Federal Housing Finance Agency
Office of Inspector General

FHFA Could Enhance the Efficiency of the Agency's Oversight of Enterprise Executive Compensation by Ensuring Sufficient Human Capital Resources and Updating Procedures

Evaluation Report • EVL-2022-003 • September 27, 2022

EVL-2022-003

September 27, 2022

Executive Summary

For nearly 30 years, the Federal Housing Finance Agency (FHFA) and its predecessor agency, the Office of Federal Housing Enterprise Oversight, have been required by statute to oversee the compensation provided to executive officers of Fannie Mae and Freddie Mac (collectively, the Enterprises). Under the Federal Housing Enterprises Financial Safety and Soundness Act of 1992, as amended (the Safety and Soundness Act), the FHFA Director must prohibit the Enterprises from providing executive compensation that is "not reasonable and comparable with compensation for employment in other similar businesses (including other publicly held financial institutions or major financial services companies) involving similar duties and responsibilities." In addition, the Housing and Economic Recovery Act of 2008 granted the FHFA Director broad authority to operate the Enterprises as their conservator, which includes the review and approval of executive compensation. As the Enterprises' conservator, FHFA has fulfilled a dual role in many of its compensation reviews.

In January 2014, the Agency issued a regulation (the Executive Compensation Rule) that defined the requirements and process for its review of executive compensation. The Executive Compensation Rule's definition of "reasonable" established factors for the Agency's review of Enterprise executive compensation, including the duties and responsibilities of the position, "added or diminished risks, constraints, or aids in carrying out the responsibilities of the position," and the performance of the regulated entity or employee with respect to goals, supervisory guidance, and legal compliance.

FHFA's executive compensation staff, currently within the Division of Conservatorship Oversight and Readiness (DCOR), have primary responsibility for assessing whether proposed compensation actions for Enterprise executives are not reasonable and comparable. The Deputy Director of DCOR and other agency stakeholders review and approve the executive compensation staff's recommendation prior to the FHFA Director's or Chief of Staff's decision on the matter. Since 2019, the leadership of the Enterprise executive compensation function has changed twice, most of the staff performing the reviews have turned over, and the function has been moved three times among three divisions and the Office of the Director.

This evaluation assesses FHFA's current framework for reviewing Enterprise executive officer compensation to meet the Agency's statutory, regulatory, and conservatorship requirements.

Our evaluation found that, following significant leadership and structural changes, FHFA's procedures for executive compensation reviews do not

EVL-2022-003

September 27, 2022

reflect the compensation review function's current structure and roles and responsibilities. The procedures also do not describe the scope of FHFA's review or prescribe the specific analytical work to be performed. As a result, the procedures do not define the Agency's minimum requirements for reviews of Enterprise executive compensation, such as the factors that must be applied during the review of whether proposed compensation is not reasonable and comparable. Nor do they set forth detailed requirements for the documentation of the compensation review and analysis in staff analysis memoranda. DCOR officials acknowledged the need to update the existing procedures and plan to complete revisions by the end of October 2022.

We also found that DCOR has not determined the necessary level of staffing to ensure the efficient execution of the Agency's statutory responsibility for oversight of Enterprise executive compensation. Compensation staff reported a backlog of compensation reviews and the division's Deputy Director acknowledged that they are overworked. He advised us that he plans to review staffing needs.

We make three recommendations in this report to address our findings. In a written management response, FHFA agreed with our recommendations.

This report was prepared by Jon Anders, Lead Program Analyst, with assistance from Angela Choy, Assistant Inspector General for Evaluations. We appreciate the cooperation of FHFA staff, as well as the assistance of all those who contributed to the preparation of this report.

This report has been distributed to Congress, the Office of Management and Budget, and others and will be posted on our website, www.fhfaoig.gov, and www.oversight.gov.

/s/

Kyle D. Roberts
Deputy Inspector General for Evaluations

TABLE OF CONTENTS ....

