May 15, 2014

Alfred M. Pollard, General Counsel
Attn: Comments/RIN 2590-AA59
Federal Housing Finance Agency("FHFA")
Constitution Center, Eighth Floor (OGC)
400 7th Street SW
Washington, DC 20024

Dear Alfred,

Fannie Mae (the "Company") is pleased to submit these comments in response to FHFA's Notice of Proposed Rulemaking on Responsibilities of Boards of Directors, Corporate Practices, and Corporate Governance Matters.

The Company respectfully acknowledges the Company's conservatorship status and that FHFA, as Conservator of the Company has "succeed[ed] to ... all rights, titles, powers, and privileges of the [Company] and of any stockholder, officer, or director of [the Company] with respect to [the Company] and the assets of [the Company]."[1] The Company further acknowledges that the Conservator, pursuant to an order dated November 24, 2008, directed that, among other things, "the directors of Fannie Mae serve on behalf of the Conservator and shall exercise authority as directed by the Conservator."[2] Thus, the Company's directors serve on behalf of the Conservator and exercise their authority as directed by and with the approval, where required, of the Conservator, and the Company's directors have no fiduciary duties to any person or entity except to the Conservator. The Company's directors are not obligated to consider the interests of the Company, or the holders of Company securities, unless specifically directed to do so by the Conservator.

In light of the fact that the proposed regulation on Responsibilities of Boards of Directors, Corporate Practices, and Corporate Governance Matters was published for public comment by FHFA in its role as regulator of the Company, the comments provided herein are for FHFA's consideration as the prudential regulator of the Company (as opposed to its role as Conservator), as FHFA considers the adoption of such proposed regulation. We understand that, as with the current corporate governance regulation, the duties or authorities provided in the proposed regulation will be applicable to the Company in conservatorship as modified by the Conservator, and only to the extent not inconsistent with Conservator directives, orders or guidance.

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[1] *See* Section 1367(b)(2)(A) of the Federal Housing Enterprise Financial Safety and Soundness Act of 1992 (12 U.S.C. § 4501 et seq.), as amended by the Federal Housing Finance Regulatory Reform Act of 2008 (which is a part of the Housing and Economic Recovery Act of 2008 (Pub L. No. 110-289, 122 Stat. 2654)).
[2] Conservator Order Regarding Functions and Authorities of the Board of Directors and its Members, Order No. 2008-006, dated November 24, 2008. The Company also acknowledges the Conservator's letter of instruction to the Board dated November 15, 2012, which revised and replaced the 2008 letter of instruction.

As you know, in accordance with Section 1710.10(b) of the FHFA regulation on corporate governance (12 CFR 1710.1 et seq.), the Company has elected to follow Delaware law for corporate governance, to the extent not inconsistent with our Charter Act and other Federal laws. The proposed regulation would appear in several instances to expand the role and duties of the Board of Directors beyond the standards established by Delaware General Corporation Law (DGCL), creating new duties exceeding those of other financial institutions. This expansion of duties, and exposure to additional personal liability, could make it difficult to recruit and retain talented directors. Of particular relevance is the apparent expansion of the duty of care. Under Delaware law, the duty of care requires that directors "'inform themselves, prior to making a business decision, of all material information reasonably available to them.'"[3] Directors also have a duty to exercise care in overseeing the conduct of corporate employees, and Delaware courts have found that liability can be imposed on directors in circumstances where: "(a) the directors utterly failed to implement any reporting or information systems or controls; or (b) having implemented such a system or controls, consciously failed to monitor or oversee its operations thus disabling themselves from being informed of risks or problems requiring their attention."[4]

In fulfilling his or her duties under Delaware law, a director may rely in good faith on "the records of the corporation and upon such information, opinions, reports or statements presented to the corporation by any of the corporation's officers or employees ... or by any other person as to matters the member reasonably believes are within such other person's professional or expert competence and who has been selected with reasonable care by or on behalf of the corporation." (DGCL sec. 141(e)). Under well-established Delaware law, the duty of care and the related oversight responsibility differs from managing the day-to-day operations of a company. Instead, the duty is to provide oversight regarding the establishment of systems and controls related to the day-to-day operations and to obtain ongoing information and reporting regarding the systems and controls. Similarly, while the Delaware duty of care requires that directors obtain and inform themselves regarding available material information prior to making a decision, the duty of care does not require that directors be day-to-day business and operational experts on each matter presented to the Board for consideration. So, for example, each director of a company can meet the duty of care standard established by Delaware law without being an expert in accounting practices or in the monitoring of the testing of risk controls at financial services organizations; directors can rely on the information and expertise of employees and professionals.

