REPORT TO THE CONGRESS

BY THE COMPTROLLER GENERAL OF THE UNITED STATES

Examination Of Financial Statements Of The Federal Home Loan Banking System: A Favorable Opinion But Some Management Problems

These financial statements present fairly the position of the Federal Home Loan Bank Board and its related organizations at December 31, 1976 and 1975. However, there are some management problems.

The Board's internal audit organizational structure does not insure maximum audit independence and conflicts with congressional intent and Board policy.

The Bank's imprest fund has financed, without congressional review, certain activities benefiting the Board.

The Congress should require the Board to submit all imprest fund budgets and expenditure information for consideration during its budget hearings.

The chairman of the Board should revise his internal audit organization so that maximum independence may be obtained.

FOD-77-15

OCTOBER 25, 1977

COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

B-114827

To the President of the Senate and the
Speaker of the House of Representatives

This report summarizes the results of our examination of the financial statements of the Federal Home Loan Bank Board, the Federal home loan banks, the Federal Savings and Loan Insurance Corporation, and the Federal Home Loan Mortgage Corporation for the year ended December 31, 1976.

We made our examination pursuant to the Budget and Accounting Act, 1921 (31 U.S.C. 53); the Accounting and Auditing Act of 1950 (31 U.S.C. 67); the Government Corporation Control Act, as amended (31 U.S.C. 850 and 857); the Federal Home Loan Bank Act, as amended (12 U.S.C. 1431(j)); and the Federal Home Loan Mortgage Corporation Act (12 U.S.C. 1456(b)).

We are sending copies of this report to the Director, Office of Management and Budget; the Secretary of the Treasury; the Acting Chairman of the Federal Home Loan Bank Board; and the Acting Chairman of the Board of Directors of the Federal Home Loan Mortgage Corporation.

Elmer B. Staats

Comptroller General
of the United States

COMPTROLLER GENERAL'S REPORT TO THE CONGRESS

EXAMINATION OF FINANCIAL STATEMENTS OF THE FEDERAL HOME LOAN BANKING SYSTEM: A FAVORABLE OPINION BUT SOME MANAGEMENT PROBLEMS

D I G E S T

The Federal Home Loan Bank Act, the Government Corporation Control Act, as amended, and the Federal Home Loan Mortgage Corporation Act, require the Comptroller General to examine the financial transactions of the Federal home loan banks, the Federal Savings and Loan Insurance Corporation, and the Federal Home Loan Mortgage Corporation.

The Federal Home Loan Bank Board supervises the activities of the banks and both Corporations; therefore, GAO included the Board's financial statements in its examination.

During 1976 the Office of Examinations and Supervision examined 3,270 savings and loan institutions. The Board used the information to identify problem institutions. The most serious cases are classified as category I, financially critical, and the next most serious cases are classified as category II, not financially critical but requiring aggressive supervisory attention. (See p. 18.)

At December 31, 1976, there were 13 category I and 70 category II problem institutions with estimated insured deposits of $658 million and $8,890 million, respectively. (See p. 25.)

The financial statements included in this report present fairly the position of the Board, Banks, and both Corporations at December 31, 1976 and 1975; the results of their operations; and the changes in financial position for the years then ended, in conformity with principles and standards of accounting prescribed by the Comptroller General of the United States.

FOD-77-15

The Board, despite previous GAO recommendations, continues to operate with an internal audit organizational structure which will not insure maximum independence. This structure requires the auditor to receive direction from supervisors who are directly or indirectly responsible for the management functions that can be audited. It is not generally used by other Federal agencies and conflicts with current congressional intent and Board policy.

The Board's decisions on the use of the Office of Finance's imprest fund have resulted in funding activities from this fund which benefit the Board but which did not receive congressional approval as did the Board's budget. (See p. 16.)

RECOMMENDATIONS

--The Congress should require the Board to submit all imprest fund budgets and expenditures information for consideration during its budget hearings. This would allow the identification of Board items being funded by other sources. (See p. 16.)

--The Chairman, Federal Home Loan Bank Board, should revise the Board's current internal audit organization structure so that maximum independence may be obtained. (See p. 9.)

GAO's recommendations were discussed with Board officials and their comments incorporated where appropriate. These officials stated that their internal audit organization is currently being studied by a private certified public accounting firm. GAO's comments will be considered along with the accounting firm's as soon as the study is completed. (See p. 9.)

Board officials stated that the imprest fund expenditures are insignificant when compared to the total budget of the Office of Finance. GAO believes the important issue is whether the Board is circumventing congressional oversight by paying for expenses from an imprest fund that is not reviewed by the Congress. (See p. 16.)

Contents

ABBREVIATIONS

FSLIC	Federal Savings and Loan Insurance Corporation
GAO	General Accounting Office

CHAPTER 1

INTRODUCTION

In the early 1930s, the Congress established three separate but interrelated organizations--the Federal Home Loan Bank Board, the Federal home loan banks, and the Federal Savings and Loan Insurance Corporation (FSLIC) to provide economical home financing and encourage thrift. The Congress created the Federal Home Loan Mortgage Corporation in 1970 to strengthen and further develop the secondary market in residential mortgages. The chart on the following page depicts the relationship of major agencies and offices within the Federal Home Loan Bank System.

This report covers our review of the Federal Home Loan Bank Board's calendar year 1976 financial statements. The report also discusses the need for increased independence of the Board's Internal Audit staff and the disclosure of all Board-related expenditure information to the Congress. These matters are discussed in chapters 2 and 3.

FEDERAL HOME LOAN BANK BOARD

The Board, an independent supervisory and regulatory agency, (1) regulates and supervises the operations of Federal home loan banks, (2) directs the operations of the Federal Savings and Loan Insurance Corporation and the Federal Home Loan Mortgage Corporation, (3) charters Federal savings and loan associations, and (4) regulates and examines institutions insured by the Federal Savings and Loan Insurance Corporation.

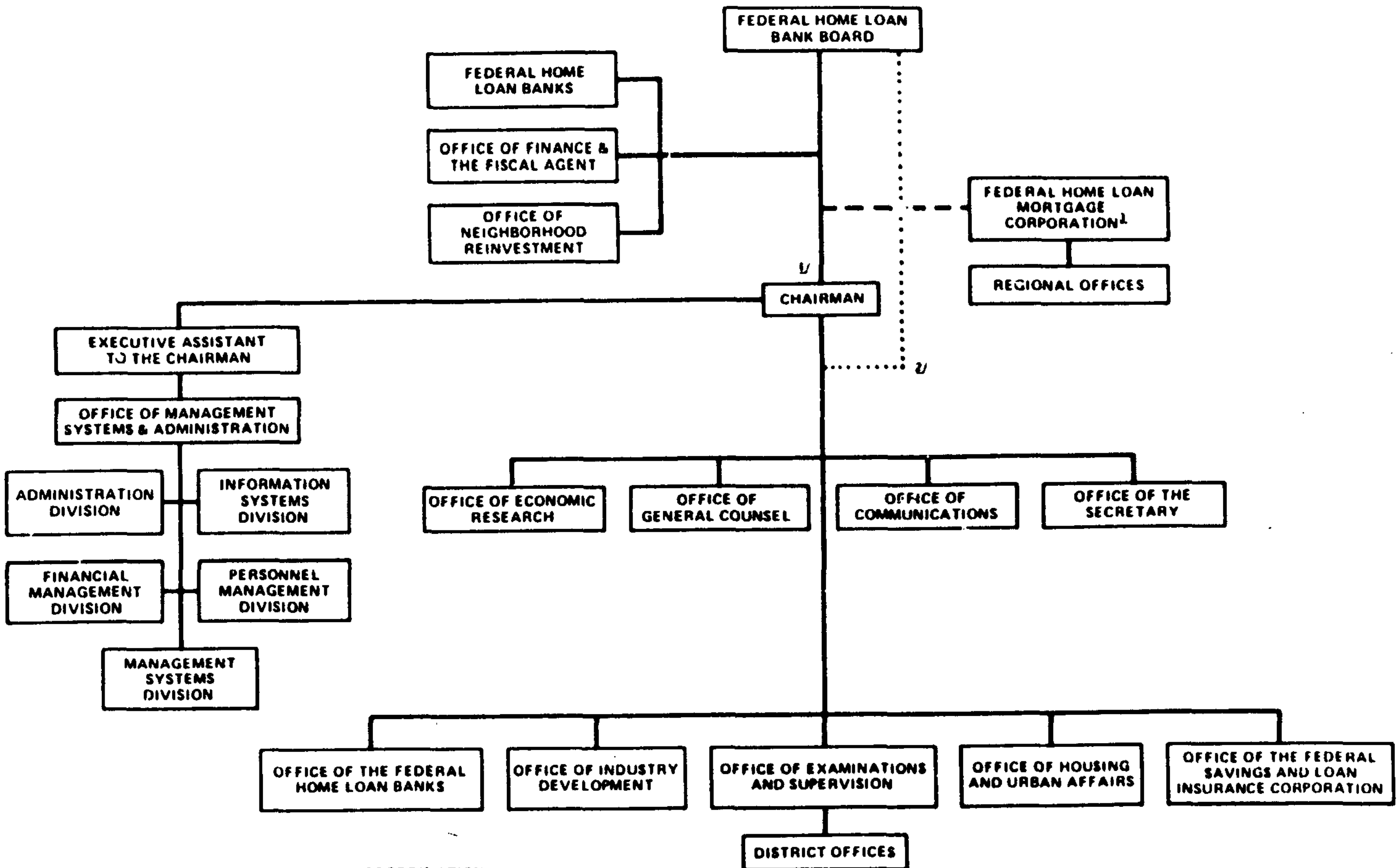
The Board is directed by a three-member Board of Directors appointed for 4-year terms by the President, with the advice and consent of the Senate. Appendix I lists the responsible officials discussed in this report.

FEDERAL HOME LOAN BANKS

The Federal Home Loan Bank Board may create no more than 12 nor less than 8 Federal home loan banks and may liquidate or reorganize any Federal home loan bank. The headquarters locations for the 12 bank districts are:

1. Atlanta, Georgia
2. Boston, Massachusetts
3. Chicago, Illinois
4. Cincinnati, Ohio
5. Des Moines, Iowa
6. Indianapolis, Indiana
7. Little Rock, Arkansas
8. New York, New York
9. Pittsburgh, Pennsylvania
10. San Francisco, California
11. Seattle, Washington
12. Topeka, Kansas

ORGANIZATIONAL CHART



1/ ——— ADMINISTRATIVE DIRECTION AND COORDINATION
2/ - - - - - - SUBSTANTIVE RESPONSIBILITIES
3/ THE BOARD MEMBERS OF THE FHLBB ALSO SERVE ON THE BOARD OF DIRECTORS OF THE MORTGAGE CORPORATION.
NOTE: THIS CHART ONLY DEPICTS OFFICES WITH AUDIT SIGNIFICANCE.

A Board of Directors operates each bank. Six members are appointed by the Board, and the remainder, ranging from eight to nine members, are elected by member institutions. Each bank's operating responsibility is vested in a president who is elected by the bank's Board of Directors subject to the approval of the Federal Home Loan Bank Board. The banks provide reserve banking facilities to their member institutions and to certain nonmember borrowers. Since their inception, the banks have provided checking accounts, investment counseling, safekeeping services, and more recently online computer services to member institutions.

FEDERAL SAVINGS AND LOAN INSURANCE CORPORATION

FSLIC, a wholly owned Government corporation, insures accounts of savers up to $40,000 for each member in all federally chartered savings and loan associations and similar institutions upon their request and approval by the Board.

The Board carries out certain FSLIC functions, such as processing applications for insurance and examining insured institutions. Other operating responsibilities, such as receivership activities and liquidation of assets, are vested in a director who is appointed by the Board.

FEDERAL HOME LOAN MORTGAGE CORPORATION

The Mortgage Corporation was created by the Congress to increase housing availability by strengthening and further developing the secondary market in residential mortgages. The Corporation fulfills its responsibilities by buying and selling mortgages. It purchases mortgages from members of the Federal Home Loan Bank System and other insured financial institutions.

The Corporation's Board of Directors is composed of members of the Board who serve in this dual capacity without additional compensation.

ACCOUNTING SYSTEMS

The Accounting and Auditing Act of 1950 places responsibility for establishing and maintaining adequate accounting systems and internal control with the head of each executive agency. These systems must meet the accounting principles, standards, and related requirements prescribed by the Comptroller General.

The act also requires that the Comptroller General approve accounting systems when they are deemed adequate and conform to prescribed principles, standards, and related requirements. This approval is not required of Government corporations subject to the Government Corporation Control Act, and certain quasi-governmental entities that, by law, are subject to that act. Accordingly, the accounting systems of the 12 home loan banks, FSLIC, and the Mortgage Corporation do not require approval by the Comptroller General. The Board's accounting system, however, must be approved by the Comptroller General.

The Comptroller General approved the Board's principles and standards for its accounting system on June 27, 1972. System design was submitted for our evaluation on August 29, 1975. After a preliminary review the design package was returned with recommendations for improvements on November 14, 1975. The Board has resubmitted sections of the design package and estimates that the remaining parts will be submitted to us by fall 1977.

