

The **GSE** REPORT

All GSEs

- *News Not Yet Reported – Ralph Nader Plans Forum on GSEs:*
 - Consumer Advocate Ralph Nader is planning to host a GSE forum on May 14th similar to the Microsoft forum he held recently. The forum is scheduled to be held at the Grand Hyatt Hotel in Washington, DC. According to a draft agenda, the panel topics will include “Subsidies”; “GSEs and Low Income Housing Goals”; “Do we need Fannie Mae and Freddie Mac?”; “Lobbying and Influence”; “Reforming the Housing Goals”; “Establishing a More Effective Regulator”; “What’s the Future? – Expand Them, Change Them, Set Them Free or Keep the Status Quo?” Chairman of Fannie Mae Jim Johnson, Freddie Mac CEO Leland Brendsel and Chairman of the House Banking Committee Jim Leach (R-IA) have all been invited to speak at the forum.
- *GAO Releases Study on GSE Non-Mortgage Investments:*
 - The GAO released a report to Chairman of the House Banking Committee Jim Leach (R-IA) to report on “(1) the GSEs’ legal authority to make nonmortgage investments and federal regulatory oversight of that activity; (2) the relationship between nonmortgage investments and federal regulatory oversight of that activity; and (3) the extent to which the enterprises have undertaken nonmortgage investments for arbitrage profits.” The GAO found that the GSEs (defined as Fannie Mae, Freddie Mac, and Farmer Mac) had broad investment authority and that the regulators of the GSEs had not been focusing on whether the investments of the agencies were mission-related but only on safety and soundness concerns. (None of the regulators found safety and soundness concerns.) The GAO noted that Congress gave the Department of Housing and Urban Development (HUD) and the Farm Credit Administration (FCA) regulatory authority over mission activities. The GAO feels that this regulatory authority has become even more important, as Farmer Mac has substantially increased its holdings of nonagricultural-mortgage

investments and Fannie and Freddie have proposed new types of nonmortgage investments.

Amount of Nonmortgage Investments:

- As of June 30, 1997, nonmortgage investments accounted for 15% of on-balance sheet assets of Fannie Mae, 10% at Freddie Mac (Freddie Mac claims only 2% of their mortgage portfolio), and 66% of Farmer Mac's assets were in nonagricultural-mortgage investments (Farmer's Mac's nonagricultural-mortgage investments expanded from \$155 million in 1997 to \$931 million). The GAO defined Fannie Mae and Freddie Mac's nonmortgage investments as cash and cash equivalents, asset-backed securities, private corporate securities, and state and municipal bonds. Farmer Mac's nonagricultural-mortgage investments consisted mostly of other government agency securities and corporate debt issues.

Nonmortgage Investments Generate Arbitrage Profits:

- The GAO stated that "government sponsorship lowers their debt costs, and they can therefore generate arbitrage profits (i.e., profits resulting from their funding advantage) by investing in nonmortgage investments." The GAO found that the GSEs nonmortgage investments could best be described along a continuum representing the degree to which they relate to the housing enterprises' missions. The GAO put short-term nonmortgage investments (such as short term federal funds which facilitate liquidity) on one end of the continuum and longer-term investments on the other end that are "less clearly related to the enterprises' mission in facilitating liquidity in the secondary market, because fluctuations in their market value reduce their usefulness in responding to changes in capital and mortgage products."

HUD's Regulatory Authority over Nonmortgage Investments:

- The GAO agrees with a recent HUD evaluation that it could use its general regulatory authority to potentially limit nonmortgage investments. HUD has not yet developed criteria for evaluating the nonmortgage investments to see if they are consistent with the agencies' charters. HUD issued an advanced notice of proposed rulemaking on the subject in December 1997 (comment period closes Monday, March 30). The GAO noted that Fannie Mae expressed to them that HUD may not "prospectively regulate" Fannie Mae's investment discretion and that its investment practices should be considered "internal corporate affairs" subject to broad discretion. Fannie Mae cited legislative history and other Congressional statements about the regulation of "internal affairs," and argued that HUD should not exercise its general regulatory authority over Fannie's investment practices except in an "extreme situation" – when the activities threaten safety and soundness. GAO reports that even if nonmortgage investments are considered corporate matters as Fannie Mae argues, HUD "could take regulatory action, such as requiring reports of nonmortgage investment activities, in cases where HUD appropriately determines the action is necessary to ensure the accomplishments of the enterprises' charter acts." In conversations with HUD in writing the report, GAO found that HUD had not focused attention on Fannie and Freddie's nonmortgage investments until the controversy arose over Freddie Mac's purchase of Phillip Morris bonds. In

November, HUD requested their first report from Fannie and Freddie on their nonmortgage investment activity.

FCA's Regulatory Authority on Nonmortgage Investments:

- The GAO found that the FCA has general regulatory authority over Farmer Mac which could be used to regulate nonagricultural-mortgage investments but has not, to date, developed criteria to do so. In October 1997, the FCA indicated that, for now, it was not concerned that Farmer Mac's nonmortgage investments were inconsistent with its mission-related charter. The GAO reported however, that the FCA stated that "the debt issuance strategy associated with the investments is intended to be temporary and to develop over a reasonable period of time. Therefore, according to FCA, its position could change if over time evidence does not show that such investments play a role in helping Farmer Mac achieve its mission."

Tension of Shareholder Profit and Mission:

- The GAO concluded that the GSEs "have incentives as private corporations to increase shareholder value; these incentives create a tension with achievement of the missions stated in the federal charters of the enterprises. It is this tension that highlights the importance of mission oversight. Without effective mission oversight, the incentives to use the benefits of government sponsorship to increase shareholder value could, over time, erode the public mission."

Recommendations by GAO:

- The GAO recommended that HUD continue developing its criteria for regulating nonmortgage investment through the rulemaking process and that the Chairman of the FCA direct the Office of Secondary Market Oversight (OSMO) to develop criteria and provide semiannual reports to the House and Senate Agricultural Committees. The GAO also recommended that Congress should monitor the actions of HUD and FCA in establishing criteria. The GAO concluded that Congressional oversight was "important to help ensure that corporate incentives to increase shareholder value do not erode the enterprises' public mission. If adequate progress is not made in a timely way, Congress may wish to consider providing further guidance to the regulatory agencies."