ABBREVIATIONS

DCOR	Division of Conservatorship Oversight and Readiness
DER	Division of Enterprise Regulation
Enterprises	Fannie Mae and Freddie Mac, collectively
Executive Compensation Rule	12 C.F.R. Part 1230 – Executive Compensation Rule
FHFA	Federal Housing Finance Agency
GAO	Government Accountability Office
Green Book	GAO's Standards for Internal Control in the Federal Government
OEC	Office of Executive Compensation
OIG	Office of Inspector General
OPM	Office of Personnel Management
Safety and Soundness Act	Federal Housing Enterprises Financial Safety and Soundness Act of 1992

BACKGROUND

The Compensation of Executive Officers at Fannie Mae and Freddie Mac Has Been Subject to Supervision and Limitation for Nearly 30 Years

For nearly 30 years, FHFA and its predecessor agency, the Office of Federal Housing Enterprise Oversight, have been required by statute to oversee the compensation provided to the Enterprises' executive officers. Under the Safety and Soundness Act, the FHFA Director must prohibit the Enterprises from providing executive compensation that is "not reasonable and comparable with compensation for employment in other similar businesses (including other publicly held financial institutions or major financial services companies) involving similar duties and responsibilities."[1] When Congress created FHFA in 2008, it amended the Safety and Soundness Act to allow the Director to "take into consideration any factors the Director considers relevant" when determining whether compensation is "not reasonable and comparable."[2] However, in performing this supervisory review, the Director may not set a specific level or range of compensation for Enterprise executives.[3]

FHFA has implemented its supervisory authority over executive compensation through the issuance of regulations and orders. In January 2014, the Agency issued a regulation (the Executive Compensation Rule) that defined the requirements and process for its review of executive compensation. It requires that each Enterprise provide advance notice of certain compensation actions, such as hiring new executives for a term of six or more months or changes in the payment of annual compensation to executive officers.[4] It also defines the terms "executive officer,"[5] "reasonable," and "comparable."[6]

---

[1] Pub. L. No. 102-550, § 1318(a) (1992) (codified as amended at 12 U.S.C. § 4518(a)).

[2] 12 U.S.C. § 4518(b). The Safety and Soundness Act defined the term "Executive Officer," with respect to the Enterprises, as "the chairman of the board of directors, chief executive officer, chief financial officer, president, vice chairman, any executive vice president, and any senior vice president in charge of a principal business unit, division, or function." Pub. L. No. 102-550, § 1303(7) (1992) (codified at 12 U.S.C. § 4502(12)).

[3] 12 U.S.C. § 4518(d).

[4] 12 C.F.R. § 1230.3(d).

[5] FHFA expanded upon the Safety and Soundness Act's definition of an "executive officer" to include "any senior vice president, any individual in charge of a principal business unit, division, or function, and any individual who performs functions similar to such positions whether or not the individual has an official title." 12 C.F.R. § 1230.2.

[6] "Reasonable" compensation is compensation, "taken in whole or in part, that would be appropriate for the position and based on a review of relevant factors, including, but not limited to: (i) The duties and responsibilities of the position; (ii) Compensation factors that indicate added or diminished risks, constraints, or aids in carrying out the responsibilities of the position; and (iii) Performance of the regulated entity, the

In November 2014, the Agency issued an order to each Enterprise that set forth the information requirements for executive compensation requests, which it revised and replaced in 2018. Under the current order from 2018, the Enterprises must submit, among other things, relevant market data that supports the executive officer's proposed change in compensation and materials from boards of directors meetings where compensation decisions are made. In March 2022, FHFA issued new guidance to the Enterprises requiring more detailed information on their compensation consultants' benchmarking process for each proposed compensation action.[7]

Under FHFA's statutory and regulatory requirements, the Enterprises submit a variety of compensation actions for FHFA's review. These include all changes to compensation for executive officers, scoring of the annual Conservatorship Scorecard measures for determination of a portion of at-risk compensation, and requests for payouts of deferred salary earned in prior years.[8] During our review period of January 1, 2021, through April 13, 2022, FHFA received 65 compensation-related requests from the Enterprises—38 in 2021 and 27 in 2022.

