STATEMENT OF

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FEDERAL HOME LOAN BANK OF SEATTLE

TO THE
THE FEDERAL HOUSING FINANCE BOARD
ON
BOARD GOVERNANCE

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Good afternoon Chairman Korsmo, and directors Weicher, Leichter, Mendelowitz, and Castaneda. I am Michael P. Radway, Chairman of the Board of Directors of the Federal Home Loan Bank of Seattle.

I'd like to thank Chairman Korsmo and the Finance Board for the opportunity to speak this morning on behalf of the Federal Home Loan Bank of Seattle and address the critically important issue of board governance and responsibility within the Bank System.

As a federally appointed Public Interest Director from the state of Oregon, and as an active and involved member of my community, I can say, without hesitation, that the issue – and practical application -- of board governance is of paramount importance to the financial institutions, the neighborhoods, the businesses, the families and the non-profit housing and economic development organizations we serve every day in the Seattle Bank region – and to me, personally.

Simply put, I'm accountable for the safety and soundness of the Federal Home Loan Bank of Seattle, and the fulfillment of its mission.

While I'm not alone in that role -- I share it with 17 other directors and the management team of the company – I consider it my job to ensure that the financial management of this $46 billion bank is effective over the long term, including proper stewardship of our shareholders' capital.

That's a staggering responsibility when you consider that the funding provided within the Seattle Bank district fuels housing finance, affordable housing initiatives and economic development in communities from Pago Pago to Walla Walla, Washington. Our nearly 400 member institutions rely on the Federal Home Loan Bank of Seattle to be their partner in helping their communities and local economies not only survive, but thrive.

So when appointed to serve as a director of the Federal Home Loan Bank of Seattle, I understood the critical importance of my role and what I needed to bring to the board – namely, my personal integrity and accountability, and my experience in regional and national banking policy, and my commitment to building strong communities and economies.

The Seattle Bank board shares with you, our regulator, the Treasury and Congress the sense of urgency that is so pervasive today regarding the need for increased corporate accountability and responsibility. And we've worked hard over the last several years to significantly strengthen the directors' leadership and oversight of the Seattle Bank.

While we fully understand that corporate governance is a process; a discipline that can – and must be – constantly improved, I'm personally and professionally encouraged by the intensity of our efforts and the progress being made.

Over the course of the last year, the Seattle Bank's board has created, adopted and publicly disclosed a set of Core Principles and Guidelines relating to board governance, realigned our board committee structure to more effectively oversee all facets of the bank's operations, upgraded our education and training program for directors, and established a web site that provides directors with faster access to a wider range of information critical to their board roles.

Our Core Principles and Guidelines provide us with a corporate governance roadmap, if you will, keeping us focused on:

- Assuring that policies, risk assessments, internal controls and decisions are effective in managing risk and are administered fairly.
- Operating in an independent and active manner.
- Setting the strategic direction of the bank and managing progress against goals.
- Determining if management is capable and if the business is being properly managed.
- Evaluating our own board effectiveness.

I would also like to recognize the foresight and diligence of the Finance Board in overseeing and supporting sound corporate governance practices across the Bank System.

In particular, the Finance Board's 2003 Horizontal Review of Board Governance provided the 12 banks with a valuable resource for identifying practices that contribute to effective governance programs.

The Finance Board's series of targeted reviews to assess the effectiveness of board governance at the Home Loan Banks gave us a roadmap for enhancing the quality of oversight, leadership and stewardship within the Bank System at a time when so much attention is being paid to the safety and soundness of the housing GSEs.

In addition, the Finance Board is to be commended for the significant progress it has made in increasing the resources being brought to bear in the areas of examination and supervision. Since 2001, Chairman Korsmo and the Finance Board have moved quickly to add examiners, financial analysts, accountants and risk management specialists, all in the interest of providing the highest quality oversight of the Federal Home Loan Bank System.

As Chairman Korsmo stated in Senate testimony in October 2003: "…We are fast approaching world-class status in the size and skills, the capacity and sophistication of our staff and their oversight of the 12 banks."

You may also be interested to learn that as a result of our strategic planning process, my own board made the decision last year to make similar investments in our analytic and accounting systems and infrastructure. We increased our operating expenses by more than 50 percent in 2004 and will hire 48 new staff, primarily individuals with highly technical accounting, analytical, capital markets and trading skills and experience. These additional systems and staffing will significantly strengthen our dynamic hedging capabilities and our acquired member asset (AMA) purchase program, as well as enable us to provide "world class" disclosures to our regulator, the investment community and the public.

Today's hearing is further evidence of the Finance Board's intent to build a regulatory structure that offers the 12 Home Loan Banks access to consistent, effective resources, processes and guidelines that continue to enhance the Bank System and its ability to meet the housing and development needs of individuals, communities and members across this country.

To that end, on behalf of the Seattle Bank board, I would like to provide you with four specific recommendations for your consideration regarding the enhancement of Federal Home Loan Bank board governance.

Recommendation #1 -- Devolving Public Interest Director (PID) appointments to the individual Home Loan Bank boards.

> Good corporate governance requires, above all, the presence of independent, informed directors who have the courage and integrity to ask difficult questions. With such directors, any reasonable system can work. Without such directors, any system, no matter how excellent, can fail.
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> While concerns have been raised over the last decade regarding the impact of politics on the PID appointment process, the purpose of our recommendation is based only on this: finding and appointing the most qualified directors to provide the highest quality of board leadership and oversight for the Home Loan Banks.

