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BY FEDERAL EXPRESS AND EMAIL

Alfred M. Pollard, General Counsel
Federal Housing Finance Agency
Fourth Floor
1700 G Street, N.W.
Washington, DC 20552
Attention: Comments/RIN 2590-AA08

RE: Proposed Rule on Golden Parachute and Indemnification Payments

Dear Mr. Pollard:

The Federal Home Loan Bank of Atlanta ("Bank") is writing to comment on the Federal Housing Finance Agency's ("FHFA") proposed rule on Golden Parachute and Indemnification Payments published on June 29, 2009 (the "Proposal"), which is intended to implement portions of Section 1114 of the Housing and Economic Recovery Act of 2008 ("HERA") that are to be codified at 12 U.S.C. § 4518(e).[1] The Bank welcomes the opportunity to comment on the Proposal.

I. Golden Parachute Provisions

We appreciate the FHFA's prompt action to propose more detailed rules regarding the final golden parachute rule that it published on January 29, 2009.[2]

We recognize and appreciate that the golden parachute portion of the Proposal draws a range of points from the Federal Deposit Insurance Corporation's ("FDIC") regulation on Golden Parachute and Indemnification Payments, which is codified at 12 C.F.R. Part 359 ("FDIC Rule"), and addresses suggestions that were contained in comment letters which were submitted by the Federal Home Loan Banks ("FHLBanks") in response to the interim final

1 74 Fed. Reg. 30975 (to be codified at 12 C.F.R. pt. 1231).

2 74 Fed. Reg. 5101.

rule on golden parachute payments,[3] including the comment letter submitted on behalf of the Bank by the chairman of the Bank's board of directors.[4] Consistent with that prior comment letter, we offer the following comments and recommendations on the golden parachute portion of the Proposal.

A. Provide Guidance and Clarification on Certain Timing Issues

The Proposal does not clearly address a number of important issues that may confront an FHLBank. In this regard, the final rule should address the following matters:

- that a healthy FHLBank — *i.e*, one that is not subject to any of the triggering events listed in paragraph (1)(ii) of the definition of "golden parachute payment" in proposed section 1231.2 ("Triggering Event") (including an FHLBank which had previously been subject to a Triggering Event, but is no longer subject to a Triggering Event), — need not obtain the approval of the FHFA Director ("Director") to enter into an agreement that could potentially result in a "golden parachute payment" in the event that a Triggering Event later occurs;[5]

- that if an individual begins to receive golden parachute payments under an agreement prior to the occurrence of a Triggering Event, the subsequent occurrence of a Triggering Event would not have any effect on the continuation of such payments, and the FHLBank would not be required to seek approval of the Director to continue the payments;[6] and

- that if an individual's employment terminates after a Triggering Event that is then resolved so that when the employment ends no Triggering Event is in effect, the approval of the Director is not required to make payments to that individual.

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3 73 Fed. Reg. 53356 (Sept. 16, 2008), and amended at 73 Fed. Reg. 54309 (Sept. 19, 2008) (removing and reserving sections 1231.3 and 1231.4) and at 73 Fed. Reg. (Sept. 23, 2008).

4 Letter from Scott C. Harvard dated October 24, 2008, located on the FHFA's website at the following web address:

http://www.fhfa.gov/webfiles/150/%2314_Golden_Parachute_(RIN_2590-AA08)_-_FHLBank_Atlanta.pdf

5 As we understand the proposed rule, if an individual entered into an agreement that was not subject to the Director's approval because no Triggering Event had occurred and then terminated his or her employment after a Triggering Event occurred, the FHLBank can seek the Director's approval to make such golden parachute payments to the individual by making the filing described in proposed section 1231.6, and the Director may grant such approval under proposed section 1231.3(b)(i).

6 The FDIC clarified this point in its golden parachute regulation by providing that a condition for a payment being treated as a golden parachute payment is that it is an amount that becomes payable to an employee whose employment is terminated at a time when a triggering event under the FDIC golden parachute rule is in effect. 12 C.F.R. § 359.1(f)(iii)(A).