Treasury Recommendations:

- The Treasury Department recommended in a comment letter to the GAO that the enterprises' mission regulators should use their general regulatory authority to limit the enterprises' nonmortgage investment activity. The Treasury letter stated that "We believe that such regulations should limit a GSE's investments to those necessary and appropriate for normal business operations, such as cash management. In exercising its regulatory authority, each GSE regulator should remain mindful of the ready access to capital markets inherent in the GSEs' charters. Regulators should also give careful scrutiny and analysis to claims that a particular investment is mission-related. All investments should be scrutinized in light of the specific public purpose – and expressly approved lines of business – for which Congress has established each GSE." (*GAO Report GGD-98-48*, March 1998)

- *Chairman Leach Responds to GAO Report on GSE Investments- Blasts Farmer Mac:*
 - After reading the GAO Report on GSE non-mortgage investments, Chairman of the House Banking Committee Jim Leach blasted Farmer Mac for its “disturbing trend” of non-agricultural-mortgage investments. GAO’s Report notes that in the last two years Farmer Mac’s nonagricultural-mortgage investments have expanded from \$155 million to \$931 million. Chairman Leach notes that 66% of Farmer Mac’s investments are now in other government agency securities and corporate debt issues. According to the GAO Report, Farmer Mac officials indicated that their heavy nonagricultural-mortgage investments are part of a debt issuance strategy designed to lower funding costs. GAO’s Report stated: “By lowering funding costs, officials said that Farmer Mac will be able to better price its AMBS (agricultural mortgage backed securities) in the secondary market, which these officials expect to trigger greater product demand and, thus, enable Farmer Mac to better meet its mission.” However, Chairman Leach said: “Farmer Mac was established by Congress to help the farmer, not its stockholders. It is simply an abuse of government authority for a GSE to have over half its assets invested in sophisticated arbitrage instruments.” (*Press Release by the House Banking Committee, 3/25/98; ; American Banker, 3/27/98, Dow Jones Newswire, 3/25/98*)

Fannie Mae & Freddie Mac

- *Mortgage Researcher Testifies that Removing Fannie and Freddie’s Charter would be the Best Thing for the Mortgage Industry:*
 - Thomas LaMalfa, a mortgage researcher, journalist and wholesale mortgage banking consultant, testified at a hearing before the Housing Subcommittee of the House Banking Committee on the role of mortgage brokers. In his testimony, LaMalfa was asked to discuss outdated laws and regulations that affect mortgage finance. He believed there were two such examples of outdated laws: (1) Fannie Mae and Freddie Mac and (2) RESPA. He believes that Fannie and Freddie put taxpayers at risk, they are inefficient, and they are at best “mediocre mechanisms for directing subsidies to housing,” and the best thing for the mortgage industry would be to remove their charters. According to Mr. LaMalfa, Fannie and Freddie should be privatized because “(1) they are siphoning most of the economic value from the mortgage business; (2) their special privileges impede the private sector’s growth and financial opportunities; (3) they raise interest rates and indirectly increase the cost of the national debt; (4) they repeatedly have abused their charters; and (5) there is an almost inherent conflict in Fannie and Freddie’s private and public roles. They are at odds. It is a zero sum game: either shareholders and managers win, or taxpayers and the public win.” (*Written & oral testimony of Thomas LaMalfa, 3/26/98*)
- *Credit Scoring Models By Fannie and Freddie and Others are Not a Defense Against Bias:*

- At an industry conference, regulators at HUD and the DOJ warned that lenders using credit-scoring systems developed by others might still be liable for racial bias lending. Peter Kaplan, an associate at HUD, advised lenders to make sure that the pool of information used to create the scoring systems include credit applications that are accepted and those that are denied. Joan Magagna, acting chief of the civil rights division of the Justice Department also cautioned that lenders when overriding low and high credit scores (lenders believe the scores don't reflect the borrower's true strengths or risk) must be applied "evenly and across the board." A Freddie Mac spokeswoman, Sharon McHale, believes that their scoring models treat borrowers of all races and income levels fairly. Ms. McHale said their scoring models are based on racially diverse pools of mortgage borrowers. Moreover, mortgages to minorities approved by the models default as frequently as those made to other groups – which she says suggests the models are not tougher on minorities. (*American Banker*, 3/26/98)
- *Will Fannie and Freddie Mandate Electronic Data Interchange?:*
 - The most influential participants in adopting a standard for electronic data interchange (EDI) are the Mortgage Bankers Association, Fannie Mae, and Freddie Mac, who are supporting the American National Standards Institute's x12 protocol – a technology that automates the exchange of business documents using standard computer formats. David Barkley, executive vice president at Freddie Mac, said most lenders believe that "EDI is nice, but I'll get to it when I can." "Sometimes, to get some of these things implemented, it has to almost be mandated," Mr. Barkley said. He did not, however, say whether Freddie Mac was contemplating such a move, but HUD has mandated that several types of electronic interactions must be in a standard EDI format. Also, MetroStat Technologies Inc., a Sylva, NC-based company, is testing an EDI system with Fannie Mae. Mandating the use of an EDI might be a difficult proposition for Fannie and Freddie. Larry Walker, director of the real estate and mortgage division at Electronic Data Systems Corp. in Plano, TX, said the industry's "800-pound gorillas," whose automated underwriting systems interact with the majority of mortgage lenders, have yet to become x12 compliant." According to Mr. Walker, "they tend to take a nonintrusive approach" and "do not dictate it or mandate it." (*American Banker*, 3/19/98)
- *OFHEO Reports that Fannie and Freddie are Soundly Capitalized:*
 - The Office of Federal Housing Enterprise Oversight (OFHEO) reported that Fannie and Freddie are sufficiently capitalized against an economic downturn. At year-end 1997, Fannie Mae held \$13.8 billion in core capital, exceeding its minimum capital requirement of \$12.7 billion by a little over \$1 billion, OFHEO said. OFHEO said Freddie Mac's core capital reserves totaled \$7.4 billion, \$300 million more than its minimum capital requirement of \$7.1 billion. (*National Mortgage News Daily News web site*, 3/23/98)
- *Fannie & Freddie Agree that Online Mortg. Industry Growth Depends on Setting Standards:*