CHAPTER 2

INTERNAL AUDIT--A QUESTION OF INDEPENDENCE

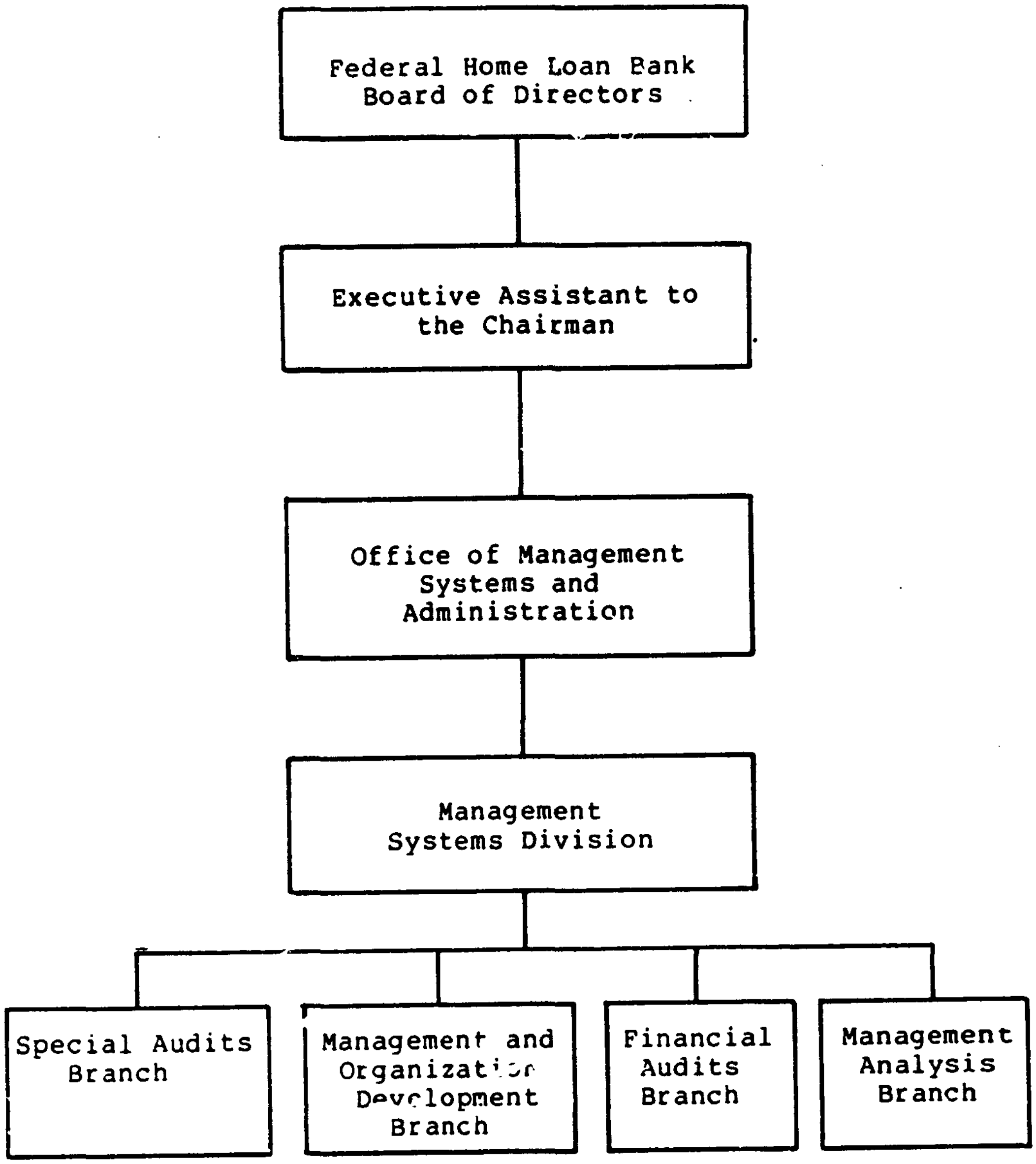
Internal auditing's objective is to assist management in attaining its goals by examining and issuing reports on its evaluations of the agency operations. The Board, each of the 12 Federal home loan banks, and the Mortgage Corporation have separate internal audit staffs. The Board's audit staff performs audits of FSLIC. We believe that each of the audit groups must be independent of line management if they are to be an effective management tool. The independence of the Board's audit staff, however, continues to be a matter of concern to us.

We have emphasized the importance of an auditor's independence by issuing audit standards for Federal agencies. The standards point out that the auditor's performance can be affected through the organizational structure because of the policy direction that can be received from superiors who are also involved either directly or indirectly in the line management process. Therefore, to achieve maximum independence, the auditor should be organizationally located outside the line management function of the entity under audit.

We have discussed internal audit organizational independence with Board officials on several occasions. In a 1974 letter to the Chairman, Federal Home Loan Bank Board, we expressed concern about the placement of the internal audit group in the organizational structure. In a 1976 letter to the Acting Chairman, Federal Home Loan Bank Board, we again expressed concern that the organizational structure could lack the necessary independence to assure an objective internal audit of the Board and FSLIC operations. We recommended the internal audit staff be removed organizationally from the line management function and report directly to the Board or an audit committee that is chaired by a Board member. However, as of June 1977, no change to the internal audit organizational placement had been made.

INCONSISTENCY IN BANK BOARD INSTRUCTIONS AND ORGANIZATIONAL PLACEMENT OF INTERNAL AUDIT

The Board's internal audit staff is divided into the Financial Audit Branch and the Special Audit Branch. The chart below shows the current placement of the Board's internal audit branches.


Federal Home Loan Bank Board of Directors
Executive Assistant to the Chairman
Office of Management Systems and Administration
Management Systems Division
Special Audits Branch
Management and Organization Development Branch
Financial Audits Branch
Management Analysis Branch

The Financial Audit Branch primarily conducts audits of the Board, FSLIC, and their related activities. The Financial Audit Branch Chief is responsible for forwarding the financial reports directly to the Board Directors. However, organizationally, the Financial Audit Branch Chief works under the Director, Management Systems Division.

According to the position description for the Branch Chief, Financial Audit, the Director Management Systems Division: (a) establishes the general scope and priority of the work to be performed by the Financial Audit Branch and (b) reviews the Audit Branch's assignments and reports. In addition, the Director will review and finalize the annual budget and training plans developed by the Chief Financial Auditor. The Director also has approval authority over branch hiring and promotion actions.

The Special Audits Branch conducts audits of Board-wide management problems and operations of Board offices. Although the Special Audits Branch Chief is responsible for reporting on the results of operational audit examinations, neither the Branch Chief position description nor the current functional organization chart specifies who should receive these reports. Board officials stated that either the Board Directors or the management official being audited would receive the report depending upon the severity of the problem(s) identified. They also stated the reporting decision is left to the Special Audit Branch Chief.

The organizational direction of the Special Audits Branch is the responsibility of the Director, Management Systems Division. According to the position description of the Special Audit Branch Chief, this Director: (a) establishes the general scope and priority of the work and (b) reviews completed assignments and reports for conformance with established policies and results achieved. The Director also has approval authority over Special Branch hiring, promotion, and budget activities.

The Director, Management Systems Division, is, in turn, under the control of the Director, Office of Management Systems and Administration. This Director has overall responsibility for financial management information systems and personnel management activities within the Board. All of these activities are subject to internal audit; therefore, the auditors assigned to these reviews are placed in the tenuous position of reviewing and reporting on the activities and deficiencies of higher management within their own organizational structure.

The Board's internal audit branch organization structure is inconsistent with the Internal Auditing Standards put forward by the Board for its banks to follow. These standards state:

> "To achieve maximum independence, the auditor and the audit organization itself not only should report directly to the Bank's Board of Directors or their Audit Committee, but should also be organizationally located outside the line management function of the Federal Home Loan Bank."

In addition, the Board's audit branch structure is also inconsistent with the internal audit structure used by the Mortgage Corporation. The Mortgage Corporation's internal audit division is located outside the line management structure and its chief internal auditor is required to report directly to the president. Thus, while the Board advocates audit organizational independence for the 12 banks and the Mortgage Corporation, it has not established a similar structure for itself.

INCONSISTENCY WITH OTHER FEDERAL AGENCIES

Under the branch organization structure, the Board's internal audit activity is located in the line management organization three levels removed from the Board Directors. This arrangement is not in line with the general Federal Government trend of making internal audit functions independent of the organizations audited.

As of April 1976, our examination of 49 other agencies' audit activities showed that only 8, including the Board, had the internal audit activity reporting to an individual more than one level below the agency head. In comparison, 18 audit groups reported directly to the heads of their agencies. The reporting level of the 49 audit groups was:

Reporting level	Number of audit groups
Directly to agency head	18
One level below agency head	23
More than one level below agency head	8

In addition, several agencies have recently changed their internal audit organization structures to have this function reporting directly to the agency head. For example, the Veterans Administration, whose internal audit organization was four levels removed from the agency head, changed its structure in 1977 to allow the audit group to report directly to the Administrator. In another instance, the Federal Deposit Insurance Corporation, a Federal banking regulatory agency with functions similar to the Bank Board, changed the organizational placement of its Office of Corporate Audits to allow that group to report directly to the Board of Directors.

Congressional interest in insuring the independence of Federal internal audit functions was recently shown in a report by the House Committee on Government Operations. In this report, the Committee recognized that audit units "lack independence and are subject to potential conflicts of interest" when "they report to officials who are directly responsible for managing the programs the units are investigating." Public Law 94-505 was subsequently passed which established a separate Office of Inspector General within the Department of Health, Education, and Welfare. This Office is to report to the Secretary and to the Congress on its activities.

CONCLUSIONS AND RECOMMENDATION

The Board is currently operating with an internal audit organizational structure which is not designed to insure maximum internal audit independence. This line-management structure is not generally used by other Federal agencies and is inconsistent with current congressional intent in the area.

Recommendation

Accordingly we recommend that the Chairman of the Board revise his internal audit organization so that maximum independence may be obtained.

AGENCY COMMENTS

Board officials stated that their internal audit organization structure is currently being studied by a private certified public accounting firm. Our comments will be considered along with the accounting firm's as soon as the study is completed.

CHAPTER 3

THE OFFICE OF FINANCE:

A FUNDING SOURCE FOR THE BOARD

The Board's expenditures are borne entirely by the savings and loan industry. These expenditures are met by assessing the 12 Federal home loan banks and FSLIC for services rendered and direct examination charges.

However, the Congress limits the expenditures by placing annual restrictions on the amounts spent. For example, in fiscal year 1977 the Board's administrative expenses were limited to $17.1 million and nonadministrative expenses to $23.6 million. These limitations were set as a result of annual congressional hearings during which the Bank Board provided a detailed justification describing the proposed expenditures of its activities. The actual amounts are reported once they are known.

The Office of Finance, created in 1972, performs the following functions:

1. Conducts all negotiations relating to the public or private offering and sale of consolidated Federal home loan bank obligations.

2. Conducts all negotiations for the purchase and/or sale of any securities on behalf of a Federal home loan bank.

3. Performs such duties as may be requested by the Board for the Federal home loan banks, FSLIC, and the Mortgage Corporation.

4. Performs such duties as were previously assigned to the fiscal agent.

The Office carries out its functions through an imprest fund which is financed through assessments levied against the 12 banks, FSLIC, the Mortgage Corporation, and the Office of Neighborhood Reinvestment. This assessment funding structure is similar to the Board's assessment activity except in one important aspect--the Office's imprest fund is not subject to congressional oversight.

When the imprest fund was created the Board Directors decided this would be principally a bank activity. However, it is the Board that controls the expenditures and not the banks. This has allowed the funding of $375,000 of activities in 1976 that has benefited the Board but which did not receive congressional review as did the Board's budget.

OFFICE OF FINANCE OPERATIONS

The Office of Finance employs 32 full-time noncivil servant employees and is organized into four divisions: Finance Planning, Investments, Debt Management, and Administrative Services. Its 1976 budget totaled $2.3 million, including $890,000 in salaries and employee benefits.

The Administrative Services Division is responsible for the administrative and personnel functions, including budgeting requirements and managing of the imprest fund. As custodian, the Division must insure there is adequate documentation to support disbursements.

The Debt Management Division develops and maintains a national group of security dealers to market the banks' consolidated obligations and Mortgage Corporation's securities. The Financial Planning Division analyzes financial alternatives, coordinates forecasts, and provides recommendations for the use of all Board activities. The Investment Division is responsible for advising and implementing an investment strategy for the banks, FSLIC, and the Mortgage Corporation. In addition, this Division provides reports and accounting services to each of these entities.

THE BOARD'S CONTROL OVER THE IMPREST FUND HAS INCREASED

In the beginning, the banks had substantial control over the Office of Finance activities. This control was maintained through a three-member budget committee elected by the 12 bank presidents. The committee was responsible for the Office's annual budget which was also approved by a majority of the presidents. The budget was then submitted to the Board for its review and approval. The Board reserved the authority to direct payments from this fund for such other expenditures which it deemed appropriate but not included in the budget.

Bank participation in the budget process was significantly reduced in February 1974, when the Board placed the Office's responsibilities under its direct control. The Board cited a meeting on January 15, 1974, where the bank presidents unanimously agreed that the previous procedures were unwieldy and inefficient and should be transferred. As the bank's participation declined, the Board's increased. This increased involvement is shown in both the budgeting and expenditure procedures.

The Office has three imprest fund budgets covering (a) the funding of specific programs and activities for the banks, (b) the operations of a Federal Savings and Loan Advisory Council, and (c) the operations of the Office of Finance. The first budget is prepared by the Bank Board's Office of Federal home loan banks. The other two budgets are subject to the approval of the Board before they can be adopted. In addition, the Board may also direct assessments for nonbudgetary items.

The Office's expenditure process is also substantially controlled by the Board. Three officials are currently authorized to certify imprest fund expenses: (a) the Secretary to the Board, (b) the Director of the Office of Finance, and (c) the Director of the Office of Federal home loan banks. All of these persons are either employed or appointed by the Board.

