



Federal Home Loan Bank of Pittsburgh

May 25, 2006

Federal Housing Finance Board
1625 Eye Street, NW
Washington, DC 20006
ATTENTION: PUBLIC COMMENTS

RE: Regulatory Information Number (RIN) 3069-AB31 and
docket number (e.g., 2006-04)

The Federal Home Loan Bank of Pittsburgh ("Bank") welcomes the opportunity to comment on the proposed rule changes designed to enhance corporate governance at the Federal Home Loan Banks ("FHLBanks") through improving the director election process consistent with the cooperative nature of the FHLBanks. While we appreciate that the proposal will permit better information to be provided to Bank members as they nominate and elect directors, we do not believe it provides sufficient optional flexibility consistent with best practices in corporate governance. We, therefore, encourage the Finance Board to provide more flexibility to the Boards of FHLBanks with respect to the nomination and election phases of the process.

I. The Bank's Commitment to Good Governance

The Board of Directors of the Bank has been a Bank System leader in staying abreast of and following best practices in corporate governance long before corporate governance was a focus of policymakers. The Bank was one of the first FHLBanks, if not the first, to establish a board committee dedicated solely to the role of the board in the governance of the institution, including the administration of a self-assessment process. Every Director of the Bank is a member of the National Association of Corporate Directors, and through that membership receives current information on emerging developments in best practices in corporate governance. The Governance Committee also ensures that Directors receive continuous training in the area of corporate governance.

The Bank has long recognized that director selection is one of the most important elements in achieving good corporate governance. To this end, the Bank developed a list of desired characteristics for individual directors as well as a list of core competencies for the entire board. The Bank's Governance Committee has routinely reviewed these lists to make sure they stay current in addressing the needs of the board. The Bank shares these lists with its members during both the nomination phase as well as the balloting phase of the election process. These lists were embraced by the Finance Board at the All Directors Conference in 2002.

II. The Finance Board's Commitment to Good Governance

The Bank applauds the Finance Board's commitment to support enhancing corporate governance at the FHLBanks, as reflected in the following quotes from the release regarding the proposed rule and the accompanying press release:

"One way the Finance Board can help ensure the safety and soundness of the Banks is to use its regulatory authority to enable the Banks to establish a process whereby capable and skilled persons may be nominated and elected to their board of directors, so that each Bank's board of directors will possess the aggregate skills needed to provide strong oversight."

"The Banks need and deserve a governance structure commensurate with the increased level of sophistication in their operations. As cooperatives, the members own the Banks and control the outcome of director elections. But in today's environment, the members need full information about the skills and qualifications most needed by their particular Bank as they decide who to nominate and ultimately elect to run their institutions."

The proposed rule would provide the option to each FHLBank to implement three additional practices to support the election process. First, 12 CFR 915.9(a) would permit each FHLBank, if it so chooses, to perform an annual assessment of the skills and experience, which if present in new directors, would enhance the capabilities of the board of directors. Second, 12 CFR 915.6(a)(3) would permit each FHLBank to include with the notice of an election to each member a brief statement describing the skills and experience that the FHLBank has identified as most likely to add strength to its board of directors. The proposal indicates that the skills or experience could include, among other things, the areas of financial management and/or financial accounting, hedging, risk management, capital markets, disclosure required of issuers of securities, and housing finance. Finally, 12 CFR 915.8(a)(1) would permit each FHLBank, as part of the information on each ballot about each nominee, to describe briefly that nominee's skills and experience.

While these proposed changes do provide for some improvement in the director selection process, it is the position of the Board of the Bank that they do not go far enough. Some of the best information that can be provided to the membership, in regard to an election of directors, is a thoughtful analysis of the skills and experiences of the candidates and whether the Board governance committees of the FHLBanks believe the candidates satisfy the range of skill sets needed to provide the most effective board, in the opinion of the existing board of that FHLBank. The proposed rule does not explicitly permit this type of information to be shared with the members during the balloting phase of the election process. As a result, we believe the rule should be revised to allow for better information to be shared with the members as they elect the directors that will oversee the collective \$1 trillion

FHLBank System. This practice would be consistent with the cooperative nature of the FHLBanks.

