

PFI Advisory

April 1, 2002

Special Attention:

PFI's MPF® Program Management

Subject:

Revised Risk-Based Capital Requirements – Impact for **Original MPF** Participants

Regulatory Update:

The four Banking Agencies (Federal Reserve, FDIC, OCC and OTS) adopted a risk-based capital rule in late 2001. This Advisory provides an overview of the rule's impact on Original MPF participants.

Brief Overview

The new capital rule is not expected to affect capital requirements for Original MPF Master Commitments. The new rule establishes a credit risk-based approach to determine risk-based capital requirements. For Original MPF Master Commitments we believe the new rule will result in an initial capital treatment that is the same as the prior rule.

The basic principle of the credit risk-based approach is that if a Participating Financial Institution's (PFI's) risk position – the PFI's Credit Enhancement (CE) obligation after the credit enhancement provided by the First Loss Account (FLA) – is lower than "BB" the PFI would be required to hold capital equal to the previous capital requirement. The FLA feature of the Original MPF product provides coverage for expected losses but generally not for "BB" or better risk levels. This results in the same risk-based capital requirement as the prior rule.

Timing

The MPF Provider is taking the necessary steps to secure Banking Agency qualification of the MPF Program. We hope to complete this process shortly. The effective date of the new capital rule was January 1, 2002 so that, for qualified products, changes in capital would begin to be reported in first quarter call reports.

When Banking Agency qualification is received, the MPF Provider will notify PFIs, and will provide details concerning capital requirements for each Master Commitment.

Other Issues

Press coverage of the new risk-based capital rule has emphasized the stringent capital requirements in the rule for residual interests. However, the MPF Program does not create “residual interests” as defined in the rule. Hence, the capital requirements in the rule regarding residual interests will not apply to any MPF products.

Additional information concerning revised capital requirements for each MPF product will be provided in a subsequent PFI Advisory. That Advisory will be issued after Banking Agency qualification of the MPF Program is obtained, and assistance will be provided to PFIs as needed prior to that time.

Please contact your MPF Marketing representative should you have any questions regarding this advisory.