

July 14, 2009

Alfred M. Pollard
General Counsel
Federal Housing Finance Agency
Fourth Floor
1700 G Street, NW.,
Washington, DC 20552

RE: Comment on RIN 2590-AA12

Dear Mr. Pollard:

After a thorough reading and analysis of the proposed rule on executive compensation, I am of the opinion that further revisions are necessary before a final regulation is issued. Specifically, I do not believe that this rule, as written, would provide adequate procedures or safeguards to ensure that executive compensation is reasonable and comparable to those paid at similar institutions for similar duties.¹

A. Critique of Proposed Rule 12 CFR Part 1230 – Executive Compensation

1. Too much discretion on the part of the Director

As you already know, the mission of the Federal Housing Finance Agency (FHFA) is “to promote a stable and liquid mortgage market, affordable housing, and community investment through *safety and soundness oversight* of Fannie Mae, Freddie Mac, and the Federal Home Loan Banks.”² Likewise, part of the purpose of proposed rule 1230 is to “...*enhance the efficiency of the FHFA’s oversight of executive compensation.*”³

Although the proposed rule would indeed provide significant procedures for the oversight of executive compensation for regulated entities, it appears that the strength of this oversight hinges on the sole discretion of the Director. In other words, rather than establish an *affirmative duty*, the proposed rule merely grants the Director of FHFA (or his designee) the *right* to determine whether to prohibit or withhold executive compensation of a regulated entity. To illustrate this point, I cite and comment to the following examples of specific language within the proposed rule:

§ 1230.3 Prohibition and withholding of executive compensation.

(a) *In general.* The Director may review the compensation arrangements for any executive officer of a regulated entity or the Office of Finance at any time, and shall

¹ NOTE: Terms used throughout this letter comport and relate to the same terms and definitions used in §1230.2 of the proposed rule.

² Federal Housing Finance Agency, *FHFA Mission*, <http://www.fhfa.gov/Default.aspx?Page=38> (emphasis added).

³ Executive Compensation, §1230.1, 74 Fed. Reg. 26989 (proposed June 5, 2009) (to be codified at 12 C.F.R. pt. 1230) (emphasis added).

prohibit the regulated entity or the Office of Finance from providing compensation to any such executive officer *that the Director determines* is not reasonable and comparable with compensation for employment in other similar businesses... involving similar duties and responsibilities.⁴

Comment 1: Although the Director “may” review the compensation arrangements, the wording is such that it fails to create an affirmative duty to actively review the compensation arrangements of executive officers in regulated entities.

Comment 2: Although regulated entities are prohibited from providing executive compensation that is not reasonable and comparable, it is up to the sole discretion of the Director to determine when compensation is reasonable and comparable.

(b) *Factors to be taken into account.* In determining whether compensation provided by a regulated entity or the Office of Finance to an executive officer is not reasonable and comparable, the Director *may* take into consideration any factors the Director considers relevant, including...⁵

Comment 3: Related to §1230.3(a) above, subsection “b” again gives the Director sole discretion on which factors to consider when determining whether compensation is reasonable and comparable.

(c) *Withholding of compensation.* During a review under paragraph (a) of this section, the Director *may* require a regulated entity or the Office of Finance to withhold any payment, transfer, or disbursement of compensation...⁶

Comment 4: As noted in comment 1 above, since the Director already has discretion on when he “may” review the executive compensation of a regulated entity, subsection “c” gives him even further discretion on whether to require a regulated entity to withhold a payment.

These examples show how using the word “may” in the proposed rule grants the Director rights of discretion, rather than affirmative duties. This difference is significant in that the Director may essentially decide as he pleases, with little or no oversight of his own choices. In a perfect world, this would not be a concern, since the Director would always act in the agency and public’s best interests. However, in a worst case scenario, how would the intent of this proposed rule be ensured if the Director purposely or unintentionally fails to prohibit excessive executive compensation? For instance, if the Director simply “may” take the factors listed in §1230.3(b) into account before he makes his determination, who is to say that he really considers any factors at all?

Not to be cynical, but the proposed rule should be constructed in a matter as to prevent and adequately safeguard against these types of loopholes. Therefore, in order to provide

⁴ *Id.* at §1230.3(a) (emphasis added).

⁵ *Id.* at §1230.3(b) (emphasis added).

⁶ *Id.* at §1230.3(c) (emphasis added).

constructive criticism, I suggest that the language in the proposed rule be amended to narrow the scope of the Director’s discretion in the following manner:⁷

§ 1230.3 Prohibition and withholding of executive compensation.

(a) *In general.* The Director **must** review the compensation arrangements for any executive officer of a regulated entity or the Office of Finance **at least annually**, and shall prohibit the regulated entity or the Office of Finance from providing compensation to any such executive officer that the Director determines is not reasonable and comparable with compensation for employment in other similar businesses... involving similar duties and responsibilities.