- At Real Estate Connect 98 (a recent mortgage technology conference sponsored by Inman), representatives from Fannie, Freddie and Microsoft all agreed that setting standards will be necessary for the growth of the online mortgage industry. Roger Conley, vice president of technology marketing at Fannie Mae, suggested adopting an overarching strategy to working with different standards. Fannie Mae developed and is advocating the use of Service Based Architecture (SBA), which is not a standard but rather works as a translating device for different standards, Conley said. Barney Corwin, director of mortgage industry technology for Freddie Mac, also agreed that industry standards were necessary. He warned, however, of the danger of adopting an inappropriate standard, saying once it was adopted, it would be hard to change. He urged members of the industry to be actively involved in adopting any standard. (*Inman News Feature*, 3/16/98)
- *Analyst Reports that Rate, Credit and Political Risks to Fannie and Freddie are Low:*
 - Thomas O'Donnell, who ranked first in the *American Banker* survey in the GSE analyst category, uses the three main factors: rate risk, credit risk, and political risk when tracking the agencies- Fannie Mae, Freddie Mac and Sallie Mae. According to Mr. O'Donnell, all three factors seem to be at low points now. He believes that credit and rates are positive factors right now with the improvement in credit quality and the favorable rate environment, he added. Political risk is the main threat to the agencies but it is now at a low point, he said. "The government in the past has tried to get into their deep pockets," but with a balanced budget, he feels the risks are low. (*American Banker-Bond Buyer*, 3/17/98)
- *EVP of a Mortgage Co. Objects to Fannie and Freddie's Credit Scoring Guidelines:*
 - Gabriel Freshour, executive vice president at Developer's Mortgage, believes credit scores can be unreliable and he objects to Fannie and Freddie's guidelines that give preference to applicants with scores of 620 or above. According to Mr. Freshour, "anything under 620 they [Fannie and Freddie] don't want." In response to criticism, last year Fannie and Freddie urged mortgage companies not to automatically disqualify borrowers with low credit scores and suggested that lenders look at why borrowers have low scores before making a credit decision. Fannie Mae's new rules tell lenders to throw out a credit score if information in an individual's credit file is inaccurate, because the inaccuracy could have tainted the score. (*Columbus Dispatch*, 3/15/98)
- *Delinquency Figures Released for Fannie and Freddie:*
 - According to the Mortgage Bankers Association of America (MBA), delinquency rates in most areas of the mortgage market increased in the fourth quarter of 1997. Fannie Mae – Serious single-family delinquencies were slightly higher, up from .59% in the third quarter to .62 in the fourth. Fannie's highest default rate was in the Northeast at .89% and the Southeast recorded the steepest quarterly increase, where the rate rose six basis points to .59%. On the multifamily side, the share of loans 60-days or more past

due or in foreclosure dropped from .43% to .37%, and the company pared in half its portfolio of multifamily real-estate owned to \$25 million.

- Freddie Mac – Single-family delinquencies went up one basis point to .22% in the fourth quarter, although foreclosure “pipelines” decreased from .34% to .33%. Freddie Mac reported an improving ARM scenario, with serious delinquencies down one basis point and foreclosures down from .85% to .80%. Freddie Mac’s REO inventory was unchanged at \$722 million. Multifamily delinquency rates dropped from 2.68% to 2.16%. The bulk of its problems were in the Northeast with 2.62% of multifamily mortgages delinquent. (*Inside Mortgage Finance website*, posted 3/16/98, as appeared in March 13, 1998 issue of *Inside Mortgage Finance*).
- *Fannie and Freddie Nominated for Inman Innovator Award:*
 - Fannie and Freddie were part of 20 finalists for awards in the 1st Annual Inman “Innovator Awards” – awards honoring individuals or companies that showed incredible foresight in bringing technology and the real estate industry together. Freddie Mac’s Loan Prospector and Fannie Mae’s Desktop Underwriter (automated underwriting systems) were nominated for the category “Software applications that help the real estate industry be more efficient and speed up the real estate transaction.” Fannie Mae/Finet’s iQualify was nominated in the category “Web-related or online services that help consumers save time or money.” Neither Fannie nor Freddie, however, was the ultimate winners in their respective categories. The awards were presented at the second Real Estate Connect Summit in San Francisco. (*Inman News Feature*, 3/12/98)
- *Fannie and Freddie Rank in Business Week’s Top 50 Best Performing Companies:*
 - *Business Week* magazine released their list of the top 50 performers in American business – Fannie Mae was ranked #42 with Freddie Mac, closely behind at #45. The “Business Week 50” is an annual ranking of the best performing companies in the S&P 500. To determine a ranking, every company in the S&P 500 is graded on the basis of top-line revenue growth, earnings growth, and total returns over one and three years, plus net margins and return on equity. (*Business Wire*, 3/19/98)

Fannie Mae

- *Fannie Mae's TV Advertising Upsets Lenders - May Blur Primary & Secondary Market Line and Blur Line Between Fannie Mae and its Foundation:*
 - Concerns have been growing about Fannie Mae's television advertising making Fannie a household name. Lenders complain Fannie Mae's advertising is a blatant move to blur, or even eliminate, the primary and secondary market lines. One particular Fannie Mae ad featuring an Hispanic family getting a home is particularly a concern to lenders, according to one industry observer. The lenders "complain that the clear implication of the ad is that Fannie Mae or its foundation somehow had a hand in approving a mortgage for the family." There is also some concern that the activities of Fannie Mae and its Foundation have also been blurred. Two years ago, Fannie Mae shifted all of its advertising and consumer outreach to the Foundation, however the Foundation's large consumer advertising campaign is administered by corporation executives, whose services are loaned to the Foundation and who previously oversaw nearly identical activities at Fannie Mae itself and even the logos themselves are very similar. Fannie Mae calls the lender's concerns "irrational." In contrast, Freddie Mac does not do advertising and they are somewhat baffled by the extent of Fannie's advertising. According to a Freddie Mac official, they don't know what Fannie Mae is "trying to do with their advertising. All we know is they spend a lot of money on it – by some estimates \$47 million or so in 1997 alone." (*Inside Mortgage Finance* website, posted on 3/23/98, as published in 3/13/98 issue of *Inside Mortgage Finance*)
- *Fannie Mae Plans to Significantly Increase its Foundation Advertising – Plans to do 30-Minute Program on Black Entertainment Television (BET):*
 - Fannie Mae plans to increase its outreach advertising, planning a goal of more than 5 million consumer responses. Fannie Mae announced that since 1993, 4.6 million consumers had responded to Fannie's outreach advertising. Thirty percent of the respondents have been African Americans. Fannie Mae also announced a new partnership with Black Entertainment Television which Fannie hopes would result in 90% of all African American adults seeing Fannie Mae Foundation ads more than 20 times each in 1998. An expansion of outreach activities to Hispanics will be announced later this year. Chairman Jim Johnson announced that Fannie's goal was to have 5 million consumers respond to an offer of a free, 27-page guide that walks homebuyers through a step-by-step self-education process. As part of the partnership with BET, the foundation will more than double its overall spending on BET, with twice as many Foundation 30-second television spots in 1998 as 1997. The Foundation will also air a 30-minute educational special designed to showcase real-life examples of families in the process of becoming homeowners, with tips on how to become a homebuyer from mortgage lenders, nonprofit counselors, and real estate professionals. The program will air as often as once a week over the course of 1998. In June, the Foundation plans to distribute copies of its "Opening Doors" consumer guide to the 1.2 million readers of the