We seek clarification that the standards in the proposed regulation are not intended to expand the well-established Delaware law fiduciary duties of the directors (which, as noted above, are owed solely to the Conservator). We also seek clarification that, under the proposed regulation, the responsibility for day-to-day operations and management would remain with the senior

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[3] Smith v. Van Gorkom, 488 A.2d 858, 872 (Del. 1985) (citing Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984)). See also, In re Caremark International Inc. Derivative Litigation, 698 A.2d 959, 971 (Del. Ch. 1996) (failure of Board oversight requires a "sustained or systemic failure of the board to exercise oversight -- such as an utter failure to attempt to assure a reasonable information and reporting system exists," also characterized as a "demanding test.")

[4] Stone v. Ritter, 911 A.2d, 362, 370 (Del. 2006).

management team, while responsibility for *oversight* of management's activities would reside with the Board.

To provide clarification, we request that FHFA consider revisions to the proposed regulation as follows:

Consider Revising:

§1239.2 — Definitions

Executive officer means the chairperson or vice chairperson of the board of directors of an Enterprise; and, with respect to any regulated entity, the chief executive officer, chief financial officer, chief operating officer, president, any executive vice president, any senior vice president, and any individual with similar responsibilities, without regard to title, who is in charge of a principal business unit, division, or function, or who reports directly to the chairperson, vice chair person, chief operating officer, or chief executive officer or president of a regulated entity.

Comment:

Section 1239.20(a)(3) states that the chairperson of the board of directors "shall ... be a director of the Enterprise that is independent, as defined under the rules of the NYSE [New York Stock Exchange]" Under NYSE rules, "a director is not independent if the director is, or has been within the last three years ... an executive officer of the listed company."[5] Defining the chairperson of the board as an "executive officer" appears to cause a direct conflict with NYSE rules.

Proposed revision:

Executive officer means any member of the board of directors of an Enterprise who also is an employee of the Enterprise; and, with respect to any regulated entity, the chief executive officer, chief financial officer, chief operating officer, president, any executive vice president, any senior vice president, and any individual with similar responsibilities, without regard to title, who is in charge of a principal business unit, division, or function, or who reports directly to the chairperson, vice chairperson, chief operating officer, chief executive officer, or president of a regulated entity.

[5] NYSE Company Listed Manual §303A.02(b).

Consider Revising:

§1239.4 — Duties and responsibilities of directors

(a) Management of a regulated entity

The management of each regulated entity shall be vested in its board of directors. While boards of directors may delegate the execution of operational functions to officers and employees of the regulated entity, the ultimate responsibility of each entity's board of directors for that regulated entity's management is non-delegable. The board of directors of a regulated entity is responsible for directing the conduct and affairs of the entity in furtherance of the safe and sound operation of the entity and shall remain reasonably informed of the condition, activities, and operations of the entity.

Comment:

The first two sentences seem to expand the Board's role from one of oversight to becoming day-to-day managers of the Company and the routine conduct of all Company affairs. As previously discussed, the Board of Directors has a duty to provide oversight, but the duty of care does not require that Directors become day-to-day experts on every business matter that the Company encounters.

Proposed revision:

Delete the first two sentences above. The final sentence of §1239.4(a) is consistent with the current corporate governance regulation, and addresses the Board oversight and duty of care responsibilities appropriately by requiring that the Board be "responsible for directing the conduct and affairs of the entity in furtherance of the safe and sound operation of the entity and ... remain reasonably informed of the condition, activities, and operations of the entity." Similarly, §1239.4(c) also appropriately addresses practices necessary to fulfill the responsibility in §1239.4(a) by requiring that the Board have "in place adequate policies and procedures to assure its oversight of, among other matters, the following: (1) the risk management and compensation programs of the regulated entity; (2) the processes for providing accurate financial reporting and other disclosures and communications with stockholders; and (3) the responsiveness of executive officers in providing accurate and timely reports to FHFA and in addressing all supervisory concerns of FHFA in a timely and appropriate manner." Deleting the first two sentences of proposed §1239.4(a) will provide greater clarity and certainty regarding the Board's role; the remaining language in §1239.4 adequately defines the Board's responsibilities.

Consider Revising:

§1239.4 – Duties and responsibilities of directors

(b) Duties of directors

Each director of a regulated entity shall have the duty to: (1) Carry out his or her duties as director in good faith, in a manner such director believes to be in the best interests of the regulated entity, and with such care, including reasonable inquiry, as an ordinarily prudent person in a like position would use under similar circumstances; (2) Administer the affairs of the regulated entity fairly and impartially …; (3) At the time of election, or within a reasonable time thereafter, have a working familiarity with basic finance and accounting practices, including the ability to read and understand the regulated entity's balance sheet and income statement and to ask substantive questions of management and the internal and external auditors; (4) Direct the operations of the regulated entity in conformity with the requirements set forth in the authorizing statutes, Safety and Soundness Act, and this chapter, and (5) Adopt and maintain in effect at all times bylaws governing the manner in which the regulated entity administers its affairs. Such bylaws shall be consistent with applicable laws and regulations administered by FHFA, and with the body of law designated for the entity's corporate governance practices and procedures."