FHFA's Authority, as Conservator, Over Enterprise Executive Compensation

The Housing and Economic Recovery Act of 2008 granted the Director broad authority to operate the Enterprises as conservator.[9] FHFA placed the Enterprises into conservatorship in

---

specific employee, or one of the entity's significant components with respect to achievement of goals, consistency with supervisory guidance and internal rules of the entity, and compliance with applicable law and regulation."

"Comparable" compensation means that the compensation "does not materially exceed compensation paid at institutions of similar size and function for similar duties and responsibilities."

12 C.F.R. § 1230.2.

[7] FHFA requested more information about, among other things, the methodology used for the benchmarking analysis, the benchmarking quality assessment, the peer group participants contained in the relevant market data, and discounts or premiums applied to the benchmark.

[8] Under the Enterprises' current executive compensation structure, fixed compensation accounts for 70% of each executive's total compensation and "at-risk" compensation accounts for the remaining 30%. Fixed compensation is comprised of base salary, which is paid on a recurring basis throughout the year and capped at $600,000 for every Enterprise executive, and deferred salary, which is payable in quarterly installments after a two-year deferral period. Half of the at-risk compensation (or 15% of total compensation) is based on FHFA's determination of how each Enterprise performed against FHFA's annual Conservatorship Scorecard measures; the other half is determined by the Enterprises, based on the Enterprise CEO's and board of directors' evaluation of an executive's performance against annual Enterprise Corporate Scorecard performance measures or other measures (for certain executives).

[9] Under the Housing and Economic Recovery Act of 2008, FHFA may "operate the regulated entity with all the powers of the shareholders, the directors, and the officers of the regulated entity and conduct all business of the regulated entity . . .." 12 U.S.C. § 4617(b)(2)(B)(i). FHFA asserts that, as conservator of the Enterprises, it may set executive compensation using this and other statutory authorities.

September 2008, and as conservator, the Agency determined to delegate authority for general corporate governance and day-to-day matters to the Enterprises' boards of directors and executive management and to retain authority for certain significant decisions, including executive compensation decisions.[10] As such, since 2008, FHFA has fulfilled a dual role in many of its compensation reviews. Specifically, it has received notice of and reviewed executive officer compensation agreements as regulator and supervisor under the Safety and Soundness Act and reviewed them for approval as conservator.

Recent OIG Assessment Related to FHFA's Oversight of Enterprise Executive Compensation

In a recent report, OIG's Office of Investigations found that the former FHFA Director's June 2021 approval of a $250,000 "retention payment" to an Enterprise executive may have constituted the payment of a prohibited bonus in violation of the STOCK Act.[11] Of particular relevance to this evaluation is that, subsequent to that approval, the executive compensation staff were reassigned to other FHFA divisions and the lead responsibility for Enterprise executive compensation review was transferred from FHFA's Office of the Director to the Division of Accounting and Financial Standards and then to DCOR. As noted, this evaluation assesses FHFA's current framework for reviewing Enterprise executive officer compensation to meet the Agency's statutory, regulatory, and conservatorship requirements.

---

[10] The Senior Preferred Stock Purchase Agreement executed by FHFA as conservator for each Enterprise prohibits the Enterprise from entering into new compensation arrangements with or increasing compensation or benefits payable to certain executive officers without FHFA's consent, in consultation with Treasury. In its latest letters of instruction provided to each Enterprise's board of directors, issued Dec. 18, 2017, FHFA retained the authority to approve "any changes in employee compensation that could significantly impact the employees of the Enterprises," such as retention awards and special incentive plans.

[11] OIG, *Report of Administrative Inquiry into a Whistleblower Complaint Concerning an Enterprise Executive Compensation Matter* (Jan. 26, 2022) (OI/OIG-2022-001). The Representative Louise McIntosh Slaughter Stop Trading on Congressional Knowledge Act, also known as the STOCK Act, prohibited Enterprise senior executives from receiving bonuses during any period of conservatorship for those entities. *See* Pub. L. No. 112-105, § 16 (2012) (codified at 12 U.S.C. § 4518a). In April 2022, FHFA barred the Enterprise from paying the retention award after FHFA determined that it would constitute a legally prohibited bonus under the STOCK Act. FHFA also concluded that payment of a legally prohibited bonus would not be reasonable in accordance with 12 U.S.C. § 4518(a).