publication BET Weekend. Fannie Mae also plans to increase its advertising on UPN (top prime-time broadcast network for African Americans), and top-rated shows among African Americans on ABC, CBS, FOX and NBC. (*Business Wire*, 3/16/98)

- *Washington Post Calls Chairman of Fannie Mae One of Most Powerful Men in US:*

Praise of Johnson

- Jim Johnson, Chairman of Fannie Mae, was featured on a two-page spread in the *Style* Section of the *Washington Post*. The article referred to Johnson as one of the most powerful men in the US because he is chairman of three preeminent DC institutions – Fannie Mae, the Brookings Institution and the Kennedy Center. Prominent Washingtonian Harold Ickes refers to Johnson as “the chairman of the universe.” Syndicated columnist Mark Shields calls him “the face of the Washington national establishment” and chose Former Secretary of State James Baker as a Republican considered equal in stature to Johnson, but “Jim may have eclipsed even the former Secretary of State.” Vernon Jordan, another powerful Washington insider, says “If you’re chairman of Fannie Mae, the Kennedy Center, and Brookings, you’re an extraordinarily powerful person in this town.” In 1996 (latest figure available) Mr. Johnson made an estimated \$7.2 million in cash, stock options and other compensation. He has, however, given money to worthy causes, including \$1.5 million each to the Kennedy Center and Brookings. The *Washington Post* also included comments from NBC Correspondent Andrea Mitchell, who along with her husband, Federal Reserve Chairman Greenspan is considered a “pal.” Commerce Secretary William Daley said Johnson is as “tough as anybody I’ve ever seen. He’s Norwegian, so he doesn’t blow his stack and throw things and jump up and down. But if he looks at you the wrong way, most people are scared to death. And he’s subtle. He’d cut your [expletive] off, and you wouldn’t even know he was doing it. And when he was finished, you wouldn’t even know it was him.”

Criticism of Johnson:

- There were a small number of detractors but none would speak on the record to the *Washington Post*. Some believe that despite his contributions and pro bono work, “he wields his considerable clout mainly to protect and defend Fannie Mae’s congressionally mandated business advantages.” Fannie Mae isn’t a private corporation like any other (except Freddie Mac) because it is exempt from state and local taxes and has an implicit government guarantee that allows Fannie to “borrow billions at rock-bottom rates, gaining competitive advantage and driving up profits.”

Public Relations Manipulation of Political Figures:

- Johnson’s public relations efforts at Fannie Mae have been political in nature. In the last 3 ½ years, Johnson has opened “29 so-called ‘partnership offices’ in cities and rural communities nationwide, dispensing largess in high-profile ceremonies at which leading incumbent politicians can bask in Johnson’s reflected glory.” An example includes a Fannie Mae event in October 1994, when Senator Ted Kennedy (D-MA) was having a rough political re-election campaign, Johnson announced \$1.5 billion in “affordable financing” for MA with Ted Kennedy as the featured public official.

- Also, the Fannie Mae Foundation gives politicians more opportunities for glory. Recently, an event was held called the “Help the Homeless Check Presentation Ceremony” where Johnson handed out dozens of envelopes in an assembly line fashion containing \$2.5 million for Washington community groups. When the checks were presented, Senators Chuck Robb (D-VA), Paul Sarbanes (D-MD) and Reps. Connie Morella (R-MD) and Jim Moran (D-VA) praised Johnson.
- Johnson and his wife have also given more than \$100,000 (since 1992) to numerous House and Senate candidates, including key Republicans like Rick Lazio (R-NY), member of House Banking Committee, which oversees Fannie Mae; Rep. Ralph Regula (R-OH), chairman of the Appropriations subcommittee that controls the Kennedy Center’s funding; Rep. Bill McCollum (R-FL), vice chairman of the Banking Committee, and Senate Banking Committee Chairman Alfonse D’Amato (R-NY). “Through such exquisitely targeted generosity, Johnson has maximized his political bang-for-buck ratio.”

Johnson Fights Criticism:

- Johnson also “works aggressively to counter criticism and beat back threats.” The online magazine *Slate*, criticized Fannie Mae’s federal subsidies in an article last year. Johnson called the article “unbelievable trash” and wrote a letter to William Neukom, the general counsel of *Slate*’s parent company, Microsoft (whom Johnson had socialized with in Sun Valley).
- Instances were also cited in the article where Johnson has not been so successful such as the recent battles with HUD and the MBA over their support of raising FHA loan limits to Fannie’s level. However, one detractor noted that “Johnson’s lobbying skills and open checkbook are the reasons that Fannie Mae has a federal license to make money.” (*Washington Post*, 3/27/98)
- *Fannie Mae Encounters Controversial Development in Detroit:*
 - The City Council of Detroit will hear arguments from both sides (current residents and homebuilders/developers) on a new development in the east side neighborhood near the Detroit River. The homebuilders/developers want to build up to 410 homes in the neighborhood priced from \$135,000 – the largest new development of single-family homes in decades for the city. But the developers want the city to tear down almost all of the houses in the 88-acre neighborhood and use condemnation to get land from owners who don’t want to sell. Although the tract is two-thirds vacant, there are approximately 640 people living in the area – some well maintained, some not. David Dworkin, director of Fannie Mae’s Detroit Partnership Office, said that “the people who have stayed loyal to the city in these neighborhoods deserve to be heard, but our window of opportunity to leverage this incredibly strong economy and interest in the city is quite fragile and we have to be careful that we don’t let this opportunity pass us by.” Dennis Archer, mayor of Detroit, and new member of Fannie Mae’s advisory council is also tainted by the controversy as one of the Mayor’s sons works for Graimark (one of two developers on

the project) and the Mayor's sister-in-law did legal work for the company at her former law firm and now oversees the quasi-public Detroit Economic Growth Corp. which is providing staff to handle the development for the city. (*Detroit Free press, FREEP web site, 3/11/98; Business Wire, 3/3/98*)

