

# The **GSE** REPORT <sup>TM</sup>

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## Contents of GSE Report <sup>TM</sup>

**“I’m absolutely convinced the playing field [between the GSEs and private-sector companies] isn’t level.” - Cong. Christopher Shays (R-CT) after questioning the GSEs on whether their federal benefits allowed them to unfairly compete in the marketplace (Comments made during House Capital Markets Subcommittee hearing, 3/27/01 (*Dow Jones Newswire*, Jennifer Corbett Dooren, 3/28/01))**

**“It’s a scandal that these two government subsidized and Congressionally-chartered enterprises [Fannie & Freddie] are spending millions of dollars to become political players at taxpayer expense...But it is even more troubling if they are not playing by the rules of campaign finance, which would be the ultimate insult to all American taxpayers.” - National Taxpayers Union President John Berthoud (*NTU press release*, 3/27/01)**

### ***Major Events***

- Study finds that Fannie & Freddie’s automated underwriting systems resulted in a smaller percentage of loans for minorities and low-income borrowers than similar systems developed by private-sector companies ([p. 5](#))
  - Study also finds that private-sector companies’ automated underwriting systems approve 10% more borrowers for loans than Fannie & Freddie’s automated underwriting systems
  - Three mortgage insurance companies sponsored the study
  - Freddie’s response to the study was “We’d like to get rid of MI [mortgage insurance]”
  - Study concludes that if lenders had more choices among the automated underwriting systems, a greater number of prospective homebuyers would receive loan approvals
  - John Taylor, President and CEO of the National Community Reinvestment Coalition testified last year that the GSEs’ regulators “should encourage a wide diversity of credit scoring systems, competing against each other in developing sound and flexible underwriting criteria. This will open more doors to homeownership for minorities and low- and moderate-income borrowers.”
- Treasury Secretary Paul O’Neill says it is “legitimate” to discuss legislative ideas about reducing the “preferential position” or reducing the “impact” of the GSEs in the “competitive galaxy of how capital is provided to housing markets” ([p. 7](#))
- House Financial Services Committee’s Capital Markets Subcommittee holds hearing on Fannie & Freddie’s compliance with their voluntary risk management agreement ([p. 8](#))
  - Cong. Baker still plans on introducing a bill to strengthen regulation of the housing GSE – will either create a new GSE regulator under Treasury or the Fed, may leave FHLBanks out
  - Both Fannie & Freddie said they would welcome the presence of a strong regulator
- Senate Banking Committee encourages Senate Budget Committee to change the budget process to account for the GSEs’ subsidies and unfunded liabilities from the GSEs’ implied federal guarantee ([p. 16](#))
  - Senate Banking Committee calls the GSEs’ federal subsidies significant contingent liabilities for US taxpayers
  - Senate Banking Committee recommends that Fannie & Freddie’s safety and soundness regulator – OFHEO - be given full funding to carry out its oversight

- Freddie's loan to LendingTree comes under fire ([p. 17](#))
  - OFHEO is reviewing Freddie's loan to LendingTree
  - FM Watch charges that the loan is a clear example of "mission creep" and that Freddie is acting like a commercial bank
  - Freddie says the loan is not outside its mission and that LendingTree will use the money to develop its joint technology initiative with Freddie
  - LendingTree, however, initially said the loan would be used for the company's normal operating expenses, including advertising and salaries (the company's two biggest expenses) – LendingTree claimed the loan was entirely separate from its technology partnership initiative with Freddie
  - LendingTree later clarifies that the proceeds of the loan will be used to develop its joint technology initiative with Freddie
  - FM Watch says the LendingTree loan supports its new report on the GSEs' mission creep. (See [p. 27](#) for more information on the FM Watch report.)
- Nation's largest taxpayer group – National Taxpayers Union – calls for FEC investigation of Fannie & Freddie's soft money contributions ([p. 20](#))
  - NTU says hundreds of thousands of dollars of these contributions may be illegal
  - "It a scandal that these two government-subsidized and Congressionally-chartered enterprises are spending millions of dollars to become political players at taxpayer expense...But it is even more troubling if they are not playing by the rules of campaign finance, which would be the ultimate insult to all American taxpayers."
- Freddie eliminates appraisals on most loans with LTV ratios of up to 80% ([p. 21](#))
  - The appraisals can be waived, provided a lender uses Freddie's automated underwriting system and pays a \$50 or \$200 delivery fee to Freddie
  - Appraisal Institute calls Freddie's program "irresponsible" and a "sleight of hand" – says it "adds significantly" to Freddie's potential risk and is misleading since Freddie "seems to be telling people 'you don't really need an appraisal,'" while at the same time making heavy use of appraisal and public property data in its electronic valuation model
  - [Editorial Note: With just one press release, Freddie eliminates business that would otherwise go to appraisal companies. Instead, lenders are charged "delivery fees" that must be paid to Freddie.]

### **All GSEs**

- Mortgage Bankers Association of America releases comprehensive housing agenda, which includes a number of proposals related to the GSEs ([p. 23](#))
  - MBA supports creating a clear distinction between primary and secondary market activities, so Fannie & Freddie can focus on the missions prescribed in their charters – otherwise, consumers will be the ultimate losers
  - MBA supports expansion of the FHLBanks' mortgage purchase plans (such as the MPF and MPP programs), which create competition for Fannie & Freddie in the secondary mortgage market
  - MBA opposes the privatization of Ginnie Mae and opposes using Ginnie Mae as a source of funds to satisfy other government purposes

### **Fannie Mae and Freddie Mac**

- *Banker & Tradesman* editorial says Congress should determine whether through direct or indirect threats, Fannie & Freddie threatened to pull business from several major banks and financial services firms as punishment for criticizing the GSEs ([p. 26](#))
  - Chief executives of Wells Fargo, American International Group (AIG), and GE Capital were all recently quoted in the *Wall Street Journal* as stating that they have faced threats of retaliation from Fannie & Freddie for participating in the Fannie/Freddie watchdog group, FM Watch
  - If the allegations are substantiated, "Fannie Mae and Freddie Mac then deserve to be reeled in and placed under regulatory oversight that keeps them within the boundaries of their charters."
  - Fannie & Freddie claim the allegations are untrue, yet the editorial asks, "What would senior executives of leading financial services corporations have to gain by falsely attributing threats of intimidation and retaliation to Fannie Mae and Freddie Mac, two companies with whom they have long-standing business dealings?"
  - Freddie Chairman Leland Brendsel writes Letter-to-the-Editor denying that Freddie Mac threatened companies
- FM Watch releases new report outlining how Fannie & Freddie's mission creep threatens American consumers ([p. 27](#))
  - FM Watch claims that "GSE mission creep, the risk it poses to taxpayers, and the benefits to GSE shareholders, are all at the expense of the nation's homebuyers."
- Financial services consultant Bert Ely predicts Fannie & Freddie will seek privatization in the next two to four years ([p. 29](#))