FACTS AND ANALYSIS ....

FHFA's Executive Compensation Review Function Experienced Frequent Leadership and Structural Changes Over the Past Three Years

Since 2019, the leadership of the Enterprise executive compensation function has changed twice, most of the staff performing the reviews have turned over, and the function has been moved three times among three divisions and the Office of the Director. In the fall of 2019, the long-time supervisor of the Executive Compensation Branch, which was within the Division of Enterprise Regulation (DER) at that time, left the Agency. Two of the three other career compensation staff also left the branch around this time. Soon after, the Agency's then-Chief of Staff hired an attorney from FHFA's Office of General Counsel, who had worked on compensation matters for six years, to serve as the Director of the newly renamed Office of Executive Compensation (OEC). The Agency then moved OEC from DER to the Office of the Director. In March 2020, the OEC Director hired an outside attorney with experience in executive compensation to be Assistant Director of the OEC in charge of Enterprise executive compensation.

After less than two years, in July 2021, the OEC Director left the position and the Agency chose not to hire a replacement. FHFA leadership moved OEC to the Division of Accounting and Financial Standards in August 2021, and then dissolved OEC two months later. The Agency divided the office's staff and functions between the Division of Conservatorship Oversight and Readiness (DCOR) and the Division of Federal Home Loan Bank Regulation. Currently, the Enterprise executive compensation staff consist of the former OEC Assistant Director, who oversees executive compensation matters within DCOR, with assistance from a senior financial analyst, who divides his time between Enterprise and Federal Home Loan Bank compensation requests. They have primary responsibility for assessing whether proposed compensation actions for Enterprise executives are not reasonable and comparable and manage stakeholder involvement in FHFA decisions regarding compensation oversight.[12]

The Executive Compensation Review Function's Procedures Do Not Reflect Its Current Structure or Define the Minimum Analytical Requirements for Compensation Reviews

Turnover in leadership and staffing and organizational shifts can pose governance challenges. As described in the Government Accountability Office's (GAO) *Standards for Internal*

[12] The Deputy Director of DCOR and other agency stakeholders review and approve the executive compensation staff's recommendation prior to the Director's or Chief of Staff's decision on the matter. The FHFA Director has delegated approval of certain Enterprise compensation actions to the Agency's Chief of Staff. These actions include compensation to be paid to executive officers under incentive pay plans and goals for which the FHFA Director has previously provided a non-objection.

Control in the Federal Government (the Green Book), change "can often be overlooked or inadequately addressed in the normal course of operations. . . . Changes in conditions affecting the entity and its environment often require changes to the entity's internal control system, as existing controls may not be effective for meeting objectives or addressing risks under changed conditions. . . . Further, changing conditions often prompt new risks or changes to existing risks that need to be assessed."[13]

The Green Book calls for management to periodically review "policies, procedures, and related control activities for continued relevance and effectiveness in achieving the entity's objectives or addressing related risks." In addition, should significant change occur, such as changes in personnel, the Green Book advises management to review processes "in a timely manner after the change to determine that the control activities are designed and implemented appropriately."[14]

The Green Book also describes the need for management and staff at federal agencies to establish policies and procedures to support operational effectiveness and a strong control environment in government programs. It states, "[m]anagement documents in policies for each unit its responsibility for an operational process's objectives and related risks, and control activity design, implementation, and operating effectiveness. . . . Each unit also documents policies in the appropriate level of detail to allow management to effectively monitor the control activity."[15]

DCOR officials have acknowledged the need to update the existing procedures for executive compensation reviews. Those procedures do not reflect all of the current individuals, offices, and stakeholders involved in the process. For example, the procedures do not reflect the Agency Chief of Staff's role in approving certain compensation actions as that role currently is defined in FHFA's delegation of authorities document. DCOR plans to complete this update by the end of October 2022. The officials explained to us that multiple organizational changes in the past year, and reduced staffing, affected the executive compensation staff's ability to update the procedures.