THE IMPREST FUND AND CONGRESSIONAL OVERSIGHT

In determining whether or not an activity should be funded through the normal congressionally limited funds process or the imprest fund, the Board has had to periodically decide whether the requirements were generated by it or the banks. The decision is extremely important because it determines whether information on expenditures is made available for congressional review. If the Board decides the requirements were generated by it, the activity will be reviewed by the Congress. If the decision is that the requirements were generated by the banks, the activity will be funded through the imprest fund. In this case, neither the proposed nor actual expenditures are reported to the Congress. Consequently, the Board's decision on the activity's funding source has a direct impact on whether the Congress has the opportunity to review these activities.

The Board's decisions have resulted in funding activities from the imprest fund which benefited the Board but which did not receive congressional approval as did the Board's budget. Examples of 1976 expenditures, totaling about $375,000, include (a) reviews of data processing centers, (b) a pay study for bank officials, (c) travel expenses for some Federal Savings and Loan Advisory Council members, (d) the establishment of a functional budget system, and (e) official and personal expenditures for Board and FSLIC employees.

Data center reviews

The Board has routinely requested congressional approval to spend moneys to conduct financial audits of banks. In 1974, it extended financial audits of selected banks to include a review of internal controls relating to their data center services. The Board believed there was a need for policies and guidelines relating to data processing controls to reduce the financial exposure at these centers.

During 1976, the Board reported $151,000 spent on financial reviews. However, through the imprest fund, a $296,120 contract was awarded to conduct several other data processing center reviews. These reviews were to (1) make recommendations to improve the data center internal controls, (2) develop data center standards, (3) formulate training programs, and (4) provide third party data center reports. A Board official was designated as the contract administrator.

The decision by the Board to use the imprest fund was directly related to the issue of limiting congressional review. In an August 1975 memo, a top official rejected a suggestion to include the data center reviews as a congressional budgetary line item. The principal reason cited was to limit congressional access to information that might bring criticism to the Board.

Bank officer's pay study

The Board has stated that it is its function to conduct reviews of individual bank operations and management including the organizational structure, staffing, and salary guidelines. The Board reported to the Congress that $344,575 was spent in administrative expenses to carry out this and other bank supervisory responsibilities in 1976.

However, through the imprest fund, a $51,700 contract was awarded to a consulting firm to conduct a Bank Officer's Salary Study. The study was to determine a fair and justifiable salary range for the 12 bank presidents and their second in command. Consequently, while the Congress has had the opportunity to review other proposed bank salary guideline expenditures, this expenditure was not reported.

Establishment of a functional budgeting system

In its 1976 budget submission, the Board stated it was its responsibility to design and implement a functional budgeting system for the Federal Home Loan Bank System. The system would show budgeted versus actual income and expense by District Bank service function. The project was delegated to the Information System Division.

In this instance, the Congress was given the opportunity to review the project and its funding level. However, during 1976, an additional $14,500 was paid through the imprest fund to hire a consulting firm to plan and implement this system. This matter was not reported to the Congress.

Expenses of Federal Savings and Loan Advisory Council members

Section 8(a) of the Federal Home Loan Bank Act, as amended, created the Federal Savings and Loan Advisory Council. In addition, the Act provides that:

> "All members of the Council * * * shall be entitled to reimbursement from the Board for traveling expenses incurred in attendance at meetings of such Council."

The Board's 1976 budget to the Congress defined travel costs as including food, lodging, and transportation. The amount reported was $13,581.

However, through the imprest fund, another $14,000 was expended for food costs incurred at Advisory Council meetings. This was not reported to the Congress.

Board and FSLIC official and personal expenses

Among the funds established in the annual congressional limitation for expenses are moneys for Board employees' official business. Such expenses include transportation, food, and lodging.

The Board reported that $358,471 was spent for that purpose in fiscal year 1976. However, another $2,400 was spent through the imprest fund for food, lodging, and transportation expenses of Board employees while attending meetings.

In addition, imprest fund expenditures have been made for nonbusiness-type items. These include food and lodging costs for Board employees' wives and other miscellaneous recreation and entertainment expenses. Although relatively small in amount, these expenditures have spanned several years and have been questioned in reports by the Board's internal audit staff and an independent certified public accounting firm.

The criteria used by the Board to make imprest fund payments to Board employees for official travel expenses are not well-defined. The regulations state that disbursements may be made for expenses contained in the Board's approved budget and for such other expenses that are deemed "appropriate" by the Board. Imprest fund expenditure procedures, developed in late 1976, allow for the total payment of high-level Board employee expenditures at luncheons and dinners where these employees have an ongoing official interest in these activities. In addition, payments may also be made for Board employees' food and lodging expenses at meetings where arrangements have been made on a group basis with bank personnel. Nothing, however, is mentioned concerning the expenses of employees' wives.

In addition, the appropriateness of recreation and entertainment expenditures in connection with these activities is not addressed. No specific definitions of appropriate or prohibited expenditures are included as a part of the procedures.

In the absence of definitive Board criteria, a reasonable measure of expenditure propriety could be the Federal Travel Regulations. Among other things, these regulations govern the reimbursement of expenses incurred while conducting official Government business. Specifically, they state:

> "Traveling expenses which will be reimbursed are confined to those expenses essential to the transacting of the official business." (Underscore added.)

Our previous interpretations of these regulations have held that appropriated funds may not be used to furnish personal services to individuals.

Separate from the matter of propriety is the issue dealing with conflict of interest. There have been some benefits to Board employees financed from the imprest fund. Since the banks are paying for these benefits and the recipients are the system's regulators, it may seem that the Bank Board is not completely independent and impartial.

BOARD IS IMPROVING
IMPREST FUND CONTROLS

In late 1976, the Bank Board began to improve imprest fund controls. It now requires vouchers before invoices are paid. In addition: (a) documentation is required for all requests for Board directed expenses financed by the Banks whether proposed by the banks or by other Bank Board offices and (b) draft budgets are now sent to the 12 bank presidents before the Bank Board approves the budget.

Although these new control procedures represent an improvement, information on activities funded through the imprest fund is not submitted for congressional review.

CONCLUSIONS AND RECOMMENDATIONS

The Board's decisions on the use of the Office of Finance's imprest fund have resulted in funding activities from this fund which benefit the Board but which did not receive congressional approval as did the Boards's budget.

The Congress should require the Board to submit all imprest fund budgets to the respective appropriation committees for their consideration during the Board's budget hearings. These budgets should be incorporated with other justification information and contain line item classifications that allow for easy comparison with congressionally approved expenditures. Actual expenditures from the imprest fund should also be reported by the Board. This would allow the identification of Board items being funded through the Bank's imprest fund.

AGENCY COMMENTS

Board officials stated that the expense items we referred to are insignificant when compared to the total budget of the Office of Finance. We believe the issue is not one of significance but whether the Board is circumventing congressional oversight by paying for expenses from an imprest fund that is not reviewed by the Congress.

CHAPTER 4

ACTIVITIES OF THE FEDERAL HOME LOAN BANK BOARD

The Board establishes policies for, and supervises the operation of:

Organizations	Number	Total assets as of December 31, 1976
		(billions)
Federal home loan banks	12	$ 22.5
Federal Savings and Loan Insurance Corporation	1	4.5
Federal savings and loan associations	2,019	225.8
Insured State-chartered savings and loan institutions	2,025	157.4
Federal Home Loan Mortgage Corporation	1	4.8
Total	4,058	$415.0

SUPERVISION AND EXAMINATION OF INSURED INSTITUTIONS

The Board's supervisory objectives for insured institutions are to obtain compliance with applicable laws and regulations and to avoid the development or continuance of unsafe or unsound financial practices. Supervision is based on information obtained primarily through the Board's examinations of insured institutions and companies which have a controlling interest in them and through audits by State examiners and independent public accountants.

The Board supervises Federal savings and loan associations; building and loan, savings and loan, or homestead associations; and cooperative banks whose accounts are insured by FSLIC. It also reviews other matters of supervisory interest, such as reserve policies, potential losses, lending and loan collection policies, character of mortgage loans, earnings and expenses, and consistency of competitive practices with general standards of the savings and loan business.

In supervising State-chartered institutions, the Board coordinates these activities with respective State authorities.

As of December 31, 1976, the Board's Office of Examinations and Supervision had 771 professionals to carry out its responsibilities. This staff is assigned to 12 district offices throughout the country and to the Bank Board's headquarters in Washington, D.C.

During 1976 the Office of Examinations and Supervision examined 3,270 savings and loan institutions. The Board used the examination data to identify problem institutions discussed on pages 25 and 26. The Office also made 1,762 other examinations for such purposes as approving association mergers and insurance eligibility requirements and insuring compliance with applicable laws and regulations.

The examinations were made at intervals which averaged 14 months during 1976. This represents a slight reduction from the previous year's average of 14.1 months. The Board's goal, however, is an examination interval of every 12 months.

We analyzed and reviewed reports and related documents pertaining to institutions the Board has classified as problem and nonproblem associations. Problem associations are being recognized, the associations' problem and nonproblem classification appears reasonable, and additional supervisory attention is being given to those associations experiencing problems.

SOURCES, APPLICATIONS, AND SPENDING LIMITATIONS OF FINANCIAL RESOURCES

The Board's operations are financed through assessments levied against the banks and FSLIC and from examination fees charged to member associations. These resources are used to finance administrative operations, supervise insured institutions, and construct the new Board building. The Congress, however, limits the amount the Board can spend in a fiscal year for administrative and nonadministrative expenses. The fiscal year 1976 administrative expenses of $13,855,571 and nonadministrative expenses of $20,296,182 were within the prescribed limits.

NEW BUILDING

The Board is authorized to use the General Services Administration to construct its new $47 million quarters. Building construction began in January 1975 and is expected to be completed by August 1977. Occupancy of the building will begin in late 1977.

The building will have six floors, a ground-level plaza with retail shops, and a recreation area. In addition, there will be three levels below grade containing approximately 250 parking spaces and the Board's computer, printing, and cafeteria facilities.

CHAPTER 5

ACTIVITIES OF THE

FEDERAL HOME LOAN BANKS

The primary function of the 12 Federal home loan banks is to provide a credit reservoir for thrift and home-financing institutions. Any institution is eligible to become a Federal home loan bank member if it makes long-term home mortgage loans and meets other Board requirements. All institutions whose accounts are insured by FSLIC are members of a Federal home loan bank.

SOURCE OF FUNDS

The Federal home loan banks obtain funds for their lending activities primarily from consolidated obligations, member deposits, and capital stock.

Consolidated obligations are bonds and discount notes that are issued with the approval of the Federal Home Loan Bank Board. They are the joint and several obligations of all 12 banks.

The banks' members also provide funds through demand and time deposits. Members are not required to maintain cash balances with the banks. However, the banks' time-deposit facilities enable members with excess funds to earn interest, hold liquid assets, and place funds in the system for redistribution through member advances. A portion of member deposits may be used by the banks for making advances with the remaining deposits held in a deposit liquidity reserve.

The banks' capital stock also supplies funds for making advances to members or for obtaining other earning assets. To the extent that it is used for member advances, the capital stock outstanding redistributes funds within each bank district.

The banks can also obtain funds through the Secretary of the Treasury who has authority to purchase bank obligations up to $4 billion. The outstanding advances under this agreement were $1.2 billion at yearend. Proceeds from the purchase have been advanced to the Federal Home Loan Mortgage Corporation.

USE OF FUNDS

A major purpose of the bank system is to serve as an emergency source of liquidity for its members. The basic functions of member institutions are to receive deposits from various savers and to reinvest these funds in long-term mortgages. It is neither economically feasible nor desirable for these institutions to carry enough liquid assets to guard against contingencies, such as smoothing imbalances in savings receipts and mortgage loan disbursements. Thus, the banks provide the funds necessary to meet contingencies when liquid assets carried for this purpose are not sufficient.

The cash and investment security balances of the banks represent their operating funds and liquidity reserves. Reserves also are used to meet the members' demands for advances. The deposit liquidity reserves provide funds to members who withdraw their deposit balances at the banks. Only a small part of the banks' liquidity is maintained in the form of cash on deposit in commercial banks or with the Federal Reserve Bank of New York. The most important sources of liquidity are the investments and marketable Government obligations which also provide the banks with earning assets. Under the law the banks can only invest in obligations of the United States, the Federal National Mortgage Association, and the Government National Mortgage Association and other securities that are eligible for investment by fiduciary and trust funds.

OPERATIONS

The banks' retained earnings are placed in two accounts: undivided profits and legal reserve. Each bank must transfer semiannually 20 percent of its net earnings to the legal reserve until the account equals 100 percent of paid-in capital. Thereafter, 5 percent of its net earnings must be semiannually allocated for this purpose. The capital stock of the banks has grown so rapidly that earnings are still being allocated at the 20-percent rate. The banks also pay dividends to their members out of earnings.

Bank earnings totaled $175 million in calendar year 1976, of which $130 million was returned to members as dividends. The 12 banks' net worth continued to increase, exceeding $3.5 billion.