- Fannie & Freddie tell Mortgage Bankers Association that they will not expand into the primary market by vowing that they will not originate loans ([p. 30](#))
  - However, as FM Watch Chairman Gerald Friedman states, “the real threat” to lenders of every size isn’t the possibility that the GSEs will become mortgage originators, but their ability to control information. “They don’t want to originate,” he said. “They want to control the gateways and establish the connections...If they control the channel, no one --- no matter how large – will be able to compete with them.”
  - MBA and GSEs deny that their relationship is adversarial
  - MBA president notes, however, that there is a blurring of the roles of the GSEs and that there needs to be some clearly defined guidelines for the GSEs
- *Mortgage Servicing News* column advises Fannie “to make love not war” with its business partners ([p. 31](#))
  - Fannie & Freddie “face a dilemma: to continue growing at a clip that pleases its investors (and stock analysts) it has to cannibalize other pieces of the mortgage industry...Fannie faces a huge decision over the next five years: make peace with those griping about its business practices and find another way to increase earnings (is there another way?) or be prepared to experience bloodshed.”
- *US News and World Report* observes that Fannie & Freddie “are in the line of fire” ([p. 32](#))
  - Scrutiny of the GSEs is likely to continue - “For two Washington and Wall Street favorites, it’s going to be a long, hot summer”
- Fannie & Freddie’s subordinated debt has cheapened significantly compared to its senior debt ([p. 33](#))
- *American Banker* reports that mortgage insiders see the GSEs as “critic-proof” ([p. 34](#))
- Under non-risk based capital rules, OFHEO announces that Fannie & Freddie have met their minimum and critical capital levels ([p. 35](#))

### **Fannie Mae**

- Fannie starts buying back its own debt to arbitrage profits ([p. 36](#))
  - Jim Kellerman with Criterion Investment Management Co. wonders, “where the money is coming from for these buybacks.” Presumably, he states, Fannie will fund the program by issuing new debt
  - Fannie declined to comment on how the company is funding its debt buyback
  - The Fannie program could also place a price bottom under the securities and increase the borrowing activity of securities issues by Freddie unless Freddie implements a similar program
  - As *Dow Jones Newswire* reports, “one key difference between Fannie’s buyback and those of the US Treasury is that, while Uncle Sam is aiming to pay down its debt, Fannie Mae is actually increasing its amount of bonds outstanding.”
- Bowing to pressure from critics and negative publicity, Fannie says it will stop collecting its controversial fees (“equity shares”) from borrowers as part of the company’s reverse mortgage program (targeted to senior citizens) ([p. 37](#))
  - Critics charged that the effective interest rates on some of these reverse mortgages exceeded 30-40% a year
- Fannie says it will work more closely with smaller lenders ([p. 38](#))
  - Fannie wants to help smaller lenders create “virtual” mortgage businesses to compete against large lenders
- Fannie names new members to its National Advisory Council ([p. 38](#))
- Fannie further expands its political reach by including Federal and State officeholders in its press conferences and press releases and increasingly using its partnership offices in press events ([p. 41](#))
  - Fannie has 44 Partnership Offices open across the country
  - Financial consultant Bert Ely believes Fannie’s media events raise ethical questions. “This is an extension of not only their lobbying but also their political action committee contributions,” he said. “Everybody knows what they’re doing. It’s something that many of us find offensive, but that’s how they play the political game.”
  - Fannie claims its partnership offices were created “to get away from Washington,” yet *Real Estate Finance Today* reports that during the first eight months of 2000, Fannie held no fewer than 87 media opportunities across the country with Congressional Members
- Fannie Mae Foundation holds Capitol Hill press conference with lawmakers to distribute checks to homeless service providers ([p. 43](#))
  - Fannie Mae Foundation launches national spring advertising campaign to consumers
  - There’s a “perception in Washington that the company’s philanthropy is calculated to reward friends, punish enemies, curry favor with key members of Congress and brand its name with the public through an expensive television advertising campaign.” - *St. Petersburg Times*
  - “It’s clearly used as hush money to buy silence of groups that might otherwise be critical of Fannie Mae,” said Bruce Marks, one of the housing activists whose criticisms of then-Fannie Mae CEO James Johnson at a conference years ago resulted in a tiff over a grant.
  - *St. Petersburg Times* notes that “at the very least, the foundation’s long reach can call into question the

objectivity of the affordable housing organizations that rally to Fannie Mae's side."

### **Freddie Mac**

- Freddie is investing in Islamic "no interest" loans ([p. 45](#))

### **Federal Home Loan Banks**

- FleetBoston applies for dual FHLBank membership ([p. 46](#))
  - FHLBank of New York supports FleetBoston's request for dual FHLBank membership
  - FHFB is also considering Washington Mutual's request for dual FHLBank membership
  - The FHLBanks of Atlanta, Boston, Des Moines, and San Francisco object to Washington Mutual's application - ask FHFB to issue a broad rule on the issue of dual FHLBank membership instead
  - FHFB is drafting an advance notice of proposed rulemaking on dual FHLBank membership
- Florida lawmakers are considering a bill that would allow small banks and thrifts to pledge FHLBank letters of credit as collateral on public deposits ([p. 47](#))
  - Tennessee and a few other states have passed similar bills

### **Farm Credit Administration/Farm Credit Banks**

- Farm Credit Administration (FCA) delays the comment period on its controversial national charter proposal ([p. 47](#))

### **Ginnie Mae**

President Bush names Ronald Rosenfeld as President of Ginnie Mae ([p. 48](#))

## *Major Events*

**Study finds that Fannie & Freddie’s automated underwriting systems resulted in a smaller percentage of loans for minorities and low-income borrowers than similar systems developed by private-sector companies**

**Study also finds that private-sector companies’ automated underwriting systems approve 10% more borrowers for loans than Fannie & Freddie’s automated underwriting systems**

**Three mortgage insurance companies sponsored the study**

**Freddie’s response to the study was “We’d like to get rid of MI [mortgage insurance]”**

**Study concludes that if lenders had more choices among the automated underwriting systems, a greater number of prospective homebuyers would receive loan approvals**

**John Taylor, President and CEO of the National Community Reinvestment Coalition testified last year that the GSEs’ regulators “should encourage a wide diversity of credit scoring systems, competing against each other in developing sound and flexible underwriting criteria. This will open more doors to homeownership for minorities and low- and moderate-income borrowers.”**