- *Fannie Mae Cites the Issuing of Debt Instruments as Key for Profitable Growth- Fannie Plans to Borrow \$100 Billion in 1998:*
 - Fannie Mae recently held its 14th annual investor visit to the UK where it was announced at a press briefing that one of the key elements to Fannie's profitable growth was the ability to fund portfolio growth by issuing a wide range of debt instruments. According to EVP and Chief Financial Officer Timothy Howard, "our mortgage portfolio of more than \$316 billion gives us the funding flexibility to introduce innovative debt products that are attractive to European investors." Howard noted that European investors showed interest on the agency's recent three-, five- and 10-year benchmark notes. Chairman Jim Johnson announced that mortgage originations in the US are expected to rise to an all-time high of \$1.1 trillion in 1998. Johnson expects the favorable growth outlook for the US mortgage market (valued at \$4 trillion) should generate strong earnings growth for Fannie Mae. Mr. Johnson stated that "in 1997, Fannie Mae reported its 11th consecutive year of record earnings, and we are solidly on track for double digit earnings growth in future years." Mr. Johnson also noted that the share of all US residential mortgages financed by Fannie Mae is expected to rise to more than 35% in 1998 from 30% in 1997.
 - Fannie Mae said it will require approximately \$100 billion of long-term funding next year and will continue to develop its benchmark note debt issuance program. Fannie Mae Treasurer Linda Knight said Fannie would continue to raise funds via domestic issuance of callable debt and through its newly inaugurated international benchmark note program. This year, Fannie plans to raise \$80-\$85 billion in the public debt markets, approximately half from the benchmark note program. Fannie Mae said it will issue five- and 10-year bonds of between \$2.0 billion and \$5.0 billion in size from the program every quarter. Like Treasuries, Fannie Mae's bonds are rated triple-A. Knight said that Fannie might consider issuing a euro-denominated benchmark bond once a more robust euro swap market has developed. (*Dow Jones Newswire, 3/19/98; Reuters, 3/19/98*)
- *Fannie Mae Opens New Statewide Partnership Office in Denver:*
 - Fannie Mae officials and Mayor Wellington Webb held a press conference to announce the opening of a new statewide Fannie Mae Partnership Office and to release the four-year results of the \$1 billion "HouseDenver" affordable housing plan. Fannie plans to open the statewide office in April. Jamie Gorelick, Vice Chair of Fannie Mae and Tom Lund, SVP for Fannie Mae's Southwestern Regional Office were also in attendance at the press conference. Gorelick presented Mayor Webb with an "Affordable Housing Hero" award for his affordable housing commitment. (*Business Wire, 3/20/98*)
- *Fannie Mae Introduces On-Line Accounting System for Reverse Mortgages:*

- Fannie Mae introduced an online loan accounting system for servicing reverse mortgages – the Shared Accounting and Reporting System (ShAReS). According to Fannie Mae, the system is the industry’s first real time servicing transaction processing system for reverse mortgages. ShAReS was tested for a year in a pilot program with Wendover Financial Services and will now be available to all Fannie Mae reverse mortgage lenders through MortgageLinks, Fannie’s electronic commerce network for the mortgage industry. The new system allows lenders to (1) update loan activity in real time; (2) search for loans or transactions; (3) view or download monthly or daily reports; (4) quote loan payoffs over the phone with only two pieces of information needed – loan number and effective date; and, (5) submit a trial balance for automated reconciliation and use a prior period adjustment for forward reconciliation.
- Fannie Mae buys two types of reverse mortgages: a home equity conversion mortgage insured by HUD and a Fannie Mae conventional reverse mortgage (Home Keeper). At the end of 1997, Fannie Mae had 22,000 reverse mortgage loans in its portfolio, making Fannie “the primary conventional reverse mortgage investor,” said Mercy Jimenez, vice president for senior products at Fannie Mae. According to Stuart Feldstein, president of SMR Research, the potential market for reverse mortgages is gigantic, but reverse mortgage lending is “fraught with risk for the lender.” (*Business Wire*, 3/18/98; *Inman News Feature*, 3/18/98; *American Banker*, 3/25/98)
- *Fannie Mae Joins Newly Formed Nat’l Reverse Mortgage Lender’s Association (NRMLA):*
 - Fannie Mae joined the newly formed NRMLA. Nelson Locke, President of Senior Financial Services, will serve on the association’s first Board of Directors. The Consumer Education Committee of the Association plans to work closely with Fannie Mae to design and produce materials used to inform senior citizens about reverse mortgages. (*Business Wire*, 3/19/98)
- *Fannie Mae Invests in Database that Tracks Apartment Financial Information:*
 - Over 100 companies including Fannie Mae contributed to a “first-of-its-kind” database that will track apartment financial performance. The Internet-based database, AptData, will be unveiled by the Multifamily Housing Institute on March 31. The database compiles financial performance and property information from more than 3 million apartment units across the country, representing more than 24,000 properties. The data is standardized and will be available in digital form over the Internet. According to Shaun Brady, executive director of Multifamily Housing Institute, “AptData represents the first time anyone has tried to collect and standardize a critical mass of in-dept performance data for any type of commercial real estate.” For investors and owners of multifamily property, AptData will be used to underwrite and analyze investments based on comparable peer groups. (*Inman News Feature*, 3/12/98)
- *Fannie Mae Announces that It’s Near Midpoint of \$1 Trillion Affordable Housing Goal:*