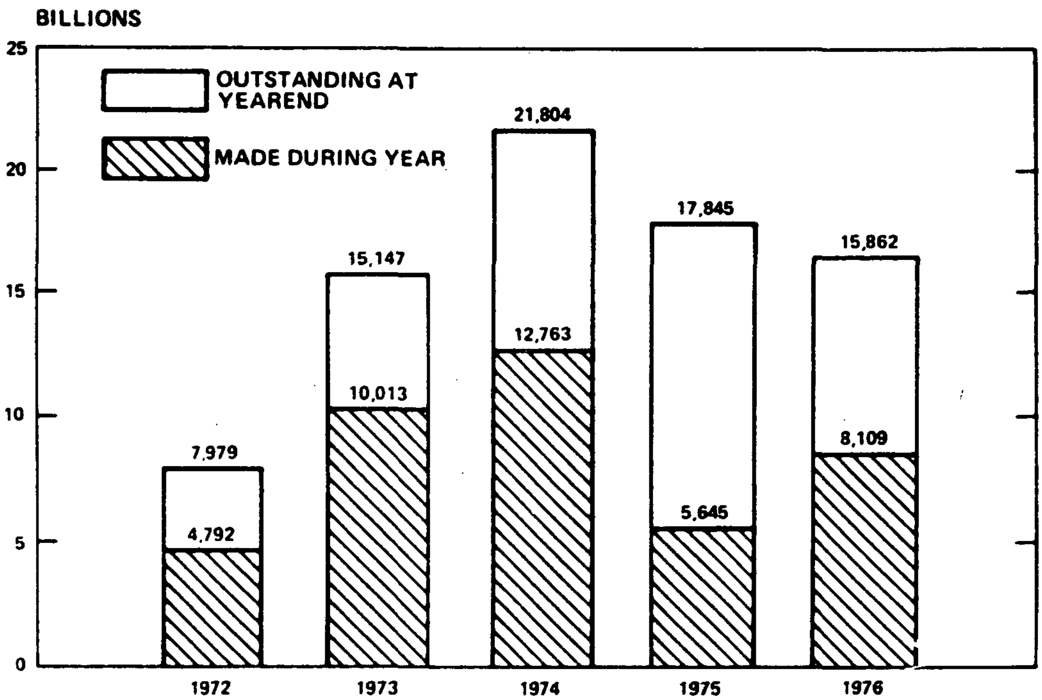
Outstanding bank advances decreased by $1.9 billion during the year from $17.8 billion to $15.9 billion. In 1975, the banks experienced a similar decrease of $4 billion.

The banks made new advances of $8.1 billion while repayments were $10.1 billion. This compares with the 1975 activity of $5.6 billion in new advances with $9.6 billion being repaid.

Of the $15.9 billion in outstanding bank advances, $14.8 billion was used as collateral by pledged investment securities, first mortgage loans, and capital stock of the banks owned by borrowing members.

The following graph gives a 5-year presentation of bank advances made each year and the outstanding yearend balances.

ADVANCES TO FEDERAL HOME LOAN BANK MEMBERS



At the end of 1976, the banks' participation in consolidated obligations stood at $14.6 billion, down $1.8 billion from the previous year's balance of $16.4 billion. The banks issued $2.8 billion in new consolidated bonds and retired $4.8 billion in maturing bonds for a net decrease in lendable funds of $2 billion.

Investments by the 12 banks in Government and commercial instruments, other than the Federal Home Loan Mortgage Corporation, stood at a record $6.1 billion on December 31, 1976, an increase of $1.7 billion over the previous year. The increase was mainly attributable to a savings influx from member associations. This also explains the decline in outstanding bank advances.

CHAPTER 6

ACTIVITIES OF THE

FEDERAL SAVINGS AND LOAN INSURANCE CORPORATION

FSLIC insures accounts of savers in federally insured institutions, assesses and collects insurance premiums, and invests surplus funds. In addition, it must be appointed receiver of defaulted Federal-chartered institutions, and it may be appointed for State-chartered institutions.

The Congress placed a limit of $1,029,000 on the amount FSLIC could spend in fiscal year 1976 and transition quarter for administrative expenses, excluding supervisory and other services provided by the Board. FSLIC's administrative expenses were within the limit.

PROBLEM INSTITUTIONS

To insure that institutions receive appropriate supervisory attention when needed, the Board's Office of Examinations and Supervision has developed procedures for rating each insured institution and for identifying those showing signs of weakness and trends which could later involve FSLIC.

The most serious cases are classified as category I, financially critical, and the next most serious cases are classified as category II, not financially critical but requiring aggressive supervisory attention. The number of problem institutions classified as categories I and II and the related estimated insured deposits are:

Category	Number of institutions		Estimated insured deposits	
	12/31/76	12/31/75	12/31/76	12/31/75
			(000 omitted)	
I	13	15	$ 658,110	$ 532,943
II	70	48	8,890,003	3,923,610
Total	83	63	$9,548,113	$4,456,553

The increase in the number of problem institutions for 1976 occurred principally because of a change in policy. Some associations, which were previously classified as non-problem, have been reclassified as problem institutions due to increased emphasis placed by the Board on identifying problem institutions as early as possible.

The estimated insured deposits in problem institutions exceed FSLIC reserves as follows:

	12/31/76	12/31/75
	(000 omitted)	
Estimated insured deposits in problem institutions	$9,548,113	$4,456,553
FSLIC secondary and primary reserves	4,480,117	4,119,622
Excess of insured deposits in problem institutions over reserves	$5,067,996	$ 336,931

The probability of all problem institutions failing in a year is remote. However, FSLIC officials do anticipate potential financial assistance to insured institutions of $21 to $24.5 million during 1977.

The reasons institutions are in the problem categories vary. They include

--unsound lending policies and practices,

--inexperienced directors and management,

--noncompliance with regulations, and

--losses incurred by an institution's service corporation.

During 1976 the Office of Examinations and Supervision took preventative actions for 11 associations which were classified as category I. All of these were merged with other associations.

INSURANCE RESPONSIBILITY ACTIVITIES

The Board and FSLIC encourage insured institutions to correct unsound operating practices before their continuance jeopardizes the financial stability of the association. However, if such practices continue, default prevention activities are initiated to prevent receivership and subsequent insurance payout.

Default prevention measures may take the form of contributions, loans, or purchase of assets to rehabilitate the association or facilitate its merger into a financially and managerially sound institution. In every case, a determination must be made that such financial assistance is less costly than liquidation.

At December 31, 1976 and 1975, FSLIC held the following assets:

Asset	Book value 12/31/76	Book value 12/31/75	Allowance for losses 12/31/76	Allowance for losses 12/31/75	Net value 12/31/76	Net value 12/31/75
	(000 omitted)					
Loans to insured institutions and accrued interest	$14,181	$ 54,503	$ -	$ 5,000	$14,181	$ 49,503
Subrogated accounts and related interest	10,680	18,945	1,500	1,500	9,180	17,445
Assets acquired from insured institutions	30,977	75,332	5,634	6,755	25,343	68,577
Total	$55,838	$148,780	$7,134	$13,255	$48,704	$135,525

The allowance for losses is based on (1) the evaluations and judgments of FSLIC officials who consider such data as actual losses experienced, (2) the latest financial data available on insured institutions in liquidation, and (3) results of independent appraisals made by contract appraisers.

Contribution agreements

One of the most frequently used default prevention methods is providing financial assistance through contribution agreement to facilitate mergers. This method indemnifies the resulting institution for certain losses arising from the assets and liabilities acquired from the problem institution.

FSLIC had 28 open contribution agreements at December 31, 1976. These agreements totaled $214.0 million with approximately $86 million having been disbursed. Of the remainder, $39.8 million has been expensed but not disbursed and FSLIC remains contingently liable for the additional $88.2 million.

Loans to insured institutions

FSLIC may make loans to financially troubled institutions to prevent their default. The loans to insured institutions and accrued interest totaled $14.2 million at December 31, 1976.

These loans consisted of $14.0 million of principal disbursements and $0.2 million in accrued interest. During 1976 no new loans were made, two were collected, and four loans remained outstanding.

Assets acquired from insured institutions

As part of the default prevention program, assets may be acquired from problem institutions. Additionally, at the termination of the receiverships, FSLIC may acquire the remaining assets as partial satisfaction for insurance payments. These assets are managed and disposed of as prudent business practices and as applicable market conditions permit.

The book value of assets acquired from insured institutions represents unpaid balances of mortgage loans at the time of acquisition, the acquisition cost of real estate and other assets, and capitalized expenditures, such as taxes and insurance, less amounts received on the principal of the loans.

Subrogated accounts

Occasionally, the circumstances of a problem association prove to be so severe that the only remedy is to declare the institution in default. This situation has occurred 13 times during FSLIC's 42 years of existence.

The institution in default is placed in the hands of a receiver and the insured account holders are paid immediately. As receiver, FSLIC proceeds to liquidate the remaining assets to recover its disbursements as well as the uninsured portions of savings accounts.

During 1976 no institutions were declared in default and placed in receivership. As of December 31, 1976, there were three active receivership cases:

Institution	Date FSLIC appointed receiver	Insured savings accounts paid by FSLIC	Liquidating dividends received by FSLIC	Balance of subrogated accounts due to FSLIC
Apollo Savings Assoc., Chicago, Illinois	Oct. 1968	$54,318,801	$47,257,161	$ 7,061,640
Old Reliable Savings and Loan Assoc., Berwyn, Illinois	Nov. 1968	7,079,061	6,795,899	283,162
Northwest Guaranty Savings and Loan Assoc., Seattle, Washington	Oct. 1971	7,755,411	4,420,584	3,334,827
		$69,153,273	$58,473,644	$10,679,629

FSLIC anticipates that all three receiverships will be terminated in 1977. Management is unable to predict collectability of interest on subrogated accounts in any of the above cases, although the statutory rate is 5 percent.

RESERVES AND BORROWING AUTHORITY

The primary and secondary reserves of FSLIC are available to protect the savings of insured account holders in insured institutions. The reserves are available to protect insured savings of about $328.2 billion in 4,044 institutions at December 31, 1976. The primary reserve represents the retained net earnings and amounted to $3.2 billion at December 31, 1976. The secondary reserve which amounted to $1.3 billion at December 31, 1976, consists of cumulative insurance premium prepayments assessed against insured institutions and a return on the outstanding balances of the secondary reserve.

Recent legislation discontinued all payments to the secondary reserve and provided for a 10-year phaseout of the reserve through partial premium charges and actual cash refunds to the industry. The cash disbursement began in May 1975 and may be of particular significance because the Board anticipates a substantial amount of these funds will be funneled into the housing market over the next few years to the benefit of the consumer and the savings and loan industry.

In our opinion, the reserves were adequate to meet potential losses that might result from problem conditions known to exist in specific insured institutions at December 31, 1976. Whether these reserves would be adequate during periods of severely adverse economic conditions is not determinable.

FSLIC may draw on three other sources for insurance purposes. The Board may require insured institutions to deposit with FSLIC up to 1 percent of their withdrawable deposits. The exercise of this authority as of December 31, 1976, would have provided funds of about $3.3 billion to FSLIC. FSLIC also may:

--Assess additional premiums against insured institutions equal to its own accumulated losses and expenses. Such assessments against an institution in any one year may not exceed one-eighth of 1 percent of the total amount of the insured members' accounts.

--Borrow up to $750 million from the Department of the Treasury.

FSLIC had not drawn on any of these sources through calendar year 1976.

CHAPTER 7

ACTIVITIES OF THE

FEDERAL HOME LOAN MORTGAGE CORPORATION

The Mortgage Corporation's principal activities consist of purchasing and reselling residential mortgages in the secondary mortgage market. The secondary mortgage market is the process by which one group of persons or companies buys mortgages from another after the mortgage has been originated.

The Corporation's principal office is in Washington, D.C., and it has five regional offices throughout the country. The Washington office is responsible for overall management of mortgage operations, research and development, and accounting policies and procedures. The regional offices are responsible for a wide range of market activities including the buying and servicing of mortgages.

The capital stock of the Corporation consists solely of nonvoting common stock held by the 12 Federal home loan banks. One hundred thousand shares have been issued for a total purchase price of $100 million. The Corporation may declare dividends on its common stock but has not yet done so. The stock may also be retired at its issue price if such retirement will not reduce the Corporation's reserves to less than $100 million.

PURCHASING ACTIVITIES

Mortgages may be purchased from the Federal home loan banks and member institutions, FSLIC, and certain other financial institutions whose deposits or accounts are insured by an agency of the United States or are insured under State law. Mortgage purchases amounted to $1.1 billion in 1976, net of discount.

The Corporation is operating six conventional purchase programs that account for 98 percent of its mortgage investment activity. Under its two whole-loan programs, the Corporation purchases single-family and multifamily conventional loans for delivery within 60 days. The whole-loan conventional mortgages amounted to $676 million at December 31, 1976, a decrease of about $38 million from the previous year's balance.

Under the three participation programs the Corporation purchases up to 95 percent ownership in conventional mortgage loans. Under these programs, the seller retains a percentage ownership and is responsible for collecting the monthly payments and remitting to the Corporation its share. The seller profits from the difference between the mortgage's interest rate and the rate at which he sells the participation. In addition, the seller receives the full amount of interest on the unsold percentage.

The Corporation's balance of participations was $809 million at December 31, 1976. This represented a decrease of $35 million from last year.

The Corporation also enters into contractual agreements (commitments) to purchase mortgages from financial institutions to be delivered within an agreed-upon time. The commitments provide insurance to the mortgage lenders and home builders that, regardless of market changes, mortgage money will be available at the interest rate and in the amount committed. A new Six-Month Forward Commitment Program was initiated for single-family conventional mortgages during 1976. This program involves the purchase and sale of future mortgages at fixed interest rates.

Delivery of mortgages under the Six-Month Forward Commitment Program is at the option of the seller; delivery is mandatory under all other commitment programs and must occur within 60 days of the contract date. These mortgages have to meet the same basic requirements as established for the purchase programs. The requirements specify quality standards and certain legal restrictions such as the loan amount, term of the mortgage, and standardized documentation. At December 31, 1976, outstanding commitments were $333 million, compared with $110 million a year earlier.

In addition, the Corporation purchases and/or enters into purchase commitments for Federal Housing Administration's and Veterans Administration's mortgages. The majority of these mortgages are pledged to a trust serving as collateral for Government National Mortgage Association's guaranteed bonds issued by the Corporation. A Corporation official stated that the guarantee was needed when the Corporation was a newly created entity and was unable to secure financing at favorable rates on its own reputation. The principal balances of the pledged mortgages and other trust assets are restricted to the payment of the bond's principal and interest.