- **A study sponsored by three mortgage insurance companies found that Fannie and Freddie’s automated underwriting systems resulted in a smaller percentage of loans for minorities and low-income borrowers than similar systems developed by private-sector companies.** The study also found that Fannie and Freddie have a 10% lower acceptance rate than similar systems developed by private-sector companies. The study found that the private sector companies’ automated underwriting systems, when compared with Fannie and Freddie’s automated underwriting systems, produced substantially more automated loan approvals for consumers. The findings were the same regardless of race, income, down payment or loan account, according to the study. Mercer Management Consulting, Boston, conducted the study, released on March 27. The Mercer study compared acceptance rates on 153,265 loans that were fed through Fannie and Freddie’s automated underwriting systems, and then through the automated underwriting systems of GE Capital Mortgage Insurance, United Guaranty Mortgage Insurance, and Republic Mortgage Insurance. **The study concludes, “if lenders had more choices among the automated underwriting systems that score home loans, a greater number of prospective homebuyers would receive loan approvals.”**
- **The study tracked both the percentages of loans approved by two out of three of the private companies’ systems, as well as the average approval rate for all three private companies’ systems, which found the following results:**

<b>Overall Fannie Mae/Freddie Mac AU Systems Rate</b>	<b>Two-Out-Of-Three Private Companies’ Systems Accept Rate</b>	<b>Average of Three Private Companies’ Systems Accept Rate</b>
78.9%	89.5%	86.6%

- When analyzing the results by racial background, there were notably higher acceptance rates for the private companies' automated underwriting systems:

<b>Borrower Race</b>	<b>Fannie Mae/Freddie Mac AU systems accept rate</b>	<b>Two-out-of-three private companies' systems accept rate</b>	<b>Average of three private companies' systems accept rate</b>
African American	65.8%	77.9%	75.9%
Hispanic	71.9%	79.8%	76.7%
Asian	78.2%	89.3%	85.8%
White	79.7%	91.3%	88.3%

- A Fannie Spokeswoman called the study flawed, and said that 44% of loans it purchased last year did not even go through its automated underwriting system, Desktop Underwriter. A Freddie Spokeswoman called the study another tactic by FM Watch and questioned the need for mortgage insurance at all. "We'd like to do away with MI," she said. "There are many alternatives to MI that would benefit both consumers and lenders."
- Mercer Management Consulting says that the study was done to help Ginnie Mae evaluate a proposal that would allow Ginnie Mae to accept conventional low down payment mortgage loans for the first time. The proposal, according to Mercer Management, would create an opportunity to introduce to the mortgage marketplace additional proven automated underwriting systems beyond the dominant systems of Fannie and Freddie. Mercer Management said the study documents that "authorizing such systems for use in the proposed public-private partnership would bring advantages to homebuyers." An MI Spokesman said the report was not "meant to be an attack on the GSEs." (*National Mortgage News Daily*, 3/27/01; *American Banker*, Erick Bergquist, 3/29/01; *Wall Street Journal*, Nicholas Kulish, 3/28/01; *Washington Post*, Sandra Fleishman and Albert Crenshaw, 3/27/01; *Mercer Management Consulting Study on Automated Underwriting Systems*, 3/27/01)

[Editorial Note: Competing automated underwriting systems would be better for homebuyers]

- In testimony before the Capital Markets Subcommittee last year, John Taylor, President and CEO of the National Community Reinvestment Coalition stated that the GSEs' regulators "should encourage a wide diversity of credit scoring systems, competing against each other in developing sound and flexible underwriting criteria. This will open more doors to homeownership for minorities and low- and moderate-income borrowers. In addition, the regulatory oversight agency should continue conducting fair lending testing of the GSE underwriting systems as HUD has just started doing." (*Testimony of John Taylor, President and CEO of the National Community Reinvestment Coalition before Capital Markets Subcommittee*, 6/15/00)
- "Fannie and Freddie could gain dominance over the AU [automated underwriting] market and lower the level of competition that would otherwise have occurred. As a result, home buyers would pay more to buy a home than they would have otherwise." – Ron Feldman, Senior Financial Analyst, Federal Reserve Bank of Minneapolis (*"Mortgage Automation Threat," The Region – Federal Reserve Bank of Minneapolis*, 12/96)
- "To the extent that the GSEs now finance a significant portion of their sector of the mortgage market, the willingness of a GSE to purchase a mortgage has become a far more significant factor in deciding whether to originate that mortgage. The GSEs' automated underwriting systems are

increasingly becoming the means by which originators decide to lend. This technology will make the process more efficient. In the long run, however, this trend may result in less diversity in credit decisions and less price competition.” – Former Treasury Under Secretary Gary Gensler  
(*Testimony of Treasury Under Secretary Gary Gensler before House Capital Markets Subcommittee, 3/22/01*)

- HUD has been conducting a fair-lending review of Fannie and Freddie’s AU systems [which control 95% of the AU market] for almost two years. In February 1999, HUD sent letters to Fannie and Freddie requesting information to ensure that the GSEs’ systems comply with fair-lending standards. The GSEs did not release this information until January 31, 2000. A March 1999 Urban Institute study commissioned by HUD found that Fannie and Freddie’s underwriting guidelines may inadvertently have a disparate impact on minority borrowers. **The study also noted that Fannie and Freddie “do not appear to have gone as far as some primary lenders to serve low-income and moderate-income borrowers and to minimize disproportionate effects on minorities.”** The study found that, **“Primary lenders are making more aggressive efforts” to serve lower income and minority homebuyers “by offering loan products with underwriting guidelines that are more flexible than the GSEs’ guidelines.”** Further, the study found that **“depository lenders are serving low- and moderate-income borrowers better than the GSEs and so the percentage of loans purchased by the GSEs that are originated to low- and moderate-income borrowers is less than the percentage of loans originated in the primary market.”** The study also found that “there is some evidence that the GSEs’ purchase of loans made to black and Hispanic homebuyers have actually declined (in share and absolute number) over the last two years.” HUD was expected to complete its fair lending review of Fannie and Freddie’s automated underwriting systems by year-end 2000 but the review has still not been completed. (*HUD/Urban Institute Study, “A Study of the GSEs’ Single Family Underwriting Guidelines,” April 1999*)

**Treasury Secretary Paul O’Neill says it is “legitimate” to discuss legislative ideas about reducing the “preferential position” or reducing the “impact” of the GSEs in the “competitive galaxy of how capital is provided to housing markets”**