- Fannie Mae announced at a reception attended by big-city mayors around the US, that it is near the midpoint of its \$1 trillion affordable housing goal by the end of this century. In four years, Fannie has financed \$440 billion of loans to 5.6 million low- to moderate-income families. Fannie Mae said prior to the \$1 trillion commitment declaration, only 55% of the company's total business served the groups targeted. Now, Fannie Mae Chairman Jim Johnson said more than 2/3 of Fannie's business serves targeted families. Allen Fishbein, general counsel at the Center for Community Change in Washington, DC believes, however, that Fannie and Freddie have "increased their efforts by leaps and bounds in recent years," however, he believes there is room for further gains in apartment financing. Mayors Marion Barry Jr. of Washington, Bill Campbell of Atlanta, Emanuel Cleaver II of Kansas City, MO and Elizabeth Flores of Laredo, TX were among the attendees. Cong. Martin Olav Sabo (D-MN) and Cong. Rick Lazio (R-NY) praised Fannie Mae's achievements in the *Congressional Record* and included submissions of congratulatory letters from the Mayors of Hartford, Houston, Kansas City, Miami and Minneapolis.
- Fannie Mae also opened four new Partnership Offices in 1997: Mississippi, Nebraska, New Mexico and Columbus, OH. Fannie Mae now has 29 Partnership Offices across the US and plans to open four more offices in 1998. (*American Banker*, 3/20/98; *Business Wire*, 3/16/98; *Dow Jones Newswire*, 3/16/98; *Congressional Record*, 3/17/98, 3/18/98)
- *Fannie Mae Offers Loan Relief for Flood Victims:*
 - Fannie Mae is providing mortgage relief to flood victims in CA by allowing mortgage servicers the option of suspending loan payments for up to three months, reducing them for 18 months, or in special cases creating longer loan payback plans. Decisions on the options will be made on a case-by-case basis. (*Inman News Feature*, 3/20/98)
- *Fannie Mae Invests in Single-Family Homes in Southeast Washington, DC:*
 - Fannie Mae's American Communities Fund recently invested \$2.7 million of financing for Oxon Creek Townhomes; the first new single-family homes built in Southeast Washington, DC in decades. American Communities Fund is the community development venture capital fund of Fannie Mae. The 210-unit townhome development will provide affordable homes to homebuyers with incomes in the mid-\$20,000 range. The development will eliminate 400 vacant and abandoned multifamily housing units in the neighborhood and homes will range from \$99,500 to \$138,000. (*Business Wire*, 3/18/98)
- *Fannie Mae Helps Sponsor Homebuying Seminar that Offers Participants Certificates that could Lower their Down Payments:*
 - Fannie Mae, the Iowa Finance Authority, and 10 local lenders are sponsoring the fifth annual Credit & Homebuying Seminar, a one-day homebuying seminar with five sessions. The participants who complete the seminar receive certificates that could lower their down payments on a mortgage. The certificates can be taken to participating

lenders to qualify for loans with lower down payments or lower closing costs. The lenders honoring the certificates include: AmerUs Bank, Brenton Bank, Mercantile Bank, Norwest Bank Iowa, Iowa State Bank, NationsBank, and Principal Residential Mortgage. (*Des Moines Register*, 3/20/98)

- *Fannie Mae and PNC offer Free Classes on Homeownership:*
 - The Fannie Mae Foundation and PNC Bank are sponsoring two series of free classes in Philadelphia to teach city residents about homeownership. The classes will be held at Temple University. (*Philadelphia Inquirer*, 3/18/98)
- *Fannie Mae Joins with NBA Basketball Player to Educate High School Students on Credit:*
 - Fannie Mae joined Jerome Williams of the Detroit Pistons at a credit awareness training class for 85 high school students. (*Business Wire*, 3/24/98)

Freddie Mac

- *Freddie Mac Will Issue Global Noncallable Debt like Fannie's "Benchmark" Issues:*
 - Freddie Mac will begin offering global noncallable debt in April and plans to issue the noncallable debt as bullet securities each quarter. The issues will be called "Reference Notes" and will be offered in a minimum size of \$4 billion. Freddie will focus on the overseas market much like Fannie. (Fannie began their intermediate-term noncallable note program in January.) Many investors have considered Fannie's benchmark notes as a proxy for government debt and observers expect overseas interest to remain strong. Freddie sold approximately \$40 billion of debt in 1997 with maturities greater than one year, and depending upon the market, anticipates offering a similar amount in 1998. In 1997, nearly \$15 billion of the corporation's borrowing needs were bullet securities with five- to 10-year maturities. (*American Banker*, 3/24/98; *Freddie Mac Press Release*, 3/16/98)
- *Freddie Mac Announces New Mortgage Appraisal Service on their GoldWorks® Network:*
 - Beginning in the second quarter, lenders using Freddie Mac's GoldWorks® electronic network will be able to use a new service, called Rapid Request™ that will allow lenders to order, manage, receive and review appraisals using a national network of appraisal providers. Rapid Request™ will be provided through ACI Development and MPACT Immedia. The new service works as follows: First, lenders choose from a national network of appraisal providers and once lenders make their choice, they can use ACI's Rapid Request software to complete the order. The lender then submits the order to the chosen appraisal provider through the connection facilitated by MPACT Immedia and the GoldWorks® network. After receiving the request, the appraisal provider completes the job and electronically returns the report back to the lender. [As reported in previous *GSE*

Reports (Jan. 30 and Feb. 13, 1998), MPACT Immedia is working with Freddie Mac on an Internet based pilot origination system.] (*Freddie Mac press release, 3/16/98*)

- *Freddie Mac Donates \$1 Million for “The Houses that Congress Built”:*
 - Freddie Mac provided \$1 million to help fund “The Houses that Congress Built,” a bipartisan initiative involving the U.S. House of Representatives, Habitat for Humanity International, and the National Partners for Homeownership. The initiative includes Members of Congress joining with local habitat affiliates to build affordable homes for low-income families in all 435 Congressional districts. As of 3/19/98, 241 House Members (more than ½) had signed up for the program. Leland Brendsel, Chairman of Freddie Mac, Tom Jones, Managing Director – Washington Office for Habitat of Humanity, Speaker Newt Gingrich (R-GA), Congressman Jerry Lewis (R-CA) and Congressman Louis Stokes (D-OH) were invited to participate and speak at the press conference announcing the initiative. (*Freddie Mac press release, 3/17/98, 3/19/98; Press-Enterprise, Riverside, CA, 3/20/98*)
- *Freddie Mac Was in “Top Ten” List of Soft Money Donors to the Republican Party:*
 - Freddie Mac contributed \$250,000 last year in soft-money donations to the Republican Party, according to Common Cause. Freddie Mac was ranked as the ninth largest soft-money contributor to the Republican Party. Common Cause’s analysis was based on reports to the FEC. (*Washington Post, 3/13/98*)
- *Freddie Mac Enhances Automated Underwriting System – Loan Prospector®:*
 - Beginning April 19, Loan Prospector ® users will benefit from an improved Accept Plus (risk evaluation program) underwriting and documentation feature; an enhanced credit reconciliation process; and a newly designed collateral assessment feature. (*Freddie Mac press release, 3/16/98*)
- *Freddie Mac Prices Its Preferred Stock Offering – S&P Rates AA-:*
 - Freddie Mac priced the offering of eight million shares of fixed-rate, non-cumulative as to dividends, perpetual preferred stock. The pricing of the preferred stock was set as \$50 per share, with a dividend of 5%. Freddie Mac will have the option to redeem all or part of the shares on or after March 31, 2003. Standard & Poor’s assigned its double-‘A’-minus rating to Freddie’s preferred stock issue. S&P reports that “the affirmation of the senior debt rating reflects the company’s status as a government-sponsored enterprise (GSE). While there is no US government guarantee on Freddie Mac’s obligations, GSEs including Freddie Mac benefit from the ability to issue debt obligations pursuant to its GSE charter.” (*Freddie Mac press release, 3/18/98; Business Wire, 3/20/98*)
- *Freddie Mac Releases Results on Refinancings:*