As of December 31, 1976, the balance of these two mortgage holdings, net of participation sales, was about $1,672 billion, which represented a decrease of $205 million from the previous year.

SERVICING MORTGAGES

When the Corporation acquires mortgages or interests in mortgages, the seller is required, for a fee, to continue servicing the mortgages (collecting and remitting funds from the borrower). The servicer's responsibility is to act in a timely, efficient, and responsible manner to protect the Corporation's interest and to afford proper service and fair treatment to the borrower. It is expected that the facilities and practices of the servicer will be sufficient to safeguard the assets, to provide proper accounting, and respond promptly to the Corporation's needs and those of the borrower.

In 1975 the Corporation entered into a program with the Government National Mortgage Association whereby the Corporation acts as the purchasing agent and receives a management and processing fee for servicing a number of these loans. The loans being serviced during 1976 amounted to $176 million.

MARKETING ACTIVITIES

In 1976, the Corporation financed the purchase of mortgages primarily through the sale of Mortgage Participation Certificates and the sale of Guaranteed Mortgage Certificates. During 1976 about 59 percent of the Corporation's financial resources came from these activities. Additional funds came from the repayment of mortgage principal and reduction in temporary investment.

The Corporation sells Mortgage Participation Certificates in its conventional participation and whole loan programs. The first sale occurred in 1971. During 1976 investors purchased $1.5 billion in certificates that were sold in multiples of $100,000.

The market for these certificates has developed faster than the Corporation had anticipated. Sales in 1977 have reached $2 billion as of June. This accelerated growth is due, in part, to (1) the development of a network of dealers to act as the Corporation's agent in the sale of mortgage instruments and (2) the activity of the dealer network in creating a secondary market for mortgage instruments.

Investment in Mortgage Participation Certificates is advantageous to members of the Federal Home Loan Bank System because the certificates are transferable and meet the definition of real property loans for tax and regulatory purposes.

During 1976 the Corporation issued two series of Guaranteed Mortgage Certificates for a total of $400 million. These were sold in denominations of $100,000, $500,000, and $1 million. The certificates do not qualify as a mortgage investment for most regulatory purposes and were sold to nontraditional residential mortgage investors, resulting in an inflow of capital for the home loan industry.

Other forms of financing include the direct sale of mortgage holdings ($35 million in 1976), the issuance of Guaranteed Mortgage-Backed Bonds and borrowings from the Federal home loan banks and commercial banks.

SPECIAL U.S. TREASURY FUNDED PROGRAM

In 1974 the U.S. Treasury and Federal Home Loan Bank Board entered into an agreement to provide the Corporation with a $3 billion line of credit. Under this program the Corporation obtained Treasury advances at below-market interest rates to purchase conventional mortgages. The agreement terms require the Corporation to make semiannual payments on the loans in amounts at least equal to the principal collections on the related mortgages pledged as collateral. During 1976 the Corporation retired $387.5 million of this debt.

The interest on borrowings and related costs reported by the Corporation includes interest charges on a significant part of the borrowings from the U.S. Treasury. Had the Corporation financed these borrowings through the issuance of Mortgage Participation Certificates, their interest and related costs would have increased by approximately $6.8 million in calendar year 1976. However, Corporation officials indicated that they would not have purchased the related mortgages without the financing made available through the Treasury program. The benefit of lower borrowing costs was passed on to mortgage borrowers in terms of lower interest rates.

The Corporation has since retired the outstanding $1.2 billion Treasury debt. In accordance with the agreement, $700 million of new debt (Federal Home Loan Bank Consolidated Obligations and Guaranteed Mortgage Certificates) was issued in January and February 1977 to finance an equal amount paid back to the Treasury. In addition, approximately $500 million in Participation Certificates was sold to retire the additional amount of Treasury debt.

CHAPTER 8

SCOPE OF EXAMINATION AND

OPINION ON FINANCIAL STATEMENTS

We have examined the statements of financial condition of the Federal Home Loan Bank Board, the Federal home loan banks, the Federal Savings and Loan Insurance Corporation, and the Federal Home Loan Mortgage Corporation as of December 31, 1976, and their related statements of income, expense, and retained earnings of primary reserve and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards and included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances. We previously made a similar examination of the financial statements for the year ended December 31, 1975.

We used, to the extent possible, the work of the Board's internal auditors on their examination of the Board and the Insurance Corporation and the work of public accounting firms on their audits of the banks and Mortgage Corporation.

In our opinion, the accompanying financial statements (scheds. 1 through 13) present fairly the financial positions of the Board, banks, and Insurance and Mortgage Corporation at December 31, 1976 and 1975, and the results of their operations and the changes in their financial positions for the years then ended, in conformity with principles and standards of accounting prescribed by the Comptroller General of the United States.

FEDERAL HOME LOAN BANK BOARD

FINANCIAL STATEMENTS

DECEMBER 31, 1976 AND 1975

SCHEDULE 1

FEDERAL HOME LOAN BANK BOARD

COMPARATIVE STATEMENT OF FINANCIAL CONDITION

AT DECEMBER 31, 1976 AND 1975

ASSETS	1976	1975
Cash with U.S. Treasury (note 2)	$ 857,641	$ 1,199,460
Accounts receivable	7,898,158	5,718,778
Land and building (note 3)	31,762,893	16,362,994
Furniture, fixtures and equipment, net (note 1)	1,212,291	1,554,055
Other	-	57,938
Total assets	$41,730,983	$24,893,225
LIABILITIES AND CAPITAL		
Accounts payable and accrued liabilities	$ 2,378,283	$ 1,739,043
Employees' accrued annual leave	1,988,732	1,906,351
Deferred credit--FHLBB cost of quarters (note 4)	31,294,280	16,229,680
Total liabilities	35,661,295	19,875,074
Capital, retained earnings	6,069,688	5,018,151
Total liabilities and capital	$41,730,983	$24,893,225

The accompanying notes to financial statements are an integral part of these statements.

 SCHEDULE 2

FEDERAL HOME LOAN BANK BOARD

COMPARATIVE STATEMENT OF INCOME, EXPENSES,

AND RETAINED EARNINGS

FOR THE YEARS ENDED DECEMBER 31, 1976 AND 1975

	1976	1975
INCOME:		
Fees from examinations of savings and loan institutions	$14,156,860	$13,740,828
Assessments:		
Federal home loan banks	6,871,809	6,425,716
Federal Savings and Loan Insurance Corporation	17,563,353	14,044,946
Reimbursements for services performed	224,839	187,648
Miscellaneous	187,213	91,454
Total income	39,004,074	34,490,592
EXPENSES:		
Personnel compensation	25,337,172	23,785,701
Personnel benefits	2,620,538	2,345,872
Travel and transportation	4,506,631	4,031,588
Rent, communication, and utilities	2,542,908	2,494,318
Depreciation of furniture, fixtures, and equipment	559,688	159,067
Other services	1,716,845	1,189,685
Printing and reproduction	215,759	108,952
Supplies and materials	452,996	389,537
Total expenses	37,952,537	34,504,720
NET INCOME (loss)	1,051,537	(14,128)
RETAINED EARNINGS AT BEGINNING OF YEAR	5,018,151	5,032,279
RETAINED EARNINGS AT END OF YEAR	$ 6,069,688	$ 5,018,151

The accompanying notes to financial statements are an integral part of these statements.

SCHEDULE 3

FEDERAL HOME LOAN BANK BOARD
COMPARATIVE STATEMENT OF CHANGES IN FINANCIAL POSITION
FOR THE YEARS ENDED DECEMBER 31, 1976 AND 1975

	1976	1975
FINANCIAL RESOURCES WERE PROVIDED FROM:		
Operations-Income		
Examination fees and charges	$14,156,860	$13,740,828
Assessments		
Federal home loan banks	6,871,809	6,425,716
Federal Savings and Loan Insurance Corporation	17,563,353	14,044,946
Reimbursements for services performed to other agencies	224,839	187,648
Miscellaneous	187,213	91,454
	39,004,074	34,490,592
Less--Expense		
Personnel compensation and benefits	27,957,710	26,131,573
Travel and transportation	4,506,631	4,031,588
Rent, communication, and utilities	2,542,908	2,494,318
Other services (excluding amortization of leasehold improvements totaling $55,921 and $96,938 in 1976 and 1975	1,660,924	1,092,747
Printing and reproduction	215,759	108,952
Supplies and materials	452,996	389,537
	37,336,928	34,248,715
Total resources provided by operations	1,667,146	241,877
Increase in:		
Deferred credit--FHLBB cost of quarters	15,064,600	6,040,000
Employees' accrued annual leave	82,381	60,210
Decrease (increase) in:		
Furniture, fixtures, and equipment	(217,924)	141,733
Accounts receivable	(2,179,380)	932,156
Other assets	2,017	55,163
Total resources provided	$14,418,840	$ 7,471,139
FINANCIAL RESOURCES WERE APPLIED TO:		
Acquisition of land and building	$15,399,899	$ 5,173,950
Increase in cash (decrease)	(341,819)	607,893
Decrease (increase) in accounts payable and accrued liabilities	(639,240)	1,689,296
Total resources applied	$14,418,840	$ 7,471,139

The accompanying notes to financial statements are an integral part of these statements.

FEDERAL HOME LOAN BANK BOARD
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 1976 AND 1975

1. Furniture, fixtures, and equipment are stated at cost less accumulated depreciation of $1,048,229 and $1,121,829 at December 31, 1976 and 1975, respectively. Depreciation is computed on the straight-line method over the estimated useful lives of the property.

2. An additional $2,451,579 is available in a separate fund provided by appropriations pursuant to the provisions of the Emergency Home Finance Act of 1970. Use of such funds is for the purpose of adjusting the effective interest charged by the Federal home loan banks on short- and long-term borrowing in order to promote an orderly flow of funds into residential construction.

3. Includes about $3.1 million which is the book value of the remaining portion of the original site for the new building.

4. In 1974 the Board assessed the Federal home loan banks $40 million for the total estimated cost to construct the new Federal Home Loan Bank Board building. As of December 31, 1976, $31,294,280 had been paid by the banks and recorded as Deferred Credit--FHLBB cost of quarters. When the Board occupies the building, this credit will be systematically amortized to income over 25 years.

FEDERAL HOME LOAN BANKS

FINANCIAL STATEMENTS

DECEMBER 31, 1976 AND 1975

SCHEDULE 4

FEDERAL HOME LOAN BANKS

COMBINED STATEMENT OF FINANCIAL CONDITION

AT DECEMBER 31, 1976, AND DECEMBER 31, 1975

ASSETS	1976	1975
	(000 omitted)	
Cash (note 2)	$ 164,443	$ 109,095
Investments, at cost (note 3)	6,078,814	4,375,742
Advances to members (note 4)	15,862,032	17,844,626
Other loans		
Guaranteed by AID, net (note 5)	56,893	80,392
Other FHLBs	68,025	50,575
Total other loans	124,918	130,967
Accrued interest receivable	84,329	97,144
Bank premises and equipment	24,028	22,572
Less: accumulated depreciation and amortization	(8,172)	(7,995)
Net book value	15,856	14,577
Other assets		
Investment in FHLMC (note 6)	100,000	100,000
Concessions and discount on consolidated obligations--bonds	16,242	17,418
Deferred charges--FHLBB cost of quarters (note 12)	31,320	16,231
Other	2,807	2,657
Total other assets	150,369	136,306
Total assets	$22,480,761	$22,708,457

The accompanying notes to financial statements are an integral part of these statements.

SCHEDULE 4

LIABILITIES AND CAPITAL

	1976	1975
Deposits and borrowings		
Members--time	$ 3,149,704	$ 2,024,015
Members--demand	716,887	626,652
Other FHLBs	68,025	50,575
Other borrowings (note 15)	90,000	
Total deposits and borrowings	4,024,616	2,701,242
Accrued interest payable	265,827	292,118
Consolidated obligations (note 7)		
Bonds	16,488,915	18,520,600
Discount notes	321,100	342,331
Less pass throughs to FHLMC	(2,190,000)	(2,480,000)
FHLBs' participations	14,620,015	16,382,931
Other liabilities		
Accounts payable	8,311	4,618
Accounts payable--FHLBB assessment	1,753	-
Other	36,772	32,741
Total other liabilities	46,836	37,359
Total liabilities	18,957,294	19,413,650
Contingencies and commitments (notes 8, 11, 12, 13, and 14)		
CAPITAL		
Capital stock outstanding (note 9)	2,888,613	2,704,625
Retained earnings		
Legal reserve	377,333	342,426
Undivided profits	257,521	247,756
Total retained earnings	634,854	590,182
Total capital	3,523,467	3,294,807
Total liabilities and capital	$22,480,761	$22,708,457

SCHEDULE 5

FEDERAL HOME LOAN BANKS

COMBINED STATEMENT OF INCOME AND EXPENSE

FOR THE YEARS ENDED DECEMBER 31, 1976 AND 1975

	1976	1975
	(000 omitted)	
INCOME:		
Interest on advances to members	$1,238,156	$1,445,542
Income from investments	332,864	338,816
Interest and fees on AID loans (note 5)	5,557	6,616
Earned commitment fees	4,729	4,498
Income from data processing services	12,358	10,032
Other income	5,614	5,041
Total income	1,599,278	1,810,545
EXPENSES:		
Interest and other costs:		
Interest and concessions--consolidated obligations	1,227,605	1,433,471
Assessments--FHLBB	6,872	6,633
Assessments--Office of Finance	1,988	1,601
Interest on deposits	140,884	136,890
Other interest	1,966	1,909
Total interest and other costs	1,379,315	1,580,504
Other operating expenses:		
Salaries and benefits (note 10)	23,523	21,489
Fees and professional services	1,432	1,337
Travel expense	1,532	1,368
Telephone and transmissions costs	2,719	2,560
Stationery and supplies	4,321	3,349
Cost of quarters	3,696	3,651
Depreciation--furniture and equipment	1,239	1,332
Equipment rental and expense	5,514	4,210
Other	1,459	1,711
Total other operating expenses	45,435	41,007
Total expenses	1,424,750	1,621,511
Net income	$ 174,528	$ 189,034

The accompanying notes to financial statements are an integral part of these statements.