(b) *Factors to be taken into account.* In determining whether compensation provided by a regulated entity or the Office of Finance to an executive officer is not reasonable and comparable, the Director **must** take into consideration any factors the Director considers relevant, including...

2. Prohibition of compensation-setting

While the Director’s discretion should be narrowed in some ways (e.g. as described in the previous section), it should be broadened in others to increase the efficiency of the FHFA’s oversight of executive compensation. As written, section 1230.3(d) of the proposed rule currently prohibits the Director’s ability to “prescribe or set a specific level or range of compensation for executives of regulated entities.”⁸ I argue that if this provision were modified to allow for discretion from the Director, it would actually enhance the oversight of executive compensation, and thus contribute in fulfilling the overall intent of the rule.

To explain, if the Director already uses certain factors to determine whether compensation of an executive officer is *not* reasonable and comparable, he should be able to use those same factors to determine what compensation *is* reasonable and comparable. In essence, in the process of making a determination of what compensation is not reasonable and comparable, he has already deduced what compensation would be fair (i.e. compensation paid at similar institutions for similar duties). Therefore, since the Director has already done a fair compensation analysis, it would be more efficient and save time for both the FHFA and regulated entities to not have to repeat the same analysis again when attempting to correct a compensation violation found during the Director’s initial review.

In light of this finding, I propose that the language in provision 1230.3(d) should be modified as follows:⁹

§ 1230.3 Prohibition and withholding of executive compensation.

(d) *Prohibition of setting compensation by Director.* In carrying out paragraph (a) of this section, the Director **may** prescribe or set a specific level or range of compensation.

⁷ NOTE: Changes in the language of the proposed rule are identified by the color **blue**.

⁸ Executive Compensation, *supra* at §1230.3(d).

⁹ NOTE: Changes in the language of the proposed rule are identified by the color **blue**.

3. Inadequate consequences for failure to comply

In order to be taken seriously, all statutes and rules should be constructed with clear and unambiguous consequences for their violation. To do otherwise would render a statute or rule meaningless by stripping it of any enforcement power. While the proposed rule has a “compliance” provision under section 1230.7, it lacks assurance that any regulated entity who violates it will face certain consequence or penalty. To illustrate this point, I cite the following language in the proposed rule:

§ 1230.7 Compliance.

Failure by a regulated entity or the Office of Finance to comply with the requirements of this part may result in supervisory action by FHFA. Such action may be taken in the form determined appropriate by the Director and may be taken...¹⁰

As you can see, relating back to an earlier argument, the use of the word “may” merely grants the Director a *right* to enforce this rule, rather than impose an *affirmative duty*. In that case, if the Director found that a regulated entity was in violation of this rule, he would be free to choose whether or not to impose any kind of penalty. How would the intent of this proposed rule and interests of justice be served if the Director purposely or unintentionally failed to justly penalize regulated entities for failing to comply? Moreover, what incentive would regulated entities have to comply with this rule if they knew there was a possibility that they would never be punished for failing to do so?

In light of these concerns, I recommend that the language in this section be modified to narrow the scope of the Director’s discretion in the following manner:¹¹

§ 1230.7 Compliance.

Failure by a regulated entity or the Office of Finance to comply with the requirements of this part will result in supervisory action by FHFA. Such action will be taken in the form determined appropriate by the Director and may be taken...

B. The Importance of Ensuring that Executive Compensation is Reasonable and Comparable

One of the foremost reasons that the FHFA was established was to ensure that the prudential operations of Fannie Mae, Freddie Mac, and the 12 other government-sponsored Banks continually run consistent with the public interest.¹² Facing one of the most drastic economic recessions since the great depression, today, more than ever, the people of this country need to be assured that their government is working for them.

¹⁰ Executive Compensation, *supra* at §1230.7 (emphasis added).

¹¹ NOTE: Changes in the language of the proposed rule are identified by the color blue.

¹² Executive Compensation, *supra* at “Background.”

According to the latest data from the U.S. Census Bureau, the real median household income in the United States was just \$48,201 in 2006.¹³ Furthermore, in that same year, 50.5% of the country's entire income belonged to merely 20% of the population, while just 26.5% of the income was earned by 60% of the population.¹⁴ I bring these numbers to light only to stress the fact that the executives of the government-sponsored enterprises are probably already earning more than they should in comparison to the rest of the hard-working public.

It is therefore in the public interest for the FHFA to have adequate procedures and safeguards in place to ensure that executive compensation is and continues to stay reasonable and comparable. It is my hope and desire that you and the FHFA will seriously consider in your deliberations all of the issues that I have discussed throughout this letter.

Respectfully,

Andrew Gregory-Mabrey

¹³ DeNavas-Walt, Carmen, Bernadette D. Proctor, and Jessica Smith, U.S. Census Bureau, Current Population Reports, P60-233, *Income, Poverty, and Health Insurance Coverage in the United States: 2006*, U.S. Government Printing Office, Washington, DC, 2007 at 4.

¹⁴ *Id.* at 9.