B. Clarify that the Director May Approve an Agreement that Provides for a "Golden Parachute Payment" with a Current Employee of an FHLBank that is Subject to a Triggering Event

Proposed section 1231.3(b)(1)(ii) expressly refers to the possibility that an FHLBank that is subject to a Triggering Event, or that is seeking to avoid being imminently subject to a Triggering Event, may obtain approval from the Director to enter into an agreement with a new hire that provides for a golden parachute payment. We request clarification that the Director under the authority of proposed section 1231.3(b)(i) may likewise approve an agreement with a current employee of an FHLBank that is subject to a Triggering Event that provides for a golden parachute payment.

The final rule should clarify that, in any circumstances in which an agreement that provides for a golden parachute payment has been approved by the Director, no further approval by the Director under proposed section 1231.3(b) or otherwise will be required to make a golden parachute payment under the agreement.[7]

C. Confirm the Meaning of the Term "Compensation" for Purposes of the Golden Parachute Payments Rule

The Proposal does not define the term "compensation." The final rule should be modified to expressly include the definition of "compensation" that is set forth in section 1303 of the Federal Housing Enterprises Financial Safety and Soundness Act of 1992, as amended ("1992 Act"):

> The term "compensation" means any payment of money or the provision of any thing of current or potential value in connection with employment (emphasis added).[8]

Since the term "golden parachute payment" is defined in section 1318(e)(4) of the 1992 Act and in proposed section 1231.2 as a "payment (or any agreement to make any payment) in the nature of compensation by any regulated entity" (emphasis added), the express inclusion of a specific definition of compensation in the final rule will ensure that the term "golden parachute payment" will only apply in the circumstances that Congress intended.

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7 Proposed section 1231.3(b)(1)(iii) provides that a regulated entity may agree to make a golden parachute payment under an agreement, which provides for severance payment not to exceed 12 months salary, in the event of a change of control, provided that the regulated entity shall obtain consent of the Director prior to making such a payment. This provision should be modified to expressly provide that approval for a payment under such an agreement could also be sought from the Director prior to the FHLBank entering into the agreement.

8 12 U.S.C. § 4502(6). The FHFA used the same sentence from the definition of compensation in the 1992 Act in its proposed definition of "compensation" in its recently proposed regulation on executive compensation. 74 Fed. Reg. 26989 (to be codified at 12 C.F.R. § 1230.2) (June 5, 2009).

This confirmation would make it clear that the final rule covers only payments "in the nature of compensation" and does not apply under any circumstances to other non-employment payments. Such non-employment payments include debt service payments from an FHLBank to the Office of Finance, payments of advance proceeds, dividends, deposit account withdrawals, and AHP funds from an FHLBank to a member institution, and payments to other parties (including payments to FHLBank directors) who may be considered to be an entity-affiliated party, but the payments to whom are not connected with an employee relationship with an FHLBank.

D. Provide Certain Exclusions from the Definition of "Entity-Affiliated Party"

The Bank requests that the definition of "entity-affiliated party" for purposes of the golden parachute payment rules be modified to exclude both (i) shareholders of an FHLBank and (ii) participants in an FHLBank's Affordable Housing Program. We believe that this change is necessary to recognize the distinctiveness of the FHLBanks (including their cooperative ownership structure and affordable housing and community development mission) consistent with Section 1201 of HERA. FHLBank shareholders are not entitled to vote on any matters other than the election of directors, and statutory caps on shares entitled to be voted effectively bar any single shareholder from controlling the selection of board members. AHP participants do not in any meaningful way control the affairs of an FHLBank. We note that the statutory language in the HERA golden parachute payments provision only requires application to "affiliated parties," not to "entity-affiliated parties" under Section 1002 of HERA.[9]

E. Provide for Exclusion of Certain Payments to Rank-and-File Employees in Connection With Negotiated Terminations of Employment

Payments under certain qualified nondiscriminatory severance pay plans or arrangements are not considered to be golden parachute payments. It is possible that depending on particular circumstances, including whether an FHLBank has such a nondiscriminatory severance pay plan and the circumstances involving a particular employee, an FHLBank may wish to enter into a negotiated termination of an employee's employment with the FHLBank, pursuant to which the employee would receive a payment that does not fall within the terms of a nondiscriminatory severance pay plan or arrangement as described in the Proposal.