SCHEDULE 6

SCHEDULE 6

FEDERAL HOME LOAN BANKS

COMBINED STATEMENT OF RETAINED EARNINGS

FOR THE YEARS ENDED DECEMBER 31, 1976 AND 1975

	1976	1975
	(000 omitted)	
LEGAL RESERVES:		
Balance, January 1	$342,425	$304,619
Add: Statutory transfer of net income	34,908	37,807
Balance, December 31	377,333	342,426
UNDIVIDED PROFITS:		
Balance, January 1	247,755	234,413
Add: Net income	174,529	189,034
Subtotal	422,284	423,447
Deductions:		
Statutory transfer of net income	34,908	37,806
Dividends paid on capital stock	129,855	137,885
Total deductions	164,763	175,691
Balance, December 31	$257,521	$247,756
TOTAL RETAINED EARNINGS	$634,854	$590,182

Note: Because of rounding, minor differences may occur in some totals.

The accompanying notes to financial statements are an integral part of these statements.

SCHEDULE 7

FEDERAL HOME LOAN BANKS

COMBINED STATEMENT OF CHANGES IN FINANCIAL POSITION

FOR THE YEARS ENDED DECEMBER 31, 1976 AND 1975

	1976	1975
	(000 omitted)	
FINANCIAL RESOURCES WERE PROVIDED FROM:		
OPERATIONS:		
Net income	$ 174,529	$ 189,033
Noncash charges/(credit) to income:		
Depreciation and amortization of fixed assets	1,864	2,132
Amortization of concessions on consolidated obligations	7,150	9,406
Amortization of discount consolidated obligation notes	16,297	22,503
Other	(148)	(151)
Total funds provided from operations	199,692	222,923
Net proceeds from issuance of consolidated obligations	5,724,340	4,311,229
Advances repaid	10,091,244	9,604,571
Proceeds from sale of capital stock	281,434	201,829
Increase (decrease) in deposits	1,305,923	256,992
Increase (decrease) in accrued interest payable	(26,301)	(67,885)
Increase (decrease) in other liabilities	9,644	(5,963)
Total	$17,585,976	$14,523,696
FINANCIAL RESOURCES WERE USED FOR:		
Payments on maturing consolidated obligations	7,509,585	7,400,785
Advances made	8,108,650	5,64[illegible],735
Redemption of capital stock	97,446	121,512
Dividends on capital stock	129,858	137,885
Net additions to bank premises and equipment	3,144	1,044
Increase (decrease) in investments	1,703,072	1,278,326
Increase (decrease) in accrued interest receivable	(12,816)	(27,680)
Increase (decrease) in other assets	(8,313)	2,385
Increase (decrease) in cash	55,350	(35,296)
Total	$17,585,976	$14,523,696

The accompanying notes to financial statements are an integral part of these statements.

FEDERAL HOME LOAN BANKS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 1976 AND 1975

1. Summary of significant accounting policies

The more significant accounting policies not described elsewhere in the notes to the financial statements are as follows:

(a) Investments--Investment securities are stated at cost, adjusted for amortization of premiums and accretion of discounts.

(b) Advances to Federal Home Loan Mortgage Corporation--Proceeds from certain consolidated obligations and the promissory note payable to the U.S. Treasury have been advanced to the Federal Home Loan Mortgage Corporation at the same interest rates and maturities as the related consolidated obligations and the promissory note. Since the Federal Home Loan Mortgage Corporation is effectively reimbursing the Banks for the interest, the advance, related consolidated obligations, interest expense, and interest income have been offset and are not reflected in the financial statements.

(c) Bank premises, furniture and equipment, and leasehold improvements--These assets are stated at cost less accumulated depreciation and amortization. Depreciation and amortization are computed on the straight-line method over the estimated useful lives of the property or life of the lease. Maintenance and repairs are charged to expense, except that major repairs which extend the useful lives of the property are capitalized. The cost, less accumulated depreciation of assets sold or retired, is eliminated from the accounts in the year of disposal; the related gain or loss is included in the statement of income.

(d) Concessions on consolidated obligations--The amounts allowed dealers in connection with the sale of consolidated obligation bonds are deferred and amortized on the straight-line method to the maturity of the obligations. The amounts applicable to the sale of consolidated obligation discount notes are charged directly to expense as incurred.

(e) Unearned commitment fees--Advance commitment fees are received at the time the agreement is made. Nonrefundable fees of less than $1,000 are taken into income immediately and fees of $1,000 or more are amortized to income over the period of the commitment on a straight-line basis. Refundable fees are deferred until the commitment expires or the loan is funded.

(f) Reclassification--Certain reclassifications have been made in 1975 financial statements to conform to the classification used in 1976.

2. Compensating balances--The banks have agreed to maintain average collected cash balances with various commercial banks in consideration for various services. These arrangements are informal and there are no legal restrictions as to the withdrawal of funds. The required compensating balances were approximately $39,002,000 at December 31, 1976.

3. Investments--The investments at December 31, 1976, were as follows:

	Carrying value	Market value
U.S. Treasury obligations	$2,811,506,000	$2,817,246,000
U.S. Government agencies	64,742,000	64,868,000
Federal funds sold	547,800,000	547,800,000
Term funds sold	175,000,000	175,000,000
Bankers acceptances	1,121,824,000	1,121,918,000
Securities held under resale agreement	67,500,000	67,500,000
Participation in the Federal Home Loan Banks' Consolidated Securities Fund	1,290,442,000	1,290,549,000
Total	$6,078,814,000	$6,084,881,000

The Federal home loan banks Consolidated Securities Fund was established by the Federal Home Loan Bank Board to offer a centralized portfolio management system for securities of the Federal home loan banks. The Fund is managed by the Office of Finance of the Federal home loan banks. The Fund invests primarily in short-term money market instruments.

4. Advances to members--At December 31, 1976, the banks have advances outstanding to members at interest rates ranging from 5.25 to 9.50 percent, maturing at various dates, as summarized below:

Years of maturity	Amount	Weighted average interest rate (percent)
1977	$ 4,130,069,000	7.14
1978	3,408,939,000	7.58
1979	4,574,286,000	7.97
1980	1,471,451,000	7.69
1981	953,283,000	7.73
1982-1986	1,324,004,000	7.81
	$15,862,032,000	7.62

Outstanding advances aggregating $14,754,182,000 are collateralized by pledged investment securities and first mortgage loans of the members having a loan value assigned by the banks of approximately $22,696,351,000.

The capital stock of the Federal home loan banks owned by borrowing members is pledged as additional collateral for any outstanding advances.

The banks are participating in a below-market interest rate advance program initiated in May 1974 to support the housing industry. Advances of $3,479,977,000 were made under this program for a period of approximately 5 years at rates of 0.5 to 0.79 percent below the FHLB system's cost of related 5-year consolidated obligations. The net interest cost of this program amounts to approximately $18,164,000 and $18,921,000 for 1976 and 1975, respectively. The advances may be prepaid without penalty, but only by tendering the related consolidated obligations sold to support this program. Remaining advances outstanding under this program at December 31, 1976, totaled $3,365,204,000.

5. Loans guaranteed by the Agency for International Development

The Agency for International Development (AID) was established by the Foreign Assistance Act of 1961, as amended. Under section 221 and 222 of the act, AID issues guarantees backed by the full faith and credit of the United States of America to eligible U.S. investors insuring against loss of investments, including unpaid accrued interest, in self-liquidating housing projects. The banks qualify as eligible investors.

Under contracts of guaranty the banks may, without the approval of AID, sell participating interests to members of any Federal home loan bank. The outstanding loan balances are reported net of participations totaling $305,635,000 and $192,326,000 at December 31, 1976 and 1975, respectively.

The outstanding loan balances bear interest at rates ranging from 7.25 to 9.25 percent and mature between 1989 and 2007. The weighted average interest rate on AID loans outstanding at December 31, 1976, is 8.33 percent.

The banks receive service fees for these loans against which direct expenses associated with the financing arrangements are netted. The balance is deferred and amortized into income at 1 percent per month.

6. Investment in Federal Home Loan Mortgage Corporation

The investment in the Federal Home Loan Mortgage Corporation which is wholly owned by the Federal home loan banks, is stated at cost and consists of 100,000 shares of nonvoting capital stock, all of which is outstanding. These shares had an underlying book value of approximately $156,000,000 and $141,815,000 at December 31, 1976 and 1975, respectively.

7. Consolidated obligations

Consolidated Federal home loan bank obligations are the joint and several obligations of all Federal home loan banks. The outstanding obligations of the Federal home loan banks, including the pass-through to the Federal Home Loan Mortgage Corporation at December 31, 1976 and 1975, were $16,810,915,000 and $18,864,800,000. (GAO note: For purposes of this footnote, the Bank Board used the par value of the discount notes in its calculation of total consolidated obligations as of Dec. 31, 1976, and Dec. 31, 1975. On the balance sheet, discount notes are stated at book value.)

Regulations require the banks to maintain unpledged qualifying assets in an amount equal to the consolidated obligations outstanding. Qualifying assets are defined as cash, obligations of or fully guaranteed by the United States, secured advances, and federally insured or guaranteed mortgages. The system is in compliance with this requirement.

The following is a summary of the banks' participation in consolidated obligations at December 31, 1976:

Years of maturity	Bonds: Range of coupon rates	Bonds: Outstanding
1977	6.75-9.15	$ 3,396,050,000
1978	7.25-9.375	1,889,910,000
1979	8.15-9.50	3,392,255,000
1980	6.70-7.80	2,650,000,000
1981	6.60-7.60	700,000,000
1982-1986	7.30-8.625	2,270,700,000
1987 or after	-	-
		$14,298,915,000

Year of maturity	Discount notes: Book value	Discount notes: Par value
1977	$321,100,000	$322,000,000

The banks' participation, as shown above, is reported net of advances to the Federal Home Loan Mortgage Corporation in the form of passthrough of the proceeds of certain Consolidated Obligations. The following is a summary of the passthrough at December 31, 1976:

Years of maturity	Bonds: Range of coupon rates	Bonds: Outstanding
1977	6.95-8.70	$ 500,000,000
1978	9.375	300,000,000
1979	9.45	100,000,000
1980	-	-
1981	8.65	400,000,000
1982-1986	8.625-8.75	490,000,000
1987 or after	7.375	400,000,000
		$2,190,000,000

8. Promissory note payable to U.S. Treasury

Section 11(i) of the Federal Home Loan Bank Act authorizes the Secretary of the Treasury to extend credit to the Federal home loan banks aggregating not more than $4,000,000,000. Pursuant to this section, the Federal Home Loan Bank of San Francisco and the U.S. Treasury entered into an agreement in August 1974, whereby funds in an aggregate amount not to exceed $3,000,000,000 may be advanced to the San Francisco Bank. The San Francisco Bank agreed to relend these funds to the Federal Home Loan Mortgage Corporation as secured advances to finance a Special Commitment Program for the purchase of certain home mortgages. The Federal Home Loan Mortgage Corporation's note to the San Francisco Bank has been assigned to the Secretary of the Treasury as collateral for the Bank's promissory note.

Semiannual principal repayments together with interest at rates of 8.375 and 7.875 percent on the unpaid principal balance, began January 1, 1975, and continue each subsequent July 1 and January 1, with the final payment due on January 1, 2006.

The promissory note to the U.S. Treasury is the joint and several obligation of all Federal home loan banks. The outstanding advances were $1,171,741,000 and $1,559,194,000 at December 31, 1976 and 1975. Proceeds from the note have been advanced to the Federal Home Loan Mortgage Corporation at the same interest rates as the note payable to the U.S. Treasury.

The note was repaid by the Federal Home Loan Mortgage Corporation on February 25, 1977.

9. Capital

The capital stock of the banks has a par value of $100 per share and may not be issued at a price less than par value. The stock is nonnegotiable and can be redeemed only at the banks, within legal limits.

Dividends are paid to members annually on the capital stock issued and outstanding at December 31, based on the actual period of time that stock is held during the year.

Retained earnings of the banks consist of undivided profits and a legal reserve. The banks must transfer 20 percent of their net income to the legal reserve semiannually until the reserve equals the capital stock amount. Thereafter, 5 percent of the banks' net income must be allocated for this purpose.

10. Employee retirement plan

The banks are participants in the Savings Association Retirement Fund and substantially all of their officers and employees are covered by the plan. The banks' contributions are determined by the Fund and represent the normal cost and prior service cost. Pension costs charged to operating expenses were $2,797,000 in 1976 and $2,905,000 in 1975.

11. Lease commitments

Rental expense of $4,718,000 in 1976 and $4,534,000 in 1975 for premises and equipment has been charged to expense. Minimum rentals for each of the next 5 years and for subsequent 5-year periods are as follows:

1977	$ 4,789,000
1978	4,033,000
1979	3,949,000
1980	3,285,000
1981	2,531,000
1982 to 1986	8,515,000
1987 and after	2,877,000
	$29,979,000

The banks' premise lease agreements provide for increases in basic rentals resulting from increased property taxes and maintenance expense.

12. Deferred charges--FHLBB cost of quarters

In December 1974, the FHLBB assessed the banks $40,000,000 for the total estimated cost of constructing an office building in Washington, D.C. The FHLBB will request payment of the remaining $8,680,000 at such times and in such amounts as deemed necessary to meet anticipated construction expenditures.

When the FHLBB takes occupancy of the new building, this deferred charge will be systematically amortized over 25 years.