The remaining sections of this comment letter reference best practices in corporate governance relating to the director nomination and election process, demonstrate that other large cooperatives are embracing these practices, and conclude by setting forth some concepts the Finance Board should consider, including in the final rule, that would improve the process for director election, and therefore, enhance the governance of the Bank System.

III. Corporate Governance Best Practices

Best corporate governance practices related to the nomination and election of directors provide for an active and engaged role for the board of directors, particularly the independent directors or a committee of independent directors, in identifying director nominees and communicating that information to those voting on the director nominees. For example, the New York Stock Exchange ("NYSE") and NASDAQ each have included requirements relating to the selection of directors in their listing standards. In addition, the Business Roundtable, an association of chief executive officers of leading U.S. corporations, has drafted several principles and commentary relating to corporate governance best practices. The Business Roundtable's "The Nominating Process and Corporate Governance Committees: Principles and Commentary" calls for additional board involvement in the identification, evaluation, and recommendation of director candidates for election. These best practices illustrate why the Finance Board proposal does not permit best practices to be achieved and why it should provide sufficient flexibility to Federal Home Loan Banks with respect to the nomination and election of Bank directors.

A. Corporate Best Practices

- Establish Qualifications/Criteria
 - The NYSE and NASDAQ listing standards require boards to establish procedures to identify and evaluate candidates and written criteria that lay out the factors considered when evaluating candidates.
 - The Business Roundtable also recommends that criteria be established for board membership.
- Nominating Committee that Establishes Criteria
 - The NYSE requires corporations to have nominating committees that review and recommend director nominations to the full board.
 - The NYSE requires the Committee to have a charter that addresses the committee's purpose and responsibilities, which, at minimum, must be to identify individuals qualified to become board members, consistent with criteria approved by

the board and to select or recommend that the board select the director nominees for the next annual meeting of shareholders.

- NASDAQ permits director nominees to be selected or recommended for board selection by a majority of independent directors or a nominations committee.
- The Business Roundtable's Principles recommend that each corporation have a nominating/governance committee whose responsibilities include: (1) identifying, evaluating, and recommending director candidates to the board; and (2) establishing written criteria for board and board committee membership.
 - When establishing written criteria for director candidates, the nominating committee should consider the background and expertise of the existing board members and the specific needs of the board. Based on these criteria, the committee should identify director candidates, review their qualifications and any potential conflicts with the corporation's interests, and recommend candidates to the board. The committee should also assess the contributions of current directors in connection with their re-nomination.
 - The committee should strive to compose the board of a mix of talents, experience, expertise, and perspectives. The committee should consider candidates from a range of backgrounds.
- Annual Review
 - The Business Roundtable principles provide for an annual evaluation of the board and board committee performances, along with the contributions of individual directors, to be supervised by the nominating/corporate governance committee.

B. Cooperatives Embrace Board Involvement in Election of Directors

The USDA recently conducted a survey of 433 cooperatives to learn more about how cooperatives select and nominate candidates for their boards.

- Out of 376 cooperatives reporting on nominating committee composition, 163 (43 percent) use only non-director members on the committee. Another 131 (35 percent) use a mix of directors and non-directors, while 82 (22 percent) have only directors on the nominating committee.

The National Cooperative Business Association ("NCBA"), the leading association representing cooperatives of all types, undertook a similar survey

to reveal the corporate governance practices of cooperatives in the United States. The results were published in September 2005, in a report titled "Governance Practices of Cooperative Boards." The following are excerpts from the survey:

- **Nominations and Elections**
 - Approximately two-thirds of responding co-ops indicated that board candidates were nominated by a nominating committee, while about 50 percent indicated board candidates were also nominated by co-op members at large (dual processes are common).
- **Source of Nominations**
 - Responses indicated that co-ops often had more than one method of nominating board candidates. Sixty-seven percent of responding co-ops said that board candidates were nominated by a nominating committee. Fifty-one percent indicated that board candidates were nominated by members. Other nomination practices were used less frequently. Twelve percent indicated nominations were made by the board as a whole, three percent by the board chair, four percent by the CEO or general manager, and four percent by self-nomination.
- **Nominating Committees**
 - Among responding co-ops with a nominating committee, 61 percent said committee members were selected by the board. Twenty-six percent said nominating committee members were selected by the board chair.