Comment:

This responsibility seems to require duties that both overlap with and conflict with the duties owed under our Charter Act and under the DGCL. As previously discussed, the Company has elected to follow Delaware law for corporate governance to the extent not inconsistent with our Charter Act and other Federal laws. In addition, the Board has adopted, in compliance with NYSE requirements, Corporate Governance Guidelines and a Director Code of Conduct and Conflicts of Interest Policy.[6]

With respect to proposed §1239.4(b)(2), at the Company, these requirements are addressed through independence testing and Board member compliance with the Policy and NYSE requirements regarding independence.[7] Adding new requirements that may be interpreted in a manner inconsistent with the Policy and NYSE requirements would create unnecessary ambiguity and inconsistency in an area where there is well-established regulation and compliance.

[6] NYSE Company Listed Manual §§ 303A.09 and 303A.10.
[7] NYSE Company Listed Manual § 303A.02.

With respect to proposed §1239.4(b)(3), this is a new requirement that does not align with our Charter Act or other applicable regulations and laws. Pursuant to our Charter Act, the Company is required to have Board members with the following qualifications: "at least one person from the homebuilding industry, at least one person from the mortgage lending industry, at least one person from the real estate industry, and at least one person from an organization that has represented consumer or community interests for not less than 2 years or one person who has demonstrated a career commitment to the provision of housing for low-income households."[8] In addition, under NYSE audit committee requirements, "each member of the audit committee must be financially literate," as such qualification is interpreted by the Board in its independent judgment.[9] Additionally, "at least one member of the audit committee must have accounting or related financial management expertise."[10] The NYSE provides that a director who satisfies the definition of "audit committee financial expert" as set forth in applicable SEC requirements[11] can be presumed to meet this requirement.[12] As we read the requirements of proposed §1239.4(c)(3), the proposed regulation could be interpreted to suggest that each Board member would have to be an audit committee financial expert. Such a requirement may pose a challenge in recruiting new Board members who meet both our Charter Act requirements and the audit committee financial expert standards, and may limit our ability to retain the full diversity of backgrounds and perspectives that we currently have represented on the Board. We believe that the existing requirement that Board members comply with the current applicable legal and regulatory regime is sufficient to provide for a Board that as a whole is composed of a diverse blend of skills, expertise, and backgrounds.

Proposed revision:

Each director of a regulated entity shall have the duty to comply with the applicable authorizing statutes; other Federal laws, rules, and regulations; and, to the extent not inconsistent with the foregoing, the corporate governance practices and procedures relating to director duties in the jurisdiction whose law the regulated entity has elected to follow pursuant to §1239.3(b).

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[8] Federal National Mortgage Association Charter Act §308(b), 12 U.S.C. § 1723(b).
[9] NYSE Listed Company Manual Commentary to Section 303A.07(a).
[10] Ibid.
[11] Item 407(d)(5)(ii) of SEC Regulation S-K.
[12] NYSE Listed Company Manual Commentary to Section 303A.07(a).

Consider Revising:

§1239.5 — Board committees

(d) Frequency of meetings

> Each committee ... shall meet with sufficient timeliness as necessary in light of relevant conditions and circumstances to fulfill its obligations and duties.

Comment:

This responsibility sets an unclear standard regarding number and frequency of committee meetings. As previously discussed, the duty of care under Delaware law requires that Directors "inform themselves, prior to making a business decision, of all material information reasonably available to them."[13] This standard for timeliness ("prior to making a business decision") is appropriate and allows for discretion in the number and frequency of committee meetings, provided that any other applicable requirements are met.

Proposed revision:

When scheduling meetings, each committee shall comply with the requirements found elsewhere in this regulation; the applicable authorizing statutes; other Federal laws, rules, and regulations; and, to the extent not inconsistent with the foregoing, the corporate governance practices and procedures of the jurisdiction whose law the regulated entity has elected to follow pursuant to §1239.3(b).

Consider Revising:

§1239.11 – Risk management

(c) Risk committee structure and requirements.