- During a Question and Answer period at the National Association of Business Economics Policy conference, Treasury Secretary Paul O’Neill clarified earlier comments about Fannie and Freddie. Secretary O’Neill was asked the following question: “What concerns do you have about the continuing growth of Fannie Mae and Freddie Mac...Particularly in light of the recent charges by some of their private sector competitors that Fannie and Freddie are engaging in intimidation practices?”
- According to transcripts, Secretary O’Neill gave the following response:  
“...You know, these are large, important institutions in our society. And I’m sure you must have seen what I said in a hit and run Bloomberg interview when I was asked about these organizations. And I said in passing...I’m learning that it’s not ok to say what you think in passing any more, but I did anyway. And I’ll repeat it here, because it’s true. Frank Raines [Fannie’s Chairman and CEO] is a person I’ve known for a very long time, served with him together on a board at something called the MDRC...So that’s the base from which I know Frank Raines as a decent, caring human being, trying to make things better. And I observed that. And so it was hung around my neck, ‘Well, you can’t be objective about Fannie Mae because Frank Raines he admits is a good friend of his.’...I find that really difficult to live with that characterization.”

“To the more important point about these institutions, there’s an ongoing conversation in town, and the lobbyists are hired and deployed on both sides of the issue that I think essentially boils down to the question, which is this: As a society, should we give some part of a preferential place in capital markets to housing? That’s the question.”

“And there are people who believe, I think in good faith, that the answer is no. Most of them would not like to walk out here and stand with me and say that; they’d rather do stealth attacks. But I’m here to tell you, as an economist...that’s the essential issue.”

“And how we deal with it, we’ll see. There are legislative ideas about how one could reduce the preferential position or reduce the impact of these particular institutions in the competitive galaxy of how capital is provided to housing markets, and that’s a legitimate conversation. And I think it’s going to go on.” (*Transcript of Treasury Secretary Paul O’Neill’s remarks at the National Association of Business Economics policy conference, Federal Document Clearing House, 3/27/01*)

**House Financial Services Committee’s Capital Markets Subcommittee holds hearing on Fannie & Freddie’s compliance with their voluntary risk management agreement**

**Cong. Baker still plans on introducing a bill to strengthen regulation of the housing GSEs – will either create a new GSE regulator under Treasury or the Fed, may leave FHLBanks out**

**Both Fannie & Freddie said they would welcome the presence of a strong regulator**

- The Financial Services Committee’s Capital Market Subcommittee held a March 27 hearing to review Fannie’s and Freddie’s compliance with the voluntary risk management agreement they entered into last year. Freddie’s Chairman Leland Brendsel and Fannie’s Executive Vice President and CFO Timothy Howard testified.

In summary:

1. Cong. Richard Baker (R-LA) says he still plans to introduce legislation to strengthen regulation of the GSEs, hopefully before the April recess. His new bill would take oversight of Fannie and Freddie out of the hands of OFHEO. “They [OFHEO] have been poorly funded, we’ve had annual legislative battles, and they have high staff turnover,” he said. “We have to have a regulator that has credibility, funding, and professionalism.” Cong. Baker said he is considering placing oversight in the hands of separate office dealing with the GSEs either within the Treasury Department or the Federal Reserve. At this point, Cong. Baker said he is considering leaving the FHLBanks out of the new regulatory structure. While including the FHLBank System in his legislation is still “under examination,” he said his tendency is not to include the FHLBanks. Some issues may be addressed by requiring the new regulator to conduct a series of studies (with strict timelines) on GSE practices and their implications. He also suggested to reporters after the hearing that a committee could be established that would determine if Fannie and Freddie are engaging in activities outside their charters. He noted that a similar structure was created in the Gramm-Leach-Bliley Act. Cong. Baker stated that he would share his legislation with executives from Fannie and Freddie and Ranking Member Cong. Paul Kanjorski (D-PA) prior to introduction.
2. House Financial Services Committee Chairman Michael Oxley (R-OH) suggests that Congress examine the existing framework for regulating Fannie and Freddie and “consider whether the

current division of regulation between OFHEO and HUD ought to be streamlined and whether the regulators have the powers they need to be effective.”

3. Cong. Baker stated that the CBO study estimating the GSEs’ subsidies is expected to be released soon and may be the topic of another hearing.
4. Both Fannie and Freddie said they would welcome the presence of a strong regulator, which they said would help increase their stature in the eyes of the market. When asked if Congress should give greater power to the GSEs’ regulators. Brendsel said, “We support a strong, credible and effective regulator.” Ultimately, the decision would be up to Congress. Howard said a strong regulator “is very much in our interest.”
5. Although Freddie’s controversial amendment to self-insure mortgage loans failed a few years ago, Brendsel still thinks “it’s a good idea.”
6. Brendsel and Howard were questioned about allegations of threats by the GSEs. Howard said the allegations were “completely baseless.” Howard said the only specific charge that was mentioned in recent articles was Wells Fargo’s allegation that Fannie had removed Wells Fargo from the list of approved bidders for Fannie Mae bonds. Howard said this was untrue. Brendsel said the allegations of threats were untrue and confirmed that no one in his company had engaged in threats. If it were brought to his attention that an employee had engaged in threats, he would review the matter and potentially fire them.
7. Fannie said it has met all six of the components of its voluntary risk management agreement made last October to increase capital and information disclosure.
8. Freddie said it has met five of the six components – expects to put in place the final component on interest rate risk in April.
9. There was a lot of praise for Fannie and Freddie’s adherence to the voluntary risk management agreement. Howard noted, however, that Fannie was already conducting several of the activities in the voluntary agreement. Howard stated that conforming to the voluntary agreement entailed some costs but the agreement mostly codified practices that the company had already taken. Brendsel stated that there were some costs involved, particularly in its issuance of subdebt, but the costs were more than offset by providing better assurances to investors. Fannie and Freddie claimed that their compliance with the voluntary agreement would be regulated internally through its own organizations and externally by OFHEO through its regular examinations of the GSEs.
10. Cong. Christopher Shays (R-CT) asked the GSEs very tough questions.
11. Many of the Democratic Members were highly supportive of the GSEs for their work in affordable housing and combating predatory lending.

## Opening Statements

### Opening Statement of Financial Services Committee Chairman Cong. Oxley (R-OH)

- Fannie and Freddie are well managed and highly sophisticated institutions.
- “However, in light of their size and growth, a number of concerns have been raised. These include the adequacy of their supervision, the nature of their mission, and the risk they could pose to the financial system in the event of a downturn.” The voluntary agreement addresses many of those concerns.
- Suggests Congress examine the existing GSE regulatory framework and “consider whether the current division of regulation between OFHEO and HUD ought to be streamlined and whether the regulators have the powers they need to be effective.”
- “More effective regulation, along with improved market discipline resulting from the voluntary agreement, could give Congress and the markets even greater confidence in Fannie and Freddie.”