- Freddie Mac released the results of a representative sample of refinanced loans that found that a larger percentage of homeowners refinanced into loans of at least a 5% higher amount than did so in 1996. “Higher loan amount” refers to loan amounts that were at least 5% greater than the amortized unpaid principle balance (UPB) of the original loan. The review found that the percentage of refinancings that resulted in a loan with an UPB at least 5% higher than the original loan was 59%, up from 54% in 1996. These estimates come from a sample of properties on which Freddie Mac has funded at least two successive loans. (*Freddie Mac press release, 3/16/98*)
- *Freddie Mac Assists Local DC School:*
 - KaBoom! (a District-based nonprofit organization) has helped join together Freddie Mac and local community groups to build a playground for an urban DC elementary school – J.C. Nalle Elementary. KaBoom! believes building playgrounds breaks down barriers and creates symbols of optimism. Freddie Mac invested between \$50,000 and \$60,000 for the J.C. Nalle project. (*Washington Business Journal, 3/16/98*)
- *Freddie Mac Creates New Position - Director of Wall Street Sales, Multifamily Division:*
 - Freddie Mac named George Wisniewski, director, Wall Street sales in its Multifamily division, Wisniewski will be responsible for actively marketing Freddie Mac Multifamily products to Wall Street firms and other capital markets groups. (*Freddie Mac press release, 3/19/98*)

Federal Home Loan Banks

- *Federal Housing Finance Board (FHFB) Still Undergoing Controversy Over White House Termination of Board Member - FHFB Board Holds Meeting to Discuss Investment Practices and other FHLBank Business:*
 - In the March 13th issue of the *GSE Report*, we reported that the White House had terminated the FHFB membership of Lawrence Costiglio. The termination, effective March 23 was two days before a scheduled meeting of the FHFB on March 25. A White House spokesman told *MortgageWire* that Costiglio’s political views clashed with President Clinton’s and “even though he is a Democrat, Larry Costiglio has fought the Administration on practically every issue that has come before the Finance Board.” Another senior White House official said “the guy [Costiglio] is a Democrat. He could switch parties and [Senate Majority Leader Trent] Lott could put him back up...It’s a Democratic seat, it’s our Democratic seat.”
 - Costiglio has decided to fight the termination in a number of ways. Despite his termination, Costiglio showed up at the March 25th meeting anyway and proclaimed that he would “take his rightful seat.” Chairman of the FHFB Bruce Morrison insisted,

however, that Costiglio sit with the public and stated that “if there is to be further review into this matter, it must be the President who makes the decision, not the finance board.” Costiglio told reporters after the meeting that he may challenge the firing in court and he is consulting with attorneys on the matter. Costiglio believes his termination was unjust, illegal, and “subject to legal challenge.” He said, “I feel obligated to the board and to those it serves to continue my service until a successor has been appointed and qualified.” Costiglio has also written to Attorney General Reno at the Justice Department to investigate the alleged unlawful conduct by Morrison calling the actions in question “unlawful” and “could jeopardize the independence” of the FHFB. Costiglio said he was particularly concerned that Chairman Morrison is using his position “to exact compliance” by the FHLBank Presidents and the public interest directors of the individual banks with his policies and objections. Costiglio also charged that the Chairman had threatened the compensation of the FHLBank Presidents if they did not support the Chairman’s policies and initiatives. Costiglio thinks Chairman Morrison has overstepped his legal authority by engaging in such actions as detailing Board staff to other agencies. In a letter to top members of the House and Senate Banking Committees, Costiglio noted that with his removal, “Morrison will have achieved the removal of dissent from the Board and control thereof.” This would effectively result in the Administration’s control of an independent agency.” Chairman Morrison has called Costiglio’s charges “factual misrepresentations” and in a statement, the Chairman stated that the allegations were false and “part of his [Costiglio’s] continuing attack on the Constitutional authority of the President of the United States.”

- According to Section 2A(d) of the FHLBank Act, a member of the board of directors of the Finance Board “may continue to serve until a successor has been appointed and qualified.” However, it is silent on the issue of removal. Costiglio stated that: “First and foremost, I believe my presence on the board until a successor has been appointed and qualified is essential to preserve the integrity and independence of the Federal Housing Finance Board. I believe my removal is yet another attempt by Chairman Morrison and the Administration to control the board by stifling all dissent thereon.”
- Finance Board member J. Timothy O’Neill, a board member who often votes in alignment with Costiglio, said that the board is in an “uncertain situation” regarding Costiglio’s termination. He said that he had reviewed the statute and found the president’s actions “questionable” because the position should not end until a successor is “appointed and qualified.” O’Neill also asked the Department of Justice to clarify the matter. However, Chairman Morrison rejected O’Neill’s motion to research the matter and declared the request “out of order and out of [the board’s] jurisdiction.”

Ousted FHFB Member has Support on Capitol Hill:

- Chairman of the Senate Banking Committee, Alfonse D’Amato (R-NY) called the President’s termination of Costiglio “legally dubious” and has promised “vigorous oversight” of the Finance Board and the termination matter. Senator Lauch Faircloth (R-NC) demanded that the Administration reinstate Costiglio. At a hearing on a FHLBank bill on 3/12/98, Senator Faircloth stated that if the Administration did not reinstate Costiglio, “this committee should think very seriously...about whether anymore Clinton

banking appointees will be confirmed.” Senator Faircloth noted that he would oppose any reform of the FHLBank System unless the FHFB Chairman’s power is curbed.