We observed that FHFA has not established minimum requirements in its procedures for FHFA's assessment of executive compensation requests. As written, the procedures describe at a high level the assessment to be performed by FHFA staff. For example, the procedures

---

[13] GAO, *Standards for Internal Control in the Federal Government*, at 42-43, paragraphs 9.02 and 9.05 (Sep. 10, 2014). The Green Book sets the standards for an effective internal control system for federal agencies like FHFA and provides the overall framework for designing, implementing, and operating an effective internal control system.

[14] *Id*. at 62-63, paragraph 12.05.

[15] *Id*. at 56, paragraph 12.03.

state that staff members "validate calculations, follow-up with management for clarification, and conduct an assessment of the action requested" and that "[the executive compensation staff] ensures . . . that calculations are accurate and market data supports the compensation action." However, the procedures do not describe the scope of FHFA's review or prescribe the specific analytical work to be performed, particularly those steps related to the executive compensation staff's review of the reasonability of a compensation request. The procedures do not reference the factors set forth in FHFA's Executive Compensation Rule that must be applied during the analysis of whether proposed compensation is not reasonable and comparable, or other factors FHFA may choose to apply.[16] Nor do the procedures detail the documentation requirements for the staff analysis memoranda.[17]

The DCOR Deputy Director acknowledged that there are many viewpoints within the Agency on how the compensation review process should be conducted, but few written policies. The Deputy Director said that it was his priority in the coming year to address that issue.

FHFA Compensation Staff Advised OIG that the Agency Recently Hired a Consultant to Assist with Independent Validation of the Enterprises' Market Data for Compensation Actions

Although FHFA's compensation review procedures state that compensation staff will ensure that market data support proposed compensation actions, in a November 2021 staff analysis memorandum, the executive compensation staff described an "over-reliance by FHFA on the Enterprises' external compensation consultants, who provide compensation market data to the Enterprises." They wrote that they were unable to verify the Enterprises' compensation conclusions and that they "must accept this market data as fact without much opportunity to independently validate it." The compensation staff also raised the concern that "the Enterprises may have the ability to influence or manipulate market data . . . [which] may result in higher market data than would otherwise be acceptable or appropriate for a position."

The staff recommended that FHFA hire its own compensation consultant to address this over-reliance on the Enterprises' consultants. The Assistant Director for Executive Compensation explained to us that an independent compensation consultant would provide a second opinion

[16] Despite the lack of detail in the procedures, the Deputy Director informed us that he believes that the executive compensation staff operate with a good, precedential set of factors for their review of executive compensation.

[17] The executive compensation staff prepare a staff analysis memorandum with a recommendation concerning the proposed action. The procedures contain high-level instruction on the elements of staff analysis memoranda. For example, they state, "[t]he Staff Analysis Memorandum captures all pertinent information and discussion to support FHFA's decision, including relevant discussions that occur during the analysis period." We note that FHFA reduced the level of detail in the procedures when it removed guidance on the assessment of Enterprise performance against the Conservatorship Scorecards for the determination of at-risk compensation and testing of executives' compensation payments.

on proposed compensation actions and validate the Enterprises' submissions. Compensation staff informed us that FHFA engaged its compensation consultant in July 2022.

FHFA Did Not Consistently Apply the Executive Compensation Rule's Factors in Its Reviews of Enterprise Executive Compensation

The Executive Compensation Rule's definition of "reasonable" establishes factors for the Agency's review of Enterprise executive compensation. It states that "reasonable" compensation is compensation that would be appropriate to the position and,

> based on a review of relevant factors *including*, but not limited to: (i) The duties and responsibilities of the position; (ii) Compensation factors that indicate added or diminished risks, constraints, or aids in carrying out the responsibilities of the position; and (iii) Performance of the regulated entity, the specific employee, or one of the entity's significant components with respect to achievement of goals, consistency with supervisory guidance and internal rules of the entity, and compliance with applicable law and regulation.[18] (Emphasis added).

OIG interprets this language to require FHFA to apply the factors specifically listed. The FHFA Assistant Director for Executive Compensation told us the executive compensation staff apply the factors listed in the Executive Compensation Rule's definition of "reasonable" to their reviews only as needed. The Assistant Director explained that the specific factors considered during their assessment of the reasonableness of compensation depend on the FHFA Director's priorities, in part, because the Executive Compensation Rule states that the Director may consider for the analysis any factor the Director considers to be relevant.