### Capital Markets Subcommittee Chairman Richard Baker (R-LA)

- Regarding recent news reports on allegations of threats by the GSEs to their business partners, he hopes that “both sides of these disputes will promptly cool their rhetoric.” He states, “While these charges may deserve consideration by the subcommittee they are not the subjects of today’s proceedings. I do not think the subcommittee should jump recklessly into these disputes.”
- Called the voluntary risk management agreement a “meaningful first step” to ensure safety and soundness. Was pleased with the GSEs’ implementation of the voluntary risk management agreement to date.
- Noted that Fannie and Freddie were the third and seventh largest companies, respectively in the world.
- Noted that Fannie and Freddie’s outstanding debt is expected to surpass Treasury debt by 2005 and that the GSEs operate with less equity capital per dollar of debt than other financial institutions.

### Ranking Member Paul Kanjorski (D-PA)

- During last year’s GSE hearings a consensus was reached that: (1) the US has the most successful housing finance system with the GSEs playing an important role; (2) Fannie and Freddie have grown significantly in recent years; and (3) we must have strong, independent regulators for the housing GSEs with the resources to get things done
- Legislation impacting the GSEs must be done cautiously.
- Suggests exploring a “modernizing” of the GSEs’ mission. Suggest that the GSEs could work to improve economic development in distressed areas and create a secondary market for investments made pursuant to CRA.

### Cong. Stephanie Tubbs Jones (D-OH)

- “If it ain’t broke, don’t fix it.” There are no safety and soundness concerns about Fannie and Freddie. “All I can say is let them do their job.”
- The housing market has not reached a saturation point. There is still a need for housing assistance for the African American and Hispanic communities. Need Fannie and Freddie for affordable housing and eliminating the homeownership gap between whites and minorities.

### Cong. Robert Ney (R-OH)

- Fannie has invested in his district.
- The voluntary risk management agreement exceeds the standards for which other financial institutions are held.

Cong. Gregory Meeks (D-NY)

- Creating Fannie and Freddie was one of the wisest things Congress has ever done.
- Fannie and Freddie have a significant impact on minority communities.

Cong. Spencer Bachus (R-AL)

- Fannie and Freddie have shaped the secondary market.
- The US has one of the best housing finance systems in the world.
- The GSEs' advantages are offset by the GSEs' affordable housing mandates and strong regulatory oversight that other private sector entities do not have.

Cong. Ruben Hinojosa (D-TX)

- Fannie and Freddie are doing an admirable job for affordable housing, particularly in his district in South Texas.
- Housing has not reached a saturation point. There are still gaps in homeownership, particularly in the Hispanic community in his district.
- Congress should try to be careful not to cause unintended consequences when examining the GSEs.

Cong. Steve Israel (D-NY)

- Congress got it right when it created Fannie and Freddie.
- Fannie and Freddie are well-run, safe companies.

Cong. Brad Sherman (D-CA)

- Agrees with Cong. Israel.
- Fannie and Freddie do a lot for homeownership

**Panel:**  
**Freddie Chairman Leland Brendsel**  
**Fannie CFO Timothy Howard**

Components of the Voluntary Risk Management Agreement include:

- (1) Issue subordinated debt – after a three-year phase in - on a semi-annual basis equal to or in excess of 4% of on-balance-sheet assets. (On January 23, Fannie issued \$1.5 billion of subordinated debt with a maturity of 10 years. On March 21, Freddie issued \$2 billion of subordinated debt with a maturity of 10 years. Standard & Poor’s rated both “AA-minus”.)
- (2) Maintain more than three months’ worth of liquidity assuming the GSEs have no access to public debt markets. (On March 8, Freddie announced that it had met the liquidity commitment. On March 12, Fannie announced that it had met the liquidity commitment.)
- (3) Implement an interim risk-based capital stress test until permanent risk-based capital regulations are finalized by OFHEO. (On March 26, Fannie and Freddie announced that they had passed their respective interim stress tests as of December 31, 2000.)
- (4) Disclose interest-rate risk sensitivity analyses and results on a monthly basis. (On March 26, Fannie disclosed that as of February 28, 2001, the company’s net interest income at risk from a 50 basis point change in interest rates was 3% over the next one year, and 2.1% over the next four years. The company’s net interest income at risk from a 25 basis point change in the slope of the yield curve was 3.2% over the next one year, and 5.2% over the next four years. Freddie will begin the monthly disclosure of interest-rate risk in mid-April, as part of its regular public disclosures.)
- (5) Disclose credit-risk sensitivity analyses and results on a quarterly basis. (On March 26, Freddie disclosed the impact on Freddie of a 5 percent decline in house prices everywhere around the country. On March 26, Fannie announced that as of December 31, 2000, the company’s net sensitivity of future credit losses, taking into account the effect of credit enhancements, was \$295 million. The figure reflects a gross credit loss sensitivity of \$1,065 million without the effect of credit enhancements, and was net of projected credit risk sharing proceeds of \$770 million.)
- (6) Obtain an annual “risk to the government” rating of the independent financial strength of each of the companies from a rating organization and disclose the rating to the public. (On February 27, Fannie and Freddie announced that the companies had fulfilled this commitment with the release of Fannie and Freddie’s “AA-“ risk-to-the-government ratings from Standard & Poor’s.)

**Freddie Chairman Leland Brendsel**

- The voluntary risk management agreement places Freddie at the “vanguard of world financial practices” and at the “cutting edge of financial products and disclosure.”
- Freddie has met five of the six components of the voluntary risk management agreement and expects to implement the final commitment – its commitment to disclose its interest-rate risk sensitivity analyses - in April.

- With the implementation of these commitments, Freddie and Fannie will supply more information to the market than any other financial institution. Former FDIC Chairman William Seidman said the commitment “puts [Freddie Mac] in a position of providing more and better public information than any other financial institution, both regulated and non-regulated.”
- The voluntary risk management agreement should put to rest any future concerns about Fannie and Freddie’s safety and soundness.

### **Fannie CFO Timothy Howard**

- Fannie does not believe that the national housing market is “saturated.” There is a housing gap between whites and minorities that is “frankly alarming.” Fannie is prepared to help close that gap.
- Fannie has met all six of the components of the voluntary risk management agreement.
- The voluntary agreement, “combined with the regulatory mechanisms Congress enacted in 1992, place Fannie Mae at the vanguard of risk management and disclosure practices worldwide.”
- Fannie now discloses more information and more timely information to the public, investors, and policymakers than any other financial institution in the world. No financial institution in the world provides policymakers and investors more information about its financial status than Fannie Mae does.
- Fannie’s safety and soundness regime “goes well beyond any government-chartered bank or financial institution today”
- The voluntary risk management agreement “is nothing less than a new model for financial institutions in America and around the world.”