The final rule should make it clear that an FHLBank's agreement to pay severance to a rank-and-file employee (i.e., an employee who is not an "executive officer" under FHFA regulations) in an amount not exceeding compensation paid to the employee during the 12 months preceding a negotiated termination of his or her employment is excluded from the definition of a golden parachute payment and thus would not require FHFA approval if a Triggering Event were in effect with regard to the FHLBank. Such an exclusion would ensure that the FHLBank retains the flexibility to

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9 Compare HERA § 1002 with HERA § 1114.

conduct its ordinary course personnel operations without the need for FHFA approval of customary limited payments in connection with negotiated terminations.

F. Clarify that Unused Leave is Not a "Golden Parachute Payment"

The final rule should clarify that the customary payment of unused annual leave in connection with the termination of employment does not constitute a "golden parachute payment." We believe that this could be appropriately addressed through an additional exclusion to the term golden parachute payment in paragraph (2) of the definition of that term in proposed section 1231.2.

G. Treatment of Nonqualified Deferred Compensation Plans and Supplemental Retirement Plans

Under paragraph 3(i) of the definition of bona fide deferred compensation plan or arrangement in proposed section 1231.2, a plan or arrangement that would otherwise qualify for an exclusion from treatment as a golden parachute payment would not qualify for such treatment, if the plan or arrangement were not in effect at least one year prior to the occurrence of a Triggering Event. Furthermore, under paragraph (3)(ii) of the deferred compensation definition, an increase in benefits payable under a qualifying plan or arrangement pursuant to an amendment made during the one-year period prior to the occurrence of a Triggering Event, would appear not to be excluded from the definition of a golden parachute payment.

Paragraphs (3)(i) and (ii) of the definition of bona fide deferred compensation plan or arrangement in proposed section 1231.2 should be modified to provide that these one-year rules be subject to waiver by the Director on a case-by-case basis. In any event, we believe that an FHLBank could apply for approval to make a payment with respect to the plan or increased benefits under proposed sections 1231.3(b)(1)(i) and 1231.6. Further, there should be an exception for amendments that have been made to comply with law. We suggest adding the following language to the end of Paragraph 3(ii): "provided further that changes for statutory compliance, such as Code Section 409A, should be disregarded in determining whether a plan provision has been in effect for one year."

H. Modify the Circumstances that Constitute a Triggering Event

The portion of proposed paragraph (1)(ii)(D) of the definition of golden parachute payment in proposed section 1231.2, which reads "or the Federal Home Loan Bank or the Office of Finance is assigned a composite rating of 3 or 4 by FHFA," should be revised to delete "3 or". We note that the Federal Housing Finance Board Office of Supervision Examination Manual ("Manual") draws a sharp distinction between a Composite 3 and a Composite 4 rating.[10] The Manual provides that the general policy

[10] Manual April 2007 at 5ROE.1.15.

in regard to a Composite 3 rated FHLBank is that supervisory action will be taken to address identified deficiencies or weaknesses. In contrast, the Manual provides that the general policy in regard to a Composite 4 rated FHLBank is that a formal enforcement action will be taken to address identified deficiencies or weaknesses. The restrictions of the golden parachute rule should not be triggered in circumstances that are not viewed as being serious enough to require formal enforcement action.

As a substitute for considering a composite exam rating of 3 to be a Triggering Event, we suggest FHFA include within paragraph (1)(ii) of the definition of golden parachute payment a new component relating to its capital classifications regulation,[11] such that the classification of an FHLBank as "significantly undercapitalized"[12] would constitute a Triggering Event. In this way the limits on golden parachute payments would dovetail with the compensation restrictions set forth in the capital classifications regulation, which prohibits the payment of bonuses and salary increases to executive officers once an FHLBank is classified as "significantly undercapitalized."[13] Note that section 1229.4(b)(3) of the capital classifications regulation permits the Director to reclassify an FHLBank downward if the Director finds that the bank is engaging in an unsafe and unsound practice because of a failure to address deficiencies in asset quality, management, earnings or liquidity deemed less than satisfactory during its most recent examination. This seems like a much more appropriate trigger for imposing golden parachute payment restrictions.

I. Consider Mitigating Factors in Determinations Regarding Approval of Golden Parachute Payments

Proposed section 1231.3(b)(2) should be modified to expressly provide that the Director will consider certain mitigating factors in determining whether to permit a golden parachute payment to be made. Such mitigating factors may include, among others, the individual's history of beneficial contribution to the FHLBank, and cooperation with FHFA's relevant remediation efforts.