We strongly believe that knowledgeable, independent directors, selected by the banks' boards rather than by the regulator, help to reinforce the "bright red line" between the regulator and the regulated, and between management and supervision. If a director is abrogating their responsibility, the Finance Board is much more likely to take action against that director if it is not an individual they have appointed.

It is also worth noting that the administration, in September 2003, asked Congress to eliminate political appointees from the boards of government-sponsored enterprises. More recently, the administration announced that the five appointed directors to the Freddie Mac board would not be re-appointed when their terms expire in March 2004.

We support these recommendations and actions and believe they represent a viable, credible direction for building stronger governance and responsibility into the board structures of the Home Loan Banks.

The Seattle Bank recommends its board form a nominating committee to identify and screen qualified PID candidates. We believe Finance Board guidelines should be created to direct boards in their selection processes, and that these guidelines and processes be developed using industry best practices.

Recommendation #2 – Director Expertise

This relates to our first recommendation – ensuring that we have directors with the expertise and experience to understand and oversee the financial complexities of our organizations, as well as the housing finance, economic development and affordable housing needs of our bank districts.

Granted, this is no small task for any individual director, no matter what their background. We all agree, however, the stakes are much higher now in terms of corporate governance, mandating that we have the ability to set higher skill and performance standards for directors, and our boards as a whole.

If selection of the Public Interest Directors were devolved to the individual bank boards, it would give us an immediate ability to assess and fill expertise and experience "gaps" in board composition. This is critical given that the majority of our board members are elected.

While elected directors come from the financial institutions that make up our cooperative, they also bring a wide range of expertise and industry experience. This mosaic represents both a strength and a vulnerability. The vulnerability – or gaps in certain knowledge areas deemed critical to board oversight – could be addressed in two significant ways:

1) Allowing bank boards to appoint its own Public Interest Directors. The banks could assess the composition and knowledge/oversight needs of its boards and look for appointed directors who could appropriately fill those needs and complement the strengths brought by elected directors.

2) Creating an ongoing director development program that continually builds board expertise -- for all members -- in pre-determined areas deemed critical to effective oversight of our bank.

Again, we believe Finance Board guidelines should be created to help direct boards in their director-selection processes. The governance guidelines and processes should be developed in line with industry best practices regarding board composition and capabilities.

Recommendation #3 – Director Compensation

The Gramm-Leach-Bliley (GLB) Act of 1999 set director compensation for bank directors in statute at $15,000 per year, with allowance for a yearly COLA adjustment that began in 2001 and slightly higher amounts for the chair and vice-chair of a bank.

Because of increased expectations stemming from evolving standards of best practice and the impacts of the Sarbanes-Oxley Act, and because of the increased financial and operational complexity surrounding Bank System activities, there is legitimate concern that the banks may have difficulty in attracting and retaining directors with the requisite experience and expertise to oversee the Home Loan Banks.

I would emphasize, again, that we are fully aware that a new era has dawned in American business – one that looks on board governance as an ongoing, rigorous discipline that demands, at all times, review and accountability.

In order to achieve that level of accountability, it is imperative that we have the resources available to attract and retain individuals who can bring the highest levels of oversight and expertise regarding financial services and community and economic development to our banks. We also need to ensure that boards do not limit their oversight of bank activities because compensation is limited. That would be penny wise and pound foolish.

We recommend removing the current compensation caps and allow the boards of the individual banks to set their own compensation levels for directors. It is important to note that the two other housing GSEs (Fannie Mae and Freddie Mac) set their own compensation levels for directors.

As a control mechanism, we recommend that each bank be mandated to adequately report all director compensation levels to the Finance Board and the public in a consistent manner that allows for appropriate member and public oversight.

Recommendation #4 – Board Terms

We've touched on how to better ensure that we have the right individuals with the right expertise overseeing our banks. This recommendation pertains to how long these individuals should serve our institutions.

We believe that, if PID appointments are devolved to the individual banks – thus allowing our institutions to select directors with higher levels of financial and community/economic development expertise – then the current three-year term standard will suffice.

If no change is made in the PID appointment process, we recommend extending board terms to four years for all directors.

We are all well aware that a quantum shift has occurred in how American corporations – large and small, privately held or publicly traded – will be run, and must be run.

In addition, as we are all well aware of, the housing GSEs are experiencing a much higher level of scrutiny that, in turn, is demanding a much higher level of corporate and board governance.

As one of 216 Bank System directors, I personally feel the pressure of that scrutiny, and I welcome it.

Given the scope and influence of Home Loan Banks on our financial institutions, our communities, and the U.S. economy, we should never shy away from the bright light of regulatory or Congressional oversight and scrutiny. Rather, we must embrace it as an integral part of the roles and responsibilities we have as Home Loan Bank directors.

In closing today, I would like to again commend the Finance Board for its efforts regarding Bank System board governance, for its horizontal reviews of best practices, its strengthened supervisory and examination staff, and for the "bright red line" it is drawing between itself and the banks it regulates. I urge the Finance Board to continue working closely with each of the 12 Federal Home Loan Bank boards of directors in creating the right tools and processes that allow us to ensure the efficiency, the profitability and the safety and soundness of our banks.

Together we have created a housing finance system that is the envy of the world; one that has made the dream of homeownership accessible, and affordable, for more families than any other nation on Earth.

I look forward to working with each of you in the near future, and discussing, in more detail, the recommendations presented here on behalf of the Seattle Bank Board of Directors.

Mr. Chairman, this concludes my testimony. Thank you, again, for allowing me the opportunity to speak with you today.