## **Questions & Answers**

### **Charter expansion**

- Brendsel noted that the company had only tried to change its charter once a few years ago, referring to Freddie’s failed amendment to self-insure mortgage loans. Although the amendment failed, he still thinks “it’s a good idea.”
- Howard noted that the company has made no requests to expand its charter. Howard thinks the company has been operating within its charter and has not seen any credible evidence to suggest otherwise.

### **Level playing field**

- **Cong. Shays noted that there is currently not a level playing field between the GSEs and other financial institutions. “I’m absolutely convinced the playing field isn’t level,” he said. He noted that the GSEs have been given opportunities and special privileges that no other financial institutions have been given, so Congress has a responsibility for oversight. Shays asked, “What obligation do I have to make sure you don’t use your advantages to drive everyone out of business.”** Brendsel noted that the GSEs’ charters do provide certain tools as a result of its charter but that the company has certain things that they are prohibited from engaging in, such as originating mortgages and credit cards, and that the company is limited to purchasing residential loans below a certain dollar amount.
- **Cong. Shays said he had “a lot of constituents who work with you...and a lot who compete with you,” and promised: “We’ll be watching you.”**

### **Implied guarantee**

- In his questioning, Cong. Baker clarified S&P's "AA-minus" risk-to-the-government rating of Fannie and Freddie. Cong. Baker noted that S&P's rating was not a true stand-alone risk-to-the-government rating of Fannie and Freddie as private businesses. S&P rated Fannie and Freddie as "GSEs", assuming no government cash infusion. The rating still assumes, however, that the GSEs have access to the market and assumes that the business operations of the companies as GSEs will continue.

### **Subordinated debt**

- Cong. Baker was concerned about recent reports that the spreads on the GSEs' subordinated debt are widening and whether this raised any liquidity concerns. He was also concerned about the consolidation of counterparties and the GSEs' ability to hedge risk.
- Howard noted that the GSEs' recent subdebt yield fluctuations were well within what other subdebt issuers have experienced. Brendsel called the fluctuations "random" fluctuations that change on a day-to-day basis.
- Cong. Bachus noted that the GSEs' subordinated debt does not convert to equity but rather interest payments are deferred.

### **GSEs' debt to surpass Treasury debt**

- Brendsel could not say whether the projections that Fannie and Freddie's debt would surpass Treasury debt by 2005 were accurate, but he thought that was like comparing apples to oranges. He noted that Freddie's increasing debt issuance was "good news" because this meant that the mortgage market was growing. He claimed that their debt issuance was in line with the growth in the US mortgage market. Howard noted that when Treasury pays down its debt, his teenager daughter would have more debt than Treasury.

### **Does GSE regulator need more authority?**

- Cong. Kanjorski noted that a recent GAO Report found that OFHEO lacks sufficient resources to regulate the GSEs but that the agency appears to have the ability under its statute.
- Brendsel noted that in his interpretation of the GAO Report, OFHEO had adequate regulatory authority, albeit somewhat different than other financial regulators. This does not surprise him since the GSEs are very different than other financial institutions.
- Howard said the GAO Report concludes that OFHEO has the tools to address significant safety and soundness concerns.
- When asked if Congress should give greater power to the GSEs' regulators. Brendsel said, "We support a strong, credible and effective regulator." Ultimately, though the decision would be up to Congress. He said based on his reading of the GAO Report, he would not recommend any changes to Members of Congress. Howard said his views were quite similar and that a strong regulator "is very much in our interest."

### **Should GSEs' capital be increased?**

- When asked if the GSEs' capital should be increased, Howard said that capital should be appropriate for risk. Since Fannie is only dealing with one asset – mortgages – it takes less risk than other institutions that are engaged in more diverse assets. Just because Fannie may have a lower nominal capital amount than other institutions, Fannie's capital class can actually be considered much stronger because the company takes less risk and its hedges are stronger than institutions with more risk. Brendsel had nothing to add and stated only that Freddie was extremely strong and well capitalized.

### **Predatory lending/Subprime market**

- Predatory lending was brought up frequently throughout the hearing, with many Congressional Members applauding Fannie's and Freddie's efforts to address predatory lending and encouraging Fannie's and Freddie's entrance into the subprime market. Fannie and Freddie were both questioned about their companies' commitments to address predatory lending. Both Brendsel and Howard noted that their companies had adopted voluntary predatory lending guidelines for loans that they will purchase and are encouraging their lender partners to adhere to these guidelines. Brendsel was asked how it could protect against predatory lending when it is currently purchasing billions of dollars of subprime loans. Brendsel stated that Freddie "only deals with good guys."
- Cong. Meeks questioned whether charges that the GSEs engage in "mission creep" led Freddie into the subprime market. Brendsel stated that if "mission creep" means trying to clean up the predatory lending market, than "we plead guilty." Freddie's entrance into the subprime market is fully within its charter. He noted that subprime lenders are complaining that the GSEs' entry into the subprime market is driving down their profits, which he refers to as excessive fees and returns. He argued that the dispute between subprime lenders and the GSEs is simply over competition. Howard noted that entering into the subprime market was not mission creep and that the company plans to move further into this area. "Making loans to people with less-than-perfect credit is not only totally within our charter, it is something we should do and something that is right to do," said Howard.
- Cong. Tubbs Jones applauded Fannie and Freddie for entering the subprime market.
- Cong. Shays asked what the lowest possible credit score for a borrower that Fannie and Freddie would accept. Both Brendsel and Howard said they had no cut-off credit score for acceptance.

### **Allegations that GSEs threatened members of FM Watch**

- Cong. Baker said he hopes that "both sides of these disputes will promptly cool their rhetoric." He states, "While these charges may deserve consideration by the subcommittee they are not the subjects of today's proceedings. I do not think the subcommittee should jump recklessly into these disputes."
- Cong. Shays asked Brendsel and Howard about allegations of threats by the GSEs. Howard said the allegations were "completely baseless." Howard said the only specific charge that was mentioned in the articles was Wells Fargo's allegation that Fannie had removed Wells Fargo from the list of approved bidders for Fannie Mae bonds. Howard said this was untrue. Cong. Shays questioned whether Brendsel could know whether other employees of his company might have issued threats. Brendsel said the allegations of threats were untrue and confirmed that no one in his company had engaged in threats. If it were brought to his attention that an employee had engaged in threats, he would review the matter and potentially fire them.