Based on our review of a sample of staff analysis memoranda supporting compensation decisions, we found that FHFA generally did not document its analysis of the reasonableness of Enterprise executive compensation requests. We reviewed approximately 20 percent (12 of 53)[19] of the completed assessments of relevant compensation requests made by the Enterprises between January 1, 2021, and April 13, 2022. We confirmed express references to the factors that FHFA applied to determine the reasonableness of the Enterprise's submission in 2 of the 12 staff analysis memoranda for these matters. These instances related to matters where the executive compensation staff raised a concern about the reasonableness of the compensation or the position benchmark used by the Enterprises' compensation consultant. This aligned with a statement from the Assistant Director for Executive

---

[18] 12 C.F.R. § 1230.2.

[19] FHFA tracking records reflected that compensation staff completed their review of 53 of the 65 compensation requests submitted by the Enterprises during this time. Some submissions were withdrawn by the Enterprises, while others were still under review at the time of FHFA's response to our request.

Compensation that the executive compensation staff do not document their reasonableness determination factors if they do not have an issue with the submission's reasonableness. In addition, for eight submissions that related to new compensation arrangements, we could not confirm any references to the Executive Compensation Rule's reasonableness factors, and discussion related to those factors was generally limited to one element: the duties and responsibilities of the position.

An associate general counsel in FHFA's Office of General Counsel who is involved in the compensation review process acknowledged that the Agency's review of reasonableness is not standardized.[20] That associate general counsel did not view the Executive Compensation Rule's factors to be a checklist that is required for the assessment. According to that associate general counsel, the elements concerning the duties and responsibilities of the position and added or diminished risks would be covered by the market data and information contained in the Enterprises' submissions. The associate general counsel said that another element concerning achievement of goals and legal and regulatory compliance is currently conducted through the Agency's annual review of the Enterprises' performance against Conservatorship Scorecard goals and of the Enterprises' assessments of individual employee performance with regard to corporate goals. To provide context, the official explained to us that the threshold for prohibiting compensation based on application of the statutory standard that it is "not reasonable and comparable" is a "high bar" for the Agency, if the Enterprise made an acceptable case that the compensation is reasonable and comparable.

The DCOR Deputy Director Plans to Review Staffing Needs for the Executive Compensation Review Function

According to the Office of Personnel Management (OPM),[21] workforce planning is the foundation for managing an organization's human capital. OPM defines workforce planning as a process for identifying and addressing gaps between an organization's current staff and its future workforce needs. Effective workforce planning enables an organization to align workforce requirements directly to an agency's strategic and annual business plans. DCOR's Deputy Director advised us that he will be reviewing staffing needs within a few months.

The Assistant Director for Executive Compensation told us in May and June 2022 that there was a backlog of compensation reviews to be performed. That Assistant Director explained that the backlog had slowed down the executive compensation staff's efforts to update the

[20] FHFA's Office of General Counsel reviews the staff analysis memorandum to determine whether the recommendation "comports to statutes and regulations administered by FHFA."

[21] OPM serves as the chief human resources agency and personnel policy manager for the federal government. For further information on OPM's role, see OPM's website at www.opm.gov/about-us.

Agency's procedures for the executive compensation review process.[22] While a financial analyst was hired in September 2021, the Assistant Director for Executive Compensation was responsible for the review of the vast majority of relevant compensation submissions—57 of 65 (approximately 90 percent)—that FHFA received between January 2021 and mid-April 2022.

In June 2022, the DCOR Deputy Director acknowledged that his staff is currently overworked. However, he explained that he plans to review the impact of recent executive compensation policy changes on workflow over the next few months before determining whether additional staffing is justified.

FINDINGS ....