13. Commitments

Commitments for advances to members and to foreign borrowers under guaranteed loans totaled $396,143,000 and 30,954,000, respectively, at December 31, 1976.

14. Contingency

On October 25, 1973, a lawsuit was instituted against the Federal Home Loan Bank of Cincinnati, the Federal Home Loan Bank Board, and certain Board members. Among other things, the plaintiffs alleged in their complaint that the on-line data processing services provided by the Federal Home

Loan Bank of Cincinnati to thrift institutions were beyond the statutory authority of the bank and that the Board could not properly authorize the bank to provide such services. The Federal Home Loan Banks of Chicago, Des Moines, New York, and Pittsburgh, which provided similar services, intervened in this lawsuit in April 1974 on the side of the Federal Home Loan Bank of Cincinnati.

The district court rendered a decision on September 27, 1976, holding, in essence, that the Board lacked the statutory authority to authorize any of the Federal home loan banks to provide on-line data processing services and that the banks were to be permanently enjoined effective January 1, 1977, from providing such services. The Board and banks appealed the decision and the district court subsequently issued an order staying the injunction previously entered pending disposition of the appeal to the United States Court of Appeals for the sixth circuit.

While the outcome of this litigation cannot be predicted with certainty, counsel and management are of the opinion that the Board and banks have meritorious defenses to the challenge to their authority to provide on-line data processing services to member institutions and intend to defend their position vigorously.

15. Loan from Consolidated Securities Fund

The San Francisco Bank borrowed $60,000,000 from the Consolidated Security Fund on an unsecured basis at a rate of 4.625 percent to adjust its cash position on December 31, 1976. The funds were repaid to the Consolidated Securities Fund on January 3, 1977. The remaining $30,000,000 classified as other borrowings, represents a deposit made by the Federal Home Loan Mortgage Corporation at the Federal Home Loan Bank of Topeka.

FEDERAL SAVINGS AND LOAN INSURANCE COPORATION

FINANCIAL STATEMENTS

DECEMABER 31, 1976 AND 1975

SCHEDULE 8

FEDERAL SAVINGS AND LOAN INSURANCE CORPORATION

COMPARATIVE STATEMENT OF FINANCIAL CONDITION

AT DECEMBER 31, 1976 AND 1975

ASSETS	1976	1975
Cash	$ 262,979	$ 281,755
Receivables	8,339,869	10,522,711
Investments at amortized cost (note 2)	4,397,749,298	3,956,452,821
Accrued interest on investments	75,054,064	68,623,955
Assets acquired from insured institutions, net (note 3)	25,343,273	68,576,833
Loans to insured institutions and accrued interest, net (note 3)	14,180,954	49,503,381
Subrogated accounts and related interest, net (note 3)	9,179,630	17,444,749
Deferred charges and other assets	111,757	158,865
Total assets	$4,530,221,824	$4,171,565,070
LIABILITIES AND RESERVES		
Miscellaneous accrued and other liabilities	$ 9,007,373	$ 6,546,181
Allowance for estimated losses for contribution agreements (notes 3 and 4)	39,770,790	43,875,788
Deferred credits	1,326,237	1,520,742
Primary reserve (cumulative net income)	3,167,235,938	2,740,246,914
Secondary reserve (premium prepayments)	1,312,881,486	1,379,375,445
Total liabilities and reserves	$4,530,221,824	$4,171,565,070

The accompanying notes to financial statements are an integral part of these statements.

SCHEDULE 9

FEDERAL SAVINGS AND LOAN INSURANCE CORPORATION

COMPARATIVE STATEMENT OF INCOME, EXPENSE, AND PRIMARY RESERVE

FOR THE YEARS ENDED DECEMBER 31, 1976 AND 1975

	1976	1975
INCOME:		
Insurance premiums	$ 250,466,642	$ 212,250,148
Interest on investments	289,441,595	260,388,096
Interest on loans to insured institutions	1,987,464	3,431,804
Interest on subrogated accounts	-	19,193,069
Income on assets acquired from insured institutions	4,548,022	5,046,658
Interest income on advance contributions	326,495	84,247
Miscellaneous income	317,506	503,838
Nonoperating income	2,064,916	233,020
Total income	549,152,640	501,130,880
EXPENSES:		
Administrative expenses	729,192	713,896
Services rendered by Federal Home Loan Bank Board	17,563,354	14,044,946
Insurance settlement and other expenses	1,608,631	2,265,438
Unallocated nonadministrative expenses	1,136,371	1,010,345
Net provision for losses (note 3)	11,070,842	31,986,064
Interest applied to members' equity in secondary reserve	90,055,226	92,736,817
Total expenses	122,163,616	142,757,506
Net income transferred to primary reserve	426,989,024	358,373,374
BALANCE, PRIMARY RESERVE, AT THE BEGINNING OF THE YEAR	2,740,246,914	2,381,873,540
BALANCE, PRIMARY RESERVE, AT THE END OF THE YEAR	$3,167,235,938	$2,740,246,914

The accompanying notes to financial statements are an integral part of these statements.

SCHEDULE 10

FEDERAL SAVINGS AND LOAN INSURANCE CORPORATION

COMPARATIVE STATEMENT OF CHANGES IN FINANCIAL CONDITION

FOR THE YEARS ENDED DECEMBER 31, 1976 AND 1975

	1976	1975
FINANCIAL RESOURCES WERE PROVIDED FROM:		
Operations:		
Insurance premiums (other than transfer from Secondary Reserve to pay insurance premiums of $73,915,543 and $62,854,065 in 1976 and 1975)	$176,551,099	$149,395,183
Interest on investments (net of $23,156,838 and $7,227,485 in amortized net discount for 1976 and 1975)	266,284,757	253,160,611
Interest on loans in insured institutions	1,987,464	3,431,804
Interest on subrogated accounts	-	19,193,069
Income on assets acquired from insured institutions	4,548,022	5,046,658
Other income	2,708,916	821,105
	452,080,258	431,048,430
Less:		
Administrative expenses	729,192	713,896
Services rendered by the FHLBB	17,563,354	14,044,946
Insurance settlement and other expenses	1,608,631	2,265,438
Unallocated nonadministrative expenses	1,136,371	1,010,345
	21,037,548	18,034,625
Total resources provided by operations	431,042,710	413,013,805
Decrease (increase) in:		
Assets acquired from insured institutions (note 3)	44,354,895	(15,874,225)
Loans to insured institutions and accrued interest	38,187,718	7,545,422
Subrogated accounts in insured institutions in liquidation and related interest	8,265,120	37,996,993
Accounts receivable	2,182,842	(807,405)
Deferred charges and other assets	47,107	(124,068)
Increase (decrease) in:		
Miscellaneous accrued and other liabilities	2,461,192	410,978
Decrease (increase) in cash	18,776	3,821,426
Total resources provided	$526,560,360	$445,982,926
FINANCIAL RESOURCES WERE APPLIED TO:		
Net additions in investments	418,139,638	361,875,220
Increase (decrease) in:		
Accrued interest on investments	6,430,109	8,813,932
Refund on secondary reserve	82,633,642	60,058,447
Contributions to insured institutions	15,539,869	12,395,801
Losses on assets acquired (note 3)	3,622,597	3,777,827
Decrease (increase) in deferred credits	194,505	(938,301)
Total resources applied	$526,560,360	$445,982,926

The accompanying notes to financial statements are an integral part of these statements.

FEDERAL SAVINGS AND LOAN INSURANCE CORPORATION

NOTES TO FINANCIAL STATEMENTS

DECEMBER 31, 1976 AND 1975

1. Summary of significant accounting policies

   (a) Investments--Investment securities are stated at cost, adjusted for amortization of premiums and accretion of discounts. Such amortization and accretion are computed on the "constant yield" method at rates based upon the lives of the related securities and are recognized as an adjustment to interest income on investments.

   (b) Furniture and equipment--These assets are stated at cost less accumulated depreciation. Depreciation is computed on the straight-line method over the estimated useful lives of the property. The net balance of this account is insignificant and is included in other assets.

   (c) Income recognition--Insurance premium income is recognized as earned when member institutions are assessed.

2. Investments--The investments at December 31, 1976 and 1975, are as follows (in millions):

	1976		1975	
	Book value	Market value	Book value	Market value
U.S. Treasury obligations	$4,256.7	$4,407.1	$3,815.8	$3,729.0
Federal agency securities	141.0	136.8	140.6	126.7
Total	$4,397.7	$4,543.9	$3,956.4	$3,855.7

3. Allowances for possible losses--An analysis of the changes in the allowances for possible losses on the accounts described below for years ended December 31, 1976 and 1975, follows:

Assets acquired from insured institutions	1976	1975
Balance, beginning of period	$6,754,893	$ 8,959,076
Add: Provision charged to expense	2,501,263	1,573,644
Add: Adjustment due to acquisition	4,047,771	3,169,465
Less: Losses on assets acquired	7,670,368	6,947,292
Balance, end of period	$5,633,559	$ 6,754,893
Loans to insured institutions		
Balance, beginning of period	$5,000,000	$ 5,000,000
Less: Provision adjustment credited to expense	2,865,290	-
Less: Losses on loans closed	2,134,710	
Balance, end of period	$ -	$ 5,000,000
Subrogated accounts in insured institutions in liquidation		
Balance, end of period	$1,500,000	$ 1,500,000
Contribution agreements		
Balance, beginning of period	$43,875,788	$25,859,169
Add: Provision charged to expense	11,434,870	30,412,420
Less: Contributions paid out	15,539,869	12,395,801
Balance, end of period	$39,770,789	$43,875,788

4. Allowance for estimated losses for contribution agreements--The Corporation enters into contribution agreements to restore an insured institution to normal operations and, under these arrangements, agrees to make, or commits itself to make, a cash contribution. The remaining contingent liability on these agreements totaled $88,176,276 and $56,003,261 at December 31, 1976 and 1975, respectively.

FEDERAL HOME LOAN MORTGAGE CORPORATION

FINANCIAL STATEMENTS

DECEMBER 31, 1976 AND 1975

SCHEDULE 11

SCHEDULE 11

FEDERAL HOME LOAN MORTGAGE CORPORATION

COMPARATIVE STATEMENT OF FINANCIAL CONDITION

AT DECEMBER 31, 1976 AND 1975

ASSETS	1976	1975
	(000 omitted)	
Mortgage loans, at unpaid principal balances: (notes 1, 2, 5, and 7)		
Insured by Federal Housing Administration (FHA) or guaranteed by Veterans Administration (VA)	$1,672,076	$1,877,166
Participation in conventional mortgages	808,635	843,697
Conventional mortgages	675,596	713,578
	3,156,307	3,434,441
Conventional mortgage loans funded under Special U.S. Treasury Program, pledged to secure advances (note 6)	1,091,991	1,528,224
	4,248,298	4,962,665
Less--Unamortized mortgage purchase discount	79,832	85,162
--Allowance for possible losses (note 3)	9,000	16,000
Total mortgage loans	4,159,466	4,861,503
Cash	222	369
Temporary cash investments, at cost plus accrued interest, which approximates market	583,945	978,433
Accrued interest receivable	8,660	41,635
Accounts receivable and other assets	1,701	2,020
Claims against FHA and VA, net of allowance for losses of $100,000 in 1976 and $200,000 in 1975	1,761	2,901
Real estate owned, at the lower of cost or estimated realizable value	2,598	2,312
Unamortized discount and commissions on mortgage loan sales	33,462	4,379
Unamortized debt expense	3,946	5,185
Total assets	$4,795,761	$5,898,737

The accompanying notes to financial statements are an integral part of these statements.

SCHEDULE 11

LIABILITIES AND STOCKHOLDERS' EQUITY

	1976	1975
	(000 omitted)	
Bonds and advances payable, including $866,507,000 at December 31, 1976 and $698,900,000 at December 31, 1975, due within one year (note 5)	$3,351,074	$4,049,952
Advances for Special U.S. Treasury Program, including $79,570,000 due in January 1977, and $30,970,000 due in January 1976 (note 6)	1,171,741	1,559,194
Other liabilities:		
Accured interest	96,489	121,298
Accounts payable and other accrued expenses	6,455	15,543
Commitment fees	910	96
	4,626,669	5,746,083
Reserve for management fee and guarantees (note 7)	13,116	10,839
Guaranteed mortgage certificates (note 7)	865,200	500,000
Less--Underlying mortgage loans sold, including principal collections held in trust of $71,250,000 at December 31, 1976, and $22,565,000 at December 31, 1975	865,200	500,000
	-	-
Commitments (note 4)		
Stockholders' equity:		
Common stock, nonvoting, $1,000 par value; no maximum authorization; 100,000 shares issued and outstanding	100,000	100,000
Retained earnings	55,976	41,815
	155,976	141,815
Total liabilities and stockholders' equity	$4,795,761	$5,898,737

SCHEDULE 12

FEDERAL HOME LOAN MORTGAGE CORPORATION

COMPARATIVE STATEMENT OF INCOME, EXPENSE, AND RETAINED EARNINGS

FOR THE YEARS ENDED DECEMBER 31, 1976 AND 1975

	1976	1975
	(000 omitted)	
INCOME:		
Interest and discount on mortgage loans, net (note 1)	$369,928	$397,526
Management fee and guarantee	3,271	3,285
Interest on temporary cash investments	66,657	41,053
Other income	4,059	3,535
Total income	443,915	445,399
EXPENSES:		
Interest on borrowings and related costs	419,058	407,745
Provision (credit) for losses, management fee, and guarantees (notes 3 and 7)	(995)	11,386
Commitment fees	1,005	587
Administrative	10,686	10,173
Total expenses	429,754	429,891
Net Income	14,161	15,508
Retained earnings, beginning of year	41,815	26,307
Retained earnings, end of year	$ 55,976	$ 41,815
Earnings per common share	$ 141.61	$ 155.08

The accompanying notes to financial statements are an integral part of these statements.