Sources: (*Written and Oral Testimony of House Financial Services Committee's hearing on Fannie and Freddie's compliance with voluntary risk management agreement, 3/27/01; American Banker, Michele Heller and Rob Garver, 3/28/01; American Banker, Michele Heller, 3/29/01; Bloomberg News, 3/27/01; BNA Daily Report for Executives, Adam Wasch, 3/28/01; Congressional Quarterly, Peter Cohn, 3/28/01; Dow Jones Newswire, 3/27/01, Jennifer Corbett Dooren; National Mortgage News Daily, 3/28/01; Reuters, Joanne Morrison, 3/27/01; Washington Post, Sandra Fleishman, 3/28/01*)

**Senate Banking Committee encourages Senate Budget Committee to change the budget process to account for the GSEs' subsidies and unfunded liabilities from the GSEs' implied federal guarantee**

**Senate Banking Committee calls the GSEs' federal subsidies significant contingent liabilities for US taxpayers**

**Senate Banking Committee recommends that Fannie & Freddie's safety and soundness regulator - OFHEO - be given full funding to carry out its oversight**

- The Senate Banking Committee released its views and estimates on the FY 2002 budget in its "FY 2002 Budget Views and Estimates" document to the Senate Budget Committee. In a March 16 letter to the Senate Budget Committee, the Senate Banking Committee recommended that OFHEO be given full funding to carry out its oversight of Fannie and Freddie. **"Given the relatively small size of OFHEO's budget and the huge assets of the regulated entities, failure to fund OFHEO adequately would certainly be penny-wise and pound-foolish,"** said the letter.
- **The Senate Banking Committee also recommends that the budget process be reformed to account for the GSEs' subsidies and contingent liabilities from the GSEs' implied federal guarantee. The Senate Banking Committee says it is concerned about the budgetary treatment of the GSEs and notes there has been a "growing and disturbing trend" of the GSEs' expansion, "particularly into areas well served by the private sector." The Committee notes that the "GSE concept allows Federal subsidies to be given without budget scoring, carrying with those guarantees significant contingent liabilities for the US taxpayers. While the obligations of GSEs may formally lack the backing of the Federal government, the markets assume that no GSE would be allowed to fail and applies a discount to the debt of these entities."**
- The letter states, **"Given the unlikelihood that the government would acquiesce in the failure of a GSE...The Budget Committee should give consideration to reforming the budget process to account for the subsidy element and unfunded liabilities of GSE operations and obligations."** The letter adds, **"This is no small matter"** as Fannie and Freddie have financial assets of well over \$2 trillion and borrowing by the FHLBanks has exceeded borrowing by the US Treasury. (*Senate Banking Committee's "FY 2002 Budget Views and Estimates,"* 3/16/01)

**Freddie's loan to LendingTree comes under fire**

**OFHEO is reviewing Freddie's loan to LendingTree**

**FM Watch charges that the loan is a clear example of "mission creep" and that Freddie is acting like a commercial bank**

**Freddie says the loan is not outside its mission and that LendingTree will use the money to develop its joint technology initiative with Freddie**

**LendingTree, however, initially said the loan would be used for the company's normal operating expenses, including advertising and salaries (the companies' two biggest expenses) – LendingTree claimed the loan was entirely separate from its technology partnership initiative with Freddie**

**LendingTree later clarifies that the proceeds of the loan will be used to develop its joint technology initiative with Freddie**

**FM Watch says the LendingTree loan supports its new report on the GSEs' mission creep (see [p. 27](#) for more information on the FM Watch report)**

- OFHEO has initiated a review of Freddie's loan to LendingTree Inc., an online loan broker of mortgages and consumer loans. LendingTree announced that Freddie provided a \$2.5 million line of credit to Lending Tree as part of a \$45 million financing package assembled to help fund the company. "We are aware of the transaction," said OFHEO spokeswoman Stefanie Mullin. "And before we come to any conclusions, we are gathering all the facts." (*National Mortgage News Daily*, 3/21/01; *American Banker*, Robert Julavits, 3/22/01)

**FM Watch claims Freddie's investment violates its charter**

- **It has become commonplace for Freddie Mac and Fannie Mae to make equity investments in technology companies. However, making a loan to a company has drawn the attention of the government-sponsored enterprises' critics. "The Freddie Mac loan to LendingTree is the first time a GSE has directly engaged in commercial banking, and one of the clearest examples of 'mission creep' that we have seen to date," said FM Watch Executive Director Mike House. FM Watch believes the loan to LendingTree violates Freddie's charter and that by extending a line of credit to LendingTree, Freddie is acting like a commercial bank. FM Watch claims this is the first time a GSE has performed a corporate finance service. "If there is a clearer example of non-charter activities than this, I haven't seen it," said House.**
- **FM Watch says Freddie's investment is also controversial because LendingTree helps consumers get auto and other consumer loans, not just mortgages. According to *Mortgage Banking*, "LendingTree perceives itself as a cyberspace financial bazaar, where potential borrowers may shop for a variety of loans – mortgage, auto, small business, personal, credit cards." LendingTree also claims it is a marketplace – not a lender.**
- **FM Watch says the LendingTree credit line supports its new report on the GSEs' mission creep claiming that Fannie and Freddie have undertaken "a conscious and concerted effort" to expand beyond their charters. The report, entitled "*GSE Mission Creep: The Threat to American***

*Consumers,*” cites what the group calls examples of Fannie and Freddie’s mission creep and expansion into the primary market. **Referring to Freddie’s investment in LendingTree, FM Watch’s House stated that “Before the ink had dried on the FM Watch GSE Mission Creep report...Freddie Mac presented us with a new and particularly egregious example of how the GSEs use their government advantages to go beyond their congressional charters and compete with private companies.”** (See [\(p. 27\)](#) for more information on the FM Watch mission creep report.) (*American Banker*, Michele Heller, 3/21/01; *National Mortgage News Daily*, 3/21/01; *Wall Street Journal*, 3/22/01; *Mortgage Banking*, Louise Schiavone, 12/00)

- **FM Watch said they would also like Fannie and Freddie’s mission regulator, HUD, to examine Freddie’s loan to LendingTree.** A spokesman for HUD had no information about the possibility of review by that agency. (*Charlotte Observer*, Rick Rothacker, 3/23/01)