- FHFA has not defined in its procedures the required scope and analytical steps in its review of the reasonableness and comparability of proposed Enterprise executive compensation. Notwithstanding the language in the Executive Compensation Rule that defines "reasonable" compensation as being based on a review of the factors identified in the rule, FHFA's procedures do not specify whether its compensation staff are expected to review each submission against those factors. In addition, FHFA's compensation staff told us that they typically document the factors applied in the review only when they identify an issue with the proposed compensation that relates to the specific factor. This lack of documentation of the factors that the Agency considered leaves a gap in the record of the scope of its review and the extent of the analysis performed.

- As the Green Book advises, management should periodically review policies and procedures for continued relevance and effectiveness. FHFA's existing procedures do not reflect the compensation review function's current structure and roles and responsibilities. DCOR officials acknowledged the need to update the existing procedures and informed us that they plan to complete the updates by the end of October 2022.

- DCOR has not determined the necessary level of staffing to ensure the efficient execution of the Agency's statutory responsibility for oversight of Enterprise executive compensation. The DCOR Deputy Director advised us that he plans to review staffing needs over the next few months.

[22] Based on data provided by FHFA, we calculated that the average completion time for the review and approval of an Enterprise compensation submission received during our review period was 24.5 days.

CONCLUSIONS

FHFA's executive compensation review function has undergone significant leadership and structural changes in recent years. The function will undergo further operational changes following the onboarding of a compensation consultant that will help staff validate the Enterprises' compensation submissions. To enhance operational effectiveness to meet its statutory responsibility, FHFA should revise its Enterprise executive compensation review procedures to: define the scope of FHFA's reviews of compensation submissions; reflect the current roles and responsibilities of FHFA personnel involved in the process; establish expectations for documenting compensation reviews in staff analysis memoranda; and reflect changes that result from incorporating the consultant into the review process. Finally, DCOR should ensure that it has sufficient human capital available to efficiently perform the executive compensation review function.

RECOMMENDATIONS

We recommend that FHFA:

1. Update its Enterprise executive compensation review procedures to include its minimum requirements for the scope of the compensation reviews and the analytical work and specific steps to be performed in its review of the reasonableness and comparability of proposed compensation actions, as well as its expectations for the level of documentation of that review in staff analysis memoranda.

2. Complete the process of updating its Enterprise executive compensation review procedures to reflect the roles and responsibilities of the individuals and entities involved in the review process.

3. Determine whether, and ensure that, the Agency has sufficient human capital resources to efficiently execute its statutory responsibility for oversight of Enterprise executive compensation.

FHFA COMMENTS AND OIG RESPONSE.................................

We provided FHFA an opportunity to respond to a draft of this evaluation. FHFA provided technical comments on the draft report, which were considered in finalizing this report. FHFA also provided a management response, which is reprinted in its entirety in the Appendix. FHFA agreed with our recommendations.

OBJECTIVE, SCOPE, AND METHODOLOGY ....

We performed this evaluation to assess FHFA's framework for reviewing Fannie Mae's and Freddie Mac's executive officer compensation to meet statutory, regulatory, and conservatorship requirements. To achieve this objective, we reviewed documentation of the Agency's review and analysis of executive compensation proposals and determined whether FHFA officials followed the Agency's documented processes and criteria. The review period of this evaluation was January 2021 to mid-April 2022.

To conduct our assessment, we reviewed all internal FHFA guidance related to executive compensation in effect during the review period, as well as governing laws, regulations, orders, and guidance to the Enterprises concerning the submission and review of executive compensation actions. We reviewed FHFA's tracking records for the compensation submissions it received during the review period, and we selected a judgmental sample of records of executive officer compensation request reviews from across that period. We reviewed the staff analysis memoranda, supporting documentation, and related communications for the sample of compensation requests.

We also interviewed DCOR staff responsible for assessing whether proposed compensation actions for Enterprise executives are not reasonable and comparable, staff from the Office of General Counsel involved in the review process, and the Deputy Director of DCOR.

This evaluation was conducted between April 2022 and August 2022 under the authority of the Inspector General Act and in accordance with the Council of the Inspectors General on Integrity and Efficiency's *Quality Standards for Inspection and Evaluation* (December 2020).

APPENDIX: FHFA MANAGEMENT RESPONSE...........................