II. Indemnification Provisions

The Proposal includes proposed provisions regarding certain limitations on indemnification by regulated entities and the Office of Finance. The Proposal states that these indemnification provisions are substantially similar to the proposed indemnification provisions published on November 14, 2008 ("November Indemnification Proposal").[14] The Proposal indicates that the FHFA will consider comments received in response to the November Indemnification Proposal. Therefore, we will not repeat the comments set forth in the Bank's comment letter

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11 12 CFR Part 1229.

12 12 CFR § 1229.3(c).

13 12 CFR § 1229.8(e) and (f).

14 73 Fed. Reg. 67426.

submitted December 19, 2008,[15] but ask that you consider them incorporated by reference. We also submit the following additional comments on the indemnification portions of the Proposal.

A. Allow for Indemnification Granted in Judicial Proceedings

Under the Proposal, an FHLBank's board of directors must specifically authorize indemnification payments made to an indemnitee. Corporate law in some jurisdictions recognizes another way in which a person may obtain permissible indemnification, specifically by obtaining a ruling from the judge before whom the underlying case was heard. The final rule should allow this alternative route to indemnification as well.

B. Partial Indemnification in Relation to Settlements and Formal Adjudications and Findings

Under the Proposal, the term "prohibited indemnification payment" shall not include "any reasonable payment by a regulated entity or the Office of Finance that represents partial indemnification for legal or professional expenses specifically attributable to particular charges for which there has been a formal and final adjudication or *finding in connection with a settlement that the entity-affiliated party has not violated certain laws or regulations or has not engaged in certain unsafe or unsound practices or breaches of fiduciary duty*, unless the administrative proceeding or civil action has resulted in a final prohibition order against the entity-affiliated party under section 1377 of the Safety and Soundness Act (emphasis added)."[16]

The definition of the term "prohibited indemnification payment" should not unduly restrict the potential to negotiate and consummate settlements with an entity-affiliated party. To the extent an entity-affiliated party is unable to obtain partial indemnification for legal and professional expenses which are not specifically or directly related to the remedy provided in a settlement agreement, the entity-affiliated party's willingness to settle other charges with the FHFA may be adversely impacted. This may lead to unnecessary and wasteful litigation.

In this regard, settlements with federal financial regulatory agencies do not typically contain findings by the charging agency which exculpate the party settling the charges from wrongdoing with respect to some or all of the charges. They almost always contain statements to the effect that the person settling the charges "neither admits nor denies" the agency's allegations. As a result, the availability of partial indemnification in the Proposal may prove to be illusory.

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15 A copy of that comment letter is available on the FHFA website at the following address:

http://www.fhfa.gov/webfiles/279/1GPFHLBankAtlanta.pdf

16 See paragraph (2)(ii) of the definition of prohibited indemnification payment in proposed section 1231.2.

In the case of either a settlement or a formal and final adjudication, the Proposal only allows indemnification for expenses specifically attributable to particular charges as to which the entity-affiliated party has been successful. As a practical matter, it will often be difficult, if not impossible, to precisely allocate expenses related, for example, to the review of documents, or the preparation for a deposition to a particular individual charge.[17] The principle sought to be addressed by this aspect of the Proposal would be better and more fairly effectuated by providing that legal and professional fees incurred may be reimbursed in proportion to the percentage of charges as to which the entity-affiliated party is entitled to reimbursement under the terms of the Proposal.

In light of the foregoing, the FHFA should revise the applicable exception to the definition of the term "prohibited indemnification payment" in section 1231.2 as follows:

> The term prohibited indemnification payment shall not include any reasonable payment by a regulated entity or the Office of Finance that represents partial indemnification for legal or professional expenses **[Delete the following bracketed text]** [specifically] attributable to particular charges for which there has been a formal and final adjudication **[Insert the following bracketed text]** [that the entity-affiliated party has not violated certain laws or regulations or has not engaged in certain unsafe or unsound practices or breaches of fiduciary duty], or **[Insert the following bracketed text]** [any matters which were the subject of a notice of charges which do not form the basis for any remedies imposed on the entity-affiliated party under the terms of a settlement with the entity-affiliated party,] [**Delete the following bracketed text**] [finding in connection with a settlement that the entity-affiliated party has not violated certain laws or regulations or has not engaged in certain unsafe or unsound practices or breaches of fiduciary duty] unless the administrative proceeding or civil action has resulted in a final prohibition order against the entity-affiliated party under section 1377 of the Safety and Soundness Act (12 U.S.C. 4636a) [**Delete the following bracketed text**] [.] **[Insert the following text]** [; provided that the amount of such permissible partial indemnification shall be determined by the ratio that is (a) the charges as to which the entity-affiliated party is deemed to be permitted to receive indemnification under this paragraph, to (b) the total number of charges.]