SCHEDULE 13

FEDERAL HOME LOAN MORTGAGE CORPORATION

COMPARATIVE STATEMENT OF CHANGES IN FINANCIAL POSITION

FOR THE YEARS ENDED DECEMBER 31, 1976 AND 1975

	1976	1975
	(000 omitted)	
Funds provided:		
Net income	$ 14,161	$ 15,508
Charges (credits) to income not affecting funds:		
Amortization of mortgage purchase discount	(7,614)	(7,668)
Amortization of debt expense	1,239	1,532
Provision (credit) for losses, management fees and guarantees (notes 3 and 7)	(995)	11,386
Funds provided from operation	6,791	20,758
Mortgage loan principal repayments	456,469	290,538
Proceeds from issuance of bonds and advances, net of debt expense	-	211,023
Proceeds from advances for special U.S. Treasury program	-	879,500
Mortgage loans sold:		
Mortgage participation certificates, net of repurchases	937,297	452,111
Guaranteed mortgages certificates	398,200	497,250
FHA/VA	35,425	66,939
Decrease (increase) in accrued interest receivable	32,975	7.180
Decrease (increase) in cash and temporary cash investments	394,635	(599,780)
Total funds provided	$2,261,792	$1,825,519
Funds applied:		
Mortgage loans purchased, net of discount:		
Regular programs	$1,125,188	$ 828,808
Special U.S. Treasury program	-	875,672
Bonds and advances retired	698,878	2,023
Repayments of advances for special U.S. Treasury program	387,453	15,306
Decrease (increase) in short-term discount notes	-	147,600
Decrease (increase) in accounts payable and other accrued expenses	9,088	(405)
Decrease (increase) in accrued interest payable	24,809	(54,455)
Other items, net	16,376	10,970
Total funds applied	$2,261,792	$1,825,519

The accompanying notes to financial statements are an integral part of these statements.

FEDERAL HOME LOAN MORTGAGE CORPORATION

NOTES TO FINANCIAL STATEMENTS

DECEMBER 31, 1976 AND 1975

1. Summary of significant accounting policies

Recognition of gain (loss) on mortgage loans

Federal Home Loan Mortgage Corporation (the "Corporation") provides for estimated losses on mortgage loan purchases, including outstanding commitments. which may be incurred upon the funding of such purchases through a security sale, or upon sale of the loans, and provides allowances for uninsured losses. To the extent a loss is indicated on the financing of mortgage loans, the loss attributable to such financing is charged against the allowance for possible losses which is reflected in the balance sheet as a reduction of mortgage loans. This reduction in the mortgage loans results in additional yield which is recognized over the term of the related borrowing.

Sales of Mortgage Participation Certificates and Guaranteed Mortgage Certificates representing undivided interests in mortgage loans provide for the Corporation to manage and guarantee the underlying mortgages. If the Corporation's net yield after estimated management fees and guarantees is less than the effective rate payable to the investor, the Corporation recognizes the estimated loss when incurred. Gains, representing the excess of the effective interest income rate to the Corporation over that payable to the investor, are recognized as earned over the life of the related mortgage loans and are reported as management fee and guarantee income in the accompanying financial statements

Mortgage purchase discount

Discount on mortgages purchased is recorded as income over the term of the related mortgage loans using the level yield method.

Unamortized discount and commissions on mortgage loan sales

Mortgage Participation Certificates and Guaranteed Mortgage Certificates (see "Mortgage Loan

Sales" note) may be sold at discounts. Discount on Mortgage Participation Certificates is amortized over the life of the related mortgage loans, and discount and brokerage commissions on Guaranteed Mortgage Certificates are amortized over the period to the optional repurchase date, both using the level yield method. This amortization is recorded as a reduction of management fee and guarantee income in the accompanying financial statements.

Amortization of debt expense

Debt expense is amortized over the period during which the related indebtedness is outstanding. Commitment Fees.

Commitment fees received/paid are deferred and treated as additional mortgage purchase/sales discount when delivery occurs, or recognized as income/expense if delivery does not occur.

2. Mortgage loans

As of December 31, 1976 and 1975, the effective net yield of mortgage loans after deducting servicing fees was as follows:

	1976	1975
FHA and VA mortgages	7.66%	7.64%
Participation in conventional mortgages	9.10%	8.97%
Conventional mortgages	8.79%	8.90%

3. Allowance for possible losses on mortgage loans

An analysis of the changes in the allowance for possible losses on mortgage loans for the years ended December 31, 1976 and 1975, follows:

	1976	1975
	(000 omitted)	
Balance, beginning of year	$16,000	$10,000
Provision (credit) reflected in current earnings	(4,625)	9,435
Reductions attributable to:		
Losses on sales of Mortgage Participation Certificates	-	(2,310)
Losses on mortgages sold	(2,375)	(1,125)
Balance, end of year	$ 9,000	$16,000

Many factors influence the determination of the Corporation's allowance for possible losses on mortgage loans, including market yields, delinquencies, financing costs, etc. During 1976 this allowance was adjusted downward, reflecting an overall reduction in the level of risk inherent in the Corporation's mortgage loan portfolio.

GAO note: Additional write downs of specific reserve accounts totaled $172,000 and are included in the balance sheet under Claim Against FHA and VA, Net of Allowances ($100,000) and Accrued Interest Receivable ($72,000).

4. Commitments

The Corporation's outstanding commitments to purchase and sell mortgage loans at December 31, 1976, are summarized below.

Commitments to purchase

The average effective net yield on commitments to purchase mortgage loans is determined after deducting servicing fees. Delivery of mortgages under the 6-month forward commitment program is at the option of the seller; delivery is mandatory under all other commitment programs, and must occur within 60 days of the contract date.

	December 31, 1976	
	Average effective net yield	Amount
		(000 omitted)
FHA/VA	8.41%	$ 1,000
Participation in conventional mortgages:		
Home	8.60%	157,000
Multifamily	9.38%	4,000
Conventional mortgages:		
Home	8.63%	70,000
Multifamily	9.50%	1,000
Six month forward	8.59%	100,000
		$333,000

Commitments to sell

The Corporation's Mortgage Participation Certificates (PCs) are continuously offered for sale under both mandatory and optional delivery programs. Delivery periods range from 7 to 150 days under the mandatory program. Offers where delivery is at the Corporation's option have settlements between 120 and 150 days from the date of the contract. The Corporation pays commitment fees ranging up to 1 percent, dependent on the length of delivery period, on all offers with specified delivery beyond 30 days from the date of the contract. The average effective rate payable to the investor includes the effect of commitment fees paid.

	December 31, 1976	
	Average effective rate payable to investor	Amount
		(000 omitted)
Mandatory	7.95%	$256,400
Optional	8.30%	162,700
		$419,100

5. Bonds and advances

A summary of bonds and advances payable is as follows:

	Maturity	December 31, 1976 Interest rate	December 31, 1976 Balance	December 31, 1975 Interest rate	December 31, 1975 Balance
			(000 omitted)		(000 omitted)
Bond payable to bank	1976/1986	7.75%	$ 19,465	7.75%	$ 20,128
Advances from Federal Home Loan Bank in the form of a pass-through of Consolidated Federal Home Loan Bank Obligations	1976	-	-	9.36	290,000
	1977	8.46	500,000	8.46	500,000
	1978	9.43	300,000	9.43	300,000
	1979	9.50	100,000	9.50	100,000
	1981	8.69	400,000	8.69	400,000
	1982	8.65	190,000	8.65	190,000
	1984	8.78	300,000	8.78	300,000
	1993	7.41	400,000	7.41	400,000
			2,190,000		2,480,000
Mortgage-Backed Bonds	1976	-	-	7.15	400,000
	1977	6.24	350,000	6.24	350,000
	1978	5.30	51,375	5.30	51,375
	1979	6.06	103,580	6.06	103,580
	1976/1980	5.24	200,193	5.25	201,408
	1985	5.33	3,461	5.33	3,461
	1976/1995	8.69	133,000	8.69	140,000
	1977/1996	7.84	150,000	7.84	150,000
	1997	7.25	150,000	7.25	150,000
			1,141,609		1,549,824
Bonds and advances payable			$3,351,074		$4,049,952

The 1997, 1976/1995, and 1977/1996 mortgage-backed bonds and the 1993 advance from the Federal Home Loan Bank are redeemable at the Corporation's option commencing 1982, 1983, 1984, and 1983, respectively, at their face value. On the 1976/1995 and 1977/1996 bonds, a sinking fund provides for annual retirements at $7 and $7.5 million principal amount of bonds, respectively, commencing in 1976 and 1977. In addition, the Corporation has a noncumulative option to increase the sinking fund amounts each year by an amount not exceeding the annual retirement amounts.

All mortgage-backed bonds are guaranteed as to principal and interest by the Government National Mortgage Association (GNMA). Under the provision of a Trust Indenture with GNMA dated October 26, 1970, and supplements thereto, the Corporation conveyed mortgages to the Trust as security for the mortgage-backed bonds. As of December 31, 1976 and December 31, 1975, Trust assets of approximately $2.1 billion, constituting primarily principal balances of such mortgages, are restricted for the payment of principal and interest on the Mortgage-Backed Bonds and are included in the accompanying balance sheet.

The bond payable to bank is collateralized by a like amount of FHA/VA mortgages and calls for specific annual principal repayments ranging from $663,000 to $1,408,000 over the life of the bond with the balance due at maturity.

6. Special U.S. Treasury-funded program

Pursuant to a joint United States Department of the Treasury-Federal Home Loan Bank System program, the Corporation acquired $1.575 billion aggregate principal balance of conventional mortgage loans. This program was financed by loans from the Treasury to the Bank System, which in turn passed through the funds to the Corporation. The mortgage loans, with an unpaid principal balance of $1,091,991,000 at December 31, 1976, and $1,528,224,000 at December 31, 1975, are pledged as collateral for the Treasury loan. The agreement provides that the Corporation's borrowing costs will not exceed its return on the mortgages. The terms of the agreement also provide for the Corporation to make semiannual installments in amounts at least equal to the principal collections on the related mortgage loans pledged as collateral.

The agreement provides that the Corporation may, at its option, retire additional amounts of the Treasury debt. The Corporation, during 1976, elected to retire $318.9 million of this debt in excess of the required payments.

7. Mortgage loan sales

The Corporation sells Mortgage Participation Certificates (PCs) and Guaranteed Mortgage Certificates (GMCs) representing undivided interests in mortgage loans. The Corporation guarantees the timely payment of interest and the collection of principal on the mortgage loans and has provided $3,802,000 in 1976 and $1,951,000 in 1975 for such guarantees. These amounts have been reflected in the provision for losses, management fee and guarantees.

Holders of Mortgage Participation Certificates receive interest monthly at the certificate rate together with their pro rata share of principal payments received by the Corporation. The issued certificates have been accounted for as sales, and the mortgage loans and the certificates issued are Unpaid balances of the outstanding certificates were not included in the accompanying balance sheet. approximately $1.900 billion and $1.143 billion at December 31, 1976 and December 31, 1975, respectively. At December 31, 1976, the weighted average remaining term to maturity of the related mortgage loans was 28 years. At December 31, 1976 and December 31, 1975, the excess effective interest income rate to the Corporation over that payable to the PC investor was .40 percent and .42 percent, respectively.

Holders of Guaranteed Mortgage Certificates are paid interest semiannually at the certificate rate, and annually, their pro rata share of principal collected or specified minimum annual principal reductions, whichever is greater. Any GMC holder may, at his option, require the Corporation to repurchase such certificates on a designated "optional repurchase date" at the then unpaid principal balance.

A summary of outstanding GMCs is as follows:

Issue	Issue date	Optional Repurchase date	Unpaid principal balances December 31, 1976	December 31, 1975
GMC Series A 1975	02/25/75	03/15/90	$277,800	$300,000
GMC Series B 1975	11/25/75	09/15/90	187,400	200,000
GMC Series A 1976	02/25/76	03/15/91	200,000	-
GMC Series B 1976	08/25/76	09/15/96	200,000	-
			$865,200	$500,000

At December 31, 1976 and December 31, 1975, the excess effective interest income rate to the Corporation over that payable to the GMC investor was .14 percent and .03 percent, respectively. The effective interest income rate to the Corporation has not been adjusted to semiannual uield equivalent.

8. Pension plan

In November 1974, the Corporation established a non-contributory pension plan covering all eligible employees. Total pension expense was approximately $422,000 and $347,000 for the years ended December 31, 1976 and December 31, 1975, respectively. The Corporation's policy is to fund pension cost accrued. The pension fund assets exceed the actuarially computed value of vested benefits. In the opinion of management, the pension plan complies with the provisions of the Pension Reform Act of 1974.

APPENDIX

PRINCIPAL OFFICIALS

RESPONSIBLE FOR THE ACTIVITIES

DISCUSSED IN THIS REPORT

	Tenure of office From	To
FEDERAL HOME LOAN BANK BOARD		
BOARD OF DIRECTORS (note a):		
Garth Marston, Chairman	Dec. 1976	July 1977
Acting Chairman	Apr. 1974	Dec. 1976
Grady Perry, Jr.	June 1973	July 1977
FEDERAL SAVINGS AND LOAN INSURANCE CORPORATION		
DIRECTOR:		
Loren Means (acting)	Aug. 1976	Present
Richard Platt, Jr.	Sept. 1973	Aug. 1976
FEDERAL HOME LOAN MORTGAGE CORPORATION		
PRESIDENT:		
Victor H. Indiek	Sept. 1974	Present

a/The board members of the Federal Home Loan Bank Board also serve as the Board of Directors of the Federal Home Loan Mortgage Corporation.