(2) The risk committee shall: (i) be chaired by a director not serving in a management capacity of the regulated entity; (ii) have at least one member with risk management expertise that is commensurate with the regulated entity's capital structure, risk profile, complexity, activities, size, and other appropriate risk-related factors; (iii) have committee members with an understanding of risk management principles and practices relevant to the regulated entity; (iv) have members with experience developing and applying risk management practices and procedures, measuring and identifying risks, and monitoring the testing risk controls with respect to financial services organizations, (v) fully document and maintain records of its meetings, including its risk management decisions and

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[13] 488 A.2d 858, 872 (Del. 1985).

recommendations; and (vi) report directly to the board and not as part of, or combined with, another committee.

Comment:

With respect to proposed §1239.11(c)(2)(i)-(iv), these are new requirements for Board members that, as previously discussed, do not align with our Charter Act or other applicable regulations and laws. In addition, as drafted, these proposed requirements differ substantively from the Federal Reserve's newly finalized Enhanced Prudential Standards for Bank Holding Companies and Foreign Banking Organizations.[14] To the extent that FHFA issues requirements for risk committee members and risk committees that differ from requirements that the Federal Reserve has issued, it may pose a challenge to retaining Board members and recruiting new Board members for the Company. We believe that, should FHFA decide to issue new requirements for members of risk committees, they should mirror the requirements for risk committees recently issued by the Federal Reserve.

Proposed revision:

(2) The risk committee shall: (i) fully document and maintain records of its meetings, including its risk management decisions and recommendations; and (ii) report directly to the board and not as part of, or combined with, another committee.

(3) The risk committee must: (i) include at least one member having experience in identifying, assessing and managing risk exposures of large, complex financial firms; and (ii) be chaired by a director who: (A) is not an officer or employee of the regulated entity and has not been an officer or employee of the regulated entity during the previous three years; (B) is not a member of the immediate family, as defined in §1239.2, of a person who is, or has been within the last three years, an executive officer of the regulated entity, as defined in §1239.2; and (C)(1) is an independent director under Item 407 of the Securities and Exchange Commission's Regulation S-K (17 CFR 229.407(a)), if the regulated entity has an outstanding class of securities traded on an exchange registered with the U.S. Securities and Exchange Commission as a national securities exchange under section 6 of the Securities Exchange Act of 1934 (15 U.S.C. 78f) (national securities exchange); or (2) would qualify as an independent director under the listing standards of a national securities exchange, as demonstrated to the satisfaction of FHFA, if the regulated entity does not have an outstanding class of securities traded on a national securities exchange.

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[14] Federal Reserve Regulation YY, 12 C.F.R. § 252.

Additional Comments:

In response to FHFA's request for comments on matters specific to audit committees, we respectfully submit the following comments:

> Under our Charter Act and other FHFA regulations, the Company is subject to the Securities and Exchange Commission's and New York Stock Exhange's requirements for audit committees. As previously discussed, these requirements are comprehensive and well-established regarding the duties and responsibilities of audit committees; thus additional regulations relating to audit committees would not enhance the function of audit committees. Should FHFA decide to issue additional regulations regarding audit committees, we respectfully submit that the new regulations should be drafted and structured so that they are not inconsistent with the other audit committee regulations to which the Company is subject. With regard to existing and any future FHFA oversight of audit committees, the least complex approach is to address all such requirements within one reference document. The Company would propose addressing all audit committee requirements entirely within the Prudential Management and Operations Standards,[15] and incorporating by reference the existing regulatory framework provided by the NYSE and SEC, which would provide the most clarity and certainty.

In bringing these particular provisions of the proposed regulations to your attention, Fannie Mae is cognizant that an expansion of the duties of the Board may impact the Company's ability to recruit and retain qualified Board members. Eligible individuals might be concerned about the consequences of an administrative enforcement action should they fail to fulfill the expanded duties required in the provisions cited.

Lastly, Fannie Mae respectfully suggests that the following sentence be deleted from the Supplementary Information section, so as to avoid confusion: "Under [the OFHEO indemnification provisions at 12 CFR 1710.20], FHFA could limit or prohibit indemnification payments to any person found to have violated any law or regulation, breached any material elements of the entity's bylaws or code of conduct, or engaged in grossly negligent actions." The sentence appears much broader in scope than the OFHEO regulation from which it purportedly derives, which applies only to board members and executive officers. Further, the listed grounds for limiting or prohibiting indemnification (e.g., breach of an entity's code of conduct) extend far beyond what is contemplated by Delaware law, Fannie Mae's by-laws, or Fannie Mae's indemnification agreement, which may complicate renewal of the company's D&O policy.

[15] 12 C.F.R. §1236.

Should any additional information be required as you consider the final rule, please do not hesitate to contact me.

Sincerely,

Christine E. Reddy
Vice President, Deputy General Counsel, and Deputy Corporate Secretary