CONTROLLED

Federal Housing Finance Agency

MEMORANDUM

TO: Kyle D. Roberts, Deputy Inspector General for Evaluations

FROM: Jason Cave, Deputy Director, Division of Conservatorship Oversight and Readiness (DCOR) JASON CAVE Digitally signed by JASON CAVE Date: 2022.09.23 19:08:19 -04'00'

SUBJECT: Draft Evaluation Report: *FHFA Could Enhance the Efficiency of the Agency's Oversight of Enterprise Executive Compensation by Ensuring Sufficient Human Capital Resources and Updating Procedures*

DATE: September 23, 2022

Thank you for the opportunity to review the Office of Inspector General (OIG) draft report referenced above (Report). The objective of the Report was to assess FHFA's framework for reviewing Fannie Mae's and Freddie Mac's (the Enterprises) executive officer compensation to meet statutory, regulatory, and conservatorship requirements. The review period of this evaluation was January 2021 to mid-April 2022.

The OIG concluded that FHFA's executive compensation review function has undergone significant leadership and structural changes in recent years, and the function will undergo further operational changes following the onboarding of a compensation consultant that will help FHFA staff validate the Enterprises' compensation submissions. The OIG further concluded that to enhance operational effectiveness to meet FHFA's statutory responsibility, FHFA should revise its executive compensation review procedures to define the scope of FHFA's reviews of Enterprise compensation submissions; reflect the current roles and responsibilities of FHFA personnel involved in that process; establish expectations for documenting Enterprise compensation reviews in staff analysis memoranda; and reflect changes that result from incorporating the consultant into the review process. Finally, OIG concluded that DCOR should ensure that it has sufficient human capital available to efficiently perform the Enterprise executive compensation review function.

Recommendation 1: *The OIG recommends that FHFA update its Enterprise compensation review procedures to include its minimum requirements for the scope of the compensation reviews and the analytical work and specific steps to be performed in its review of the reasonableness and comparability of proposed compensation actions, as well as its expectations for the level of documentation of that review in staff analysis memoranda.*

Management Response: FHFA agrees to the recommendation and is committed to updating the procedures by February 28, 2023. FHFA will include the following in the procedures: (i) the minimum requirements for the scope of FHFA's Enterprise executive compensation reviews; (ii) the analytical work and any specific steps to be performed in FHFA's review of the reasonableness and comparability of proposed compensation actions; and (iii) FHFA's expectations for the level of documentation of that review in staff analysis memoranda.

Recommendation 2: *The OIG recommends that FHFA complete the process of updating its Enterprise compensation review procedures to reflect the roles and responsibilities of the individuals and entities involved in the review process.*

Management Response: FHFA agrees to the recommendation and commits to updating its Enterprise executive compensation staff review procedures to reflect the roles and responsibilities of the individuals and entities involved in the review process by February 28, 2023.

Recommendation 3: *The OIG recommends that FHFA determine whether, and ensure that, the Agency has sufficient human capital resources to efficiently execute its statutory responsibility for oversight of Enterprise executive compensation.*

Management Response: FHFA agrees to the recommendation and is committed to ensuring that FHFA has sufficient human capital resources to efficiently execute its statutory responsibility for oversight of Enterprise executive compensation. The DCOR Deputy Director will determine whether the Agency has sufficient human capital resources for this function by November 30, 2022. The DCOR Deputy Director will utilize the Agency's Human Resources processes to ensure that the Agency has sufficient human capital resources for this function.

If you have any questions, please feel free to contact me.

cc: Edom Aweke
John Major

ADDITIONAL INFORMATION AND COPIES..............................

For additional copies of this report:

- Call: 202-730-0880
- Fax: 202-318-0239
- Visit: www.fhfaoig.gov

To report potential fraud, waste, abuse, mismanagement, or any other kind of criminal or noncriminal misconduct relative to FHFA's programs or operations:

- Call: 1-800-793-7724
- Fax: 202-318-0358
- Visit: www.fhfaoig.gov/ReportFraud
- Write:

  FHFA Office of Inspector General
  Attn: Office of Investigations – Hotline
  400 Seventh Street SW
  Washington, DC 20219