FHFB Decides to Hold Public Meeting & Publish Report for Comments on Non-Mortgage Investments:

- At the March 25th FHFB meeting, the Board voted to publish a report for public comment and hold a public hearing (May 11) on the non-mortgage investments of the FHLBanks. A staff report was discussed at the meeting that states that many of the assets held in the investment portfolios of the FHLBanks “bear little if any relationship” to the bank’s mission of supporting housing. “Such investments, beyond those required for liquidity, can thus be considered non-mission related.” The report further stated that the principal purposes of these primarily short-term investments have been to generate income to service thrift bailout bonds and to pay a dividend sufficient to attract and retain members. Chairman Morrison said the recommendations contained in the staff report were not a formal proposal but the recommendations would lay the groundwork for proposed new investment rules later this year.
- The report found that the FHLBanks held approximately \$149 billion of investments at the end of 1997, some \$98 billion of which was in money market instruments. The staff paper found that most of the most of the non-mortgage investments were in the form of “Treasury and agency securities, fed funds, resale agreements, commercial paper, bank and thrift notes, [and] bankers’ acceptances and deposits.” Under the scenario favored in the staff report, the holdings of such money market instruments could be cut in half without impairing the safety and soundness of the system or driving out members. The report also stated that the FHLBanks investments in short-term money-market investments was acceptable during economic distress, however, “now that membership and advances are at record levels and System income exceeds \$1.5 billion, the need to maintain such investments – which averaged \$98 billion in 1997 – should be examined in light of the Banks’ public mission as GSEs.”
- The staff report even questioned the value of mortgage-backed securities to housing and to the extent that the MBS investments support their housing finance mission “is debatable.” The report stated that “the FHLBanks’ presence in these markets [MBSs] may not result in increased availability of funds for housing, or in lower cost funds. Bank investments in MBS, therefore, could be considered as providing less ‘value’ to housing than advances or other investments that provide financing that is not generally available or is available at lower levels under less attractive terms.”
- The staff report also noted that the “FHLBanks, as GSEs, can be viewed as representing a social compact between the banks and their members and the federal government.” According to the report, “the federal government bestows upon the banks’ certain benefits through their GSE status, and such federal benefits should be used to fund activities that safely and soundly further the Banks’ public purposes.”

- The staff paper discussed three options for limiting investments that tied the allowable levels of money market investments to the levels of consolidated obligations outstanding. Under one option, advances would be required to be at a minimum of 70% of consolidated obligations, with MBSs “limited to the maximum of the existing 300 percent of capital limit or 20 percent of Cos (consolidated obligations) and money market investment would be limited to 10%.
- As part of a series of efforts to transfer more authority to the individual FHLBanks from the FHFB, the FHFB also approved a proposal giving the banks, rather than the Finance Board, the power to certify people as eligible to be directors.

FHFB Delays Controversial Vote on Agricultural/Commercial Lending After Objections from Treasury:

- The FHFB also delayed until April 9th a vote on a final rule that would let any loan secured by farm or business property qualify for system advances as long as there is a residence on the property. Treasury Under Secretary John Hawke said in a letter to the FHFB that the proposal “would further erode” the FHLBank System’s focus on housing finance by allowing greater support for agricultural and commercial lending and noted that no analysis was provided in support of the proposed rule. Under Secretary Hawke urged the FHFB not to adopt the proposed rule and stated “I believe the decision whether the Federal Home Loan Banks should dilute their mission by using their federal subsidies in support of agricultural and commercial lending is one for the Congress to make.” (*American Banker*, 3/16/98, 3/23/98, 3/26/98; *BNA Daily Report for Executives*, 3/26/98; *Dow Jones Newswires*, 3/13/98, 3/17/98, 3/24/98, 3/25/98; *National Mortgage News web site*, 3/16/98, 3/27/98; *Washington Post* 3/18/98)
- *Federal Housing Finance Board Approves More Borrowing:*
 - The Federal Housing Finance Board (FHFB) voted unanimously to let its Office of Finance continue borrowing without limit through the rest of the year. Without the voted-approval, the office’s ability to issue new debt would have expired March 31. The Office of Finance of the FHFB issues debt on behalf of the FHLBank System’s 12 banks and in the past has been authorized to issue debt for a full year. However recent concerns about the FHLBanks’ use of funds prompted the FHFB in December to limit that power, and they instituted the March 31 expiration.
 - The FHLBank System sold \$2.14 trillion in debt securities in 1997, with short-term debt sales accounting for \$1.97 trillion. Considerable borrowed funds have been used to fund short-term investments.
 - Concerns have been expressed that the FHLBanks use their low-cost government borrowing to invest in short-term money market accounts rather than to make advances for home loans. Chairman of the House Banking Committee Jim Leach (R-IA) called on the System to forego “government-advantaged arbitrage activities” and instead make “meat and potatoes advances” to mortgage lenders. FHFB Chairman Bruce Morrison

said the banks' borrowing practices are still a problem, but instead of restricting their borrowing, he wanted to expand the types of housing-related investments they can make. The FHFB released its recommendations for improving the FHLBank System's investment policies on March 25 (see story above). (*American Banker-Bond Buyer*, 3/17/98; *Dow Jones Newswires*, 3/13/98)

- *FHFB Chairman Morrison is on Administration's List for US Ambassador to Ireland:*
 - FHFB Chairman Bruce Morrison's name is included in the Clinton Administration's list for US Ambassador to Ireland. Mr. Morrison is a former Democratic Congressman from Connecticut who sponsored legislation to help Irish immigrants obtain US visas and has also been involved in peace talks. Other names on the list include lobbyist Paul Quinn, Education Secretary Richard Riley, former AFL-CIO treasurer Tom Donahue, and Peace Corps Director Mark Gearan. The current Ambassador Jean Kennedy Smith will retire in July. (*American Banker*, 3/23/98)
- *FHLBank of Atlanta Helps First Time Homebuyers:*
 - The FHLBank of Atlanta announced that it was offering \$1 billion in matching funds to FHLBank of Atlanta member financial institutions for qualifying first-time homebuyers. The funds can only be used for downpayment and closing cost assistance. (*Business Wire*, 3/23/98)

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