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[17] In the FDIC's final rule, the FDIC acknowledged the difficulty in allocating expenses between different charges: "The FDIC recognizes that in many cases the appropriate amount of any partial indemnification will be difficult to ascertain with certainty." 61 Fed. Reg. 5926, 5929 (1996).

C. Commencement of an Administrative Action

We note that the proposed section 1231.4(a) of the November Indemnification Proposal provided that the indemnification provisions in proposed section 1231.4 would only apply after an administrative proceeding or civil action has been instituted by the FHFA "through issuance of a notice of charges under regulations issued by the Director."[18] Similarly, in promulgating the FDIC Rule, the FDIC stated that it considers a formal administrative action to be commenced by the issuance of a "Notice of Charges."[19]

Proposed section 1231.4(a) of the Proposal, however, now omits the words "through the issuance of a notice of charges under regulations issued by the Director" and instead provides that the section applies "only after an administrative proceeding or civil action has been instituted by the FHFA." The FHFA should confirm that for purposes of an administrative action the issuance of a notice of charges would continue to be the point at which the indemnification provisions of proposed section 1231.4 would be triggered, and that the filing of a complaint in a civil action would be the point at which the indemnification provisions of proposed section 1231.4 would be triggered.[20]

D. Grandfathering Considerations

The FHFA in the preamble to the Proposal stated that it recognizes that prior to the enactment of HERA, the regulated entities or the Office of Finance "may have entered into indemnification agreements that provide for indemnification beyond that which is proposed to be permissible under section 1318(e) of the Safety and Soundness Act (12 USC 4518(e)), and the proposed amendment (emphasis added)."[21] The FHFA further stated that it "intends that the proposed amendment would apply to agreements entered into by a regulated entity ... with an entity-affiliated party on or after the date the regulation is effective (emphasis added)."[22]

Under the FHFA's preamble statements, restrictions on indemnification in certain circumstances under a new final rule adopted by the FHFA as a result of the Proposal will not apply to any agreement that provides for indemnification that is entered into

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18 73 Fed. Reg. at 67426.

19 61 Fed. Reg. at 5930.

20 As we understand the Proposal, any legal or other expenses incurred prior to the institution of an administrative proceeding or civil action would under no circumstances be deemed to be prohibited indemnification payments.

21 74 Fed. Reg. at 30976.

22 Id.

prior to the effective date of a new final rule. The Proposal does not define what constitutes an "agreement" for purposes of this grandfathering treatment.

The FHFA should clarify the final rule so that both an indemnification bylaw provision that is expressly contractual in nature and a separate indemnification agreement will be treated equally as an "agreement" for grandfathering purposes.

In addition, the final rule should also confirm that any person who is covered (either by virtue of current or past service to an FHLBank) by an existing contractual indemnification bylaw provision, or an existing separate indemnification agreement, will not be subject to any new restrictions on indemnification payments contained in the final rule that did not exist prior to the effective date of the final rule.[23] In this regard, modifications to an existing contractual bylaw or an indemnification agreement should not affect the availability of grandfathering treatment. In contrast, an individual whose coverage under either a contractual indemnification bylaw or a separate indemnification agreement that begins on or after the effective date of the final rule will be subject to any new limitations imposed under the final rule.

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On behalf of the Bank, we appreciate your consideration of these comments.

Sincerely,

Jill Spencer

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23 We note that 12 C.F.R. § 908.6(i) currently provides that an FHLBank shall not reimburse, indemnify or otherwise compensate directly or indirectly any executive officer or director for a third-tier civil money penalty imposed under the pre-HERA version of 12 U.S.C. § 4636. Thus, an individual subject to a grandfathered FHLBank contractual indemnification bylaw or a separate indemnification agreement would be permitted to receive indemnification of a first or second- tier civil money penalty under 12 U.S.C. § 4636(b)(1)-(2) and would not be subject to any limitation on advancement or ultimate indemnification of legal or other expenses or judgments incurred in connection with an administrative proceeding or civil action brought by the FHFA.