of the word "or" in section 4(b) of the Bank Act ("or secure advances from") is clearly conjunctive and, therefore, the language of the sentence supports reading the second usage of the word "or" in that same sentence also in the conjunctive. *See id.* § 1424(b). In quoting the original language of section 4(b), however, the Legal Memorandum omitted (without indicating the omission) language from section 4(b) regarding nonmember borrowers that is critical to any analysis of these provisions. The analysis in the Legal Memorandum also makes no reference to the nonmember borrower language that appears in this sentence as originally enacted in 1932. *See id.* §§ 1424(b), (e) (1989). That language appears to have been linked to the phrase "or secure advances from," which likely should have been removed in 1989 when the nonmember borrower references were removed from section 4(b) and other sections of the Bank Act by the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA). Reading section 4(b) as originally enacted argues against a conjunctive reading of the first and, therefore, also the second, usages of the word "or" in section 4(b). Please explain how a conjunctive reading of section 4(b) can be reconciled with this legislative history.

2. Statements made by the principal drafter of the original Bank Act legislation in 1932 Congressional hearings suggest that the possibility of multiple membership in more than one Bank district was considered and rejected. See Hearings Before A Subcommittee of the Committee on Banking and Currency on S. 2959 (Creation of a System of Federal Home Loan Banks), U.S. Senate, 72nd Congress, First Session (1932), at 116-117, 359-360 (Senate Hearings); Hearings Before A Subcommittee of the Committee on Banking and Currency on H.R. 7620 (Creation of a System of Federal Home Loan Banks), U.S. House of Representatives, 72nd Congress, First Session (1932), at 97-98 (House Hearings). Please explain how interpreting section 4(b) to permit multiple Bank membership can be reconciled with this legislative history.

3. Section 3 of the Bank Act provides that Bank Districts are to be “apportioned with due regard to the convenience and customary course of business of the institutions eligible to and likely” to join. See 12 U.S.C. § 1423 (emphasis added). The emphasized language is identical to that found in the Federal Reserve Act, which provides that the Federal Reserve Bank Districts shall be apportioned with due regard to the “convenience and customary course of business. . . .” See id. § 222. However, while the Federal Reserve Act provides that Federal Reserve Bank Districts “shall not necessarily be coterminous with any State or States,” the Bank Act provides that “no [Bank] district shall contain a fractional part of any State.” See id. §§ 222, 1423. By requiring that states not be divided into fractions, the Bank Act created a situation where, despite the “convenience and customary course of business” requirement in section 3, some institutions would not be able to belong to the Bank that, because of proximity, was the most convenient for such institution.

Section 3 is essentially unchanged from the language of the Bank Act as originally proposed in 1932. The original bill appears to have addressed the convenience problem caused by the requirement that states not be divided into fractions by providing in section 4(b) that an institution could unilaterally choose to join a Bank in an adjoining District, with no restriction placed on this right. Concerns subsequently were raised that an institution would be allowed to become a member of an adjoining District irrespective of the distance between the Bank of the adjoining District and the applicant. During the House Hearings, a change was proposed to section 4(b), and ultimately incorporated into the final legislation, to allow adjoining District membership only “if demanded by convenience and then only with the consent and approval of the [B]oard.” See House Hearings, at 199. The language in section 4(b), thus, appears to indicate that membership in an adjoining District should be determined based on the convenience of the member, rather than on the convenience of the Banks. Given this legislative history, please explain why the convenience of the Dallas and San Francisco Banks, and the Bank System as a whole, should be considered by the Finance Board in determining whether WMBFA should be granted membership in multiple adjoining Districts under section 4(b).

Pursuant to section 907.12(d) of the Finance Board's regulations, 12 C.F.R. § 907.12(d), responses to this Request must be submitted in writing no later than 20 calendar days after the date of this Request, to: Elaine L. Baker, Secretary to the Board, at the Federal Housing Finance Board, 1777 F Street, N.W., Washington, D.C. 20006.

Sincerely,

James L. Bothwell

Managing Director cc: Terry Smith