IV. Additional Flexibility In The Proposed Finance Board Proposal Is Necessary

A. Problem with the Proposal

The proposed rule permits the FHLBanks to annually assess and identify the needed skills/experience on their boards, but then does not permit the Boards of the FHLBanks to identify and inform the voting members about the most appropriate candidates. Thus, the proposed rule would permit the FHLBanks' Boards to identify the needs of their boards and to communicate to the members the skills/experience that each candidate has, but then would not permit that board to tell its members who, in the judgment of the board, brings these skills necessary to best complement the skills represented by the existing board.

B. Consider Expanding the Proposal

The Finance Board should consider expanding the optional authority of the boards of the FHLBanks to participate in the nomination and balloting phases of the election process. There are many ways to enhance the flexibility of the rule to allow each FHLBank board to tailor its involvement to meet the needs of their FHLBank and to complement the practices of their membership. The Finance Board should consider including some of the following in an expanded list of authorized activities for boards of directors:

- At a minimum, the Finance Board should permit the FHLBanks to indicate, on the ballot or elsewhere, which nominees in the judgment of the board provide the skill set that would best enhance the ability of the board to govern the Bank. While the proposed rules allow the FHLBanks to list what skills/experience the nominees have, this does not go far enough.
- Permit the boards of the FHLBanks to recommend to the membership certain individuals to be nominated.
- Permit the boards of the FHLBanks to actually recommend certain nominees for election.
- Permit the boards of the FHLBanks to establish a Nominating Committee comprised of a combination of member stockholders and board directors to review the eligibility and qualifications of nominees and to recommend one or more candidates for each open seat to be elected by the members. The charter of the Nominating Committee for CoBank, a \$34 billion co-op in the Farm Credit System, is a good example of this approach.

C. Rationale

We strongly believe that the Finance Board should revise the rule to allow for more flexibility and involvement of the directors in the nomination, qualification, and election of directors to the boards of the FHLBanks.

- At a minimum, our suggested expansion would give the boards of the FHLBanks the optional authority to give better information to their members/shareholders.
- Such information will give voting members the benefit of additional disclosure about those individuals who may be selected to oversee the \$1 trillion FHLBank System. And, this knowledge will come from those individuals—current board members—who have the knowledge to determine what skills/experience are necessary to make their individual boards more effective.

- Providing increased disclosure will not lead to the FHLBanks controlling the election process; the information will simply lead to better informed member voters.
- This is not a request for proxy authority.
- Best corporate governance practices are relevant to the FHLBanks, even if they are cooperatives.
 - The FHLBanks are similar in size to major corporations.
 - The FHLBanks are now registered with the SEC, like all public companies.
 - FHLBanks already have adopted many best corporate governance practices such as Audit and Compensation Committees.
- Our suggested expansion is consistent with the practices of many cooperative boards.

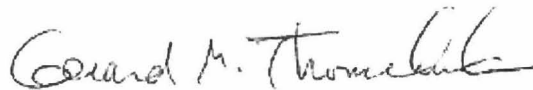
V. Conclusion

The Pittsburgh Bank fully supports the efforts of the Finance Board to improve the director selection process and, therefore, improve the governance processes in the Bank System. However, the proposed rule, although it does permit the Bank to provide the members with some additional information about the candidates for open board seats, should be revised further to provide more flexibility to the FHLBanks with respect to the information provided during both the nomination and balloting phases of the election process.

Sincerely,



Marvin N. (Skip) Schoenhals
Chairman of the Board



Gerard M. Thomchick
Chairman, Governance Committee

cc: The Honorable Ronald A. Rosenfeld
The Honorable Alphonso Jackson
The Honorable Alicia R. Castaneda
The Honorable Franz S. Leichter
The Honorable Allan J. Mendelowitz