#### Freddie denies that the investment is outside its mission

- Freddie’s Spokeswoman Sharon McHale said the company briefed OFHEO officials about the loan prior to the transaction but the agency didn’t raise any concerns. McHale noted that the company has provided OFHEO with additional information since then. “It’s completely in keeping with our statutory purpose, so we see no reason why they would take issue with it.” (*National Mortgage News*, Brian Collins, 3/26/01)
- A Spokeswoman for Freddie said the claim that the line of credit “is beyond our mission doesn’t hold water.” Investing in LendingTree “supports our mission of lowering costs and making the mortgage process more affordable to borrowers,” she said. “It also makes the process simpler for lenders.” (*American Banker*, Michele Heller, 3/21/01) “We don’t think FM Watch is a credible critic of what’s consistent with our charter and mission,” said Freddie’s Spokesman Douglas Robinson. He claimed Freddie was helping one of its lenders provide the technology it needs to perform its business. (*Dow Jones Newswire*, Jennifer Corbett Dooren, 3/20/01) LendingTree and Freddie said they were confident no problems would be found with their agreement. According to Freddie’s Spokeswoman Sharon McHale, the money will be used to develop joint technology that will help make the mortgage market more efficient for homeowners and lenders. (*Charlotte Observer*, Rick Rothacker, 3/23/01)

#### LendingTree initially provided a different perspective than Freddie on how the proceeds from Freddie’s loan will be spent

- **The intent of Freddie’s funding to LendingTree is “unclear,” reports Michael Murray with *Real Estate Finance Today*, “as both sides of the deal have offered different perspectives on how the funds will be used.”** Freddie wants the money to be used to complete the integration of LendingTree’s Lend-X technology with Freddie’s automated underwriting system, Loan Prospector. LendingTree, however, has other ideas for the cash. According to LendingTree’s Chief Financial Officer and Senior Vice President Keith Hall, the line of credit will be used for normal operating expenses, including advertising and salaries, the company’s two largest expenses. “[The line of credit] enables us to draw up to \$2.5 million at our choice, whenever we need money to draw on,” said Hall. He noted that funds were entirely separate from the Lend-X and Loan Prospector initiative. “There are no strings attached that we have to use that money to do that,” said Hall. Freddie’s Spokeswoman Sharon McHale, however, stated in the same article that “We don’t look at this as an investment, but rather, as a way of forwarding our technology initiatives. “The whole purpose of the financing was to enhance the technology partnership,” said McHale. (*Real Estate Finance Today*, Michael Murray, 3/19/01)

LendingTree later clarifies that the proceeds of the loan will be used to develop its joint technology initiative with Freddie

- Douglas Lebda, Founder and CEO of LendingTree wrote a letter to *Real Estate Finance Today* on behalf of LendingTree to “clarify some misimpressions” about its recent transaction with Freddie. Lebda clarifies that “First...Freddie Mac has been working with us for some time to integrate Lend-X...with the secondary market tools Freddie Mac provides to lenders. Due to our existing business relationship with Freddie Mac, we asked them to participate in a recent financing of \$45 million. Freddie Mac agreed to provide us debt financing in an amount of \$2.5 million. Second, LendingTree is not a mortgage lender and does not underwrite any of the loan products offered on our site. Freddie Mac’s financing documents contain explicit terms that prohibit us from using their money for activities in which they cannot engage, including warehouse lending or any other consumer loan funding purpose. We will use their funds to advance our Lend-X technology...Finally, we want to emphasize that this financing was provided in the context of our ongoing business relationship with Freddie Mac...This relationship simply cannot be characterized as an entry by Freddie Mac into the commercial banking or mortgage origination business and we certainly do not view them as a commercial lender.” (*Real Estate Finance Today*, LendingTree’s Douglas Lebda Letter-to-the-Editor, 4/2/01)

Background on LendingTree and its existing technology partnership with Freddie

- **According to *Mortgage Banking*, “LendingTree perceives itself as a cyberspace financial bazaar, where potential borrowers may shop for a variety of loans – mortgage, auto, small business, personal, credit cards.” LendingTree is the staging area where customers submit personal data and financial institutions linked to the site have the opportunity to bid on those customers. LendingTree also claims it is a marketplace – not a lender. “LendingTree is just a matchmaker, not a lender. They don’t need as much capital as a mortgage business,” said Forrester Research analyst Jamie Punishill.**
- LendingTree also sells its lending technology to other corporate clients. Its Lend-X technology is an online technology origination platform enabling companies to install a customized co-branded or privately labeled loan marketplace into their site. In the third quarter of 2000, Lend-X revenues were \$1.6 million, up 28 percent from the previous quarter. LendingTree’s Founder and CEO Douglas Lebda says LendingTree charges as much as \$50,000 to set up Lend-X and potentially as much as \$1 million for up-front licensing fees and customization. Thereafter, LendingTree would collect between \$5 and \$15 for every loan application taken on a Lend-X client’s Web site. LendingTree’s Chief Technology Officer Rick Stiegler said Lend-X is essentially a cyberspace private portal or application service provider (ASP).
- In July, LendingTree announced a multi-year partnership with Freddie to integrate LendingTree’s Lend-X technology and Freddie’s automated underwriting system, Loan Prospector. The two companies announced that they would be integrating their technologies into a private-label lending platform that will be marketed to Freddie’s 3,000 lenders. So far, Lend-X has been private-labeled to more than 20 financial institutions including Wachovia, which went live in March 1999. Under the new system, Lend-X supplies the front-end and middleware components for the loan application and integration of all the parts, while Freddie supplies back-end technology for automated underwriting and pricing. “We’ve entered into an agreement with them to bring our tools as it relates to Loan Prospector, collateral, how we price loans, plus all the various ways that you might process a loan, having the capability of our tools tightly wed to those in Lend-X,” says Freddie’s VP for Business Development James Taylor. Freddie has also agreed to purchase the

loans originated under the platform. Financial details were not released, but under the agreement, LendingTree will initially receive several million dollars in fees for loans originated through the platform. “Our goal is to make Lend-X the operating system of online lending,” said Douglas Lebda, Founder and CEO of LendingTree. (*Mortgage Banking*, Louise Schiavone, 12/00; *LendingTree press release*, 7/10/00; *The Charlotte Observer*, 7/11/00; *National Mortgage News Daily*, 7/11/00; *American Banker*, Robert Julavits, 7/12/00; *Charlotte Observer*, 3/23/01)

- LendingTree is also very focused on attracting Realtors to its Web site. As part of its strategy to attract Realtors, LendingTree purchased HomeSpace.com, which gives LendingTree a ready-built network of Realtor customers, including the offices of Coldwell Banker and Prudential. LendingTree is also planning on adapting its Lend-X technology for the Realtor community. Eric Cunliffe, LendingTree’s Senior Vice President in charge of HomeSpace integration says the Lend-X Realtor system has been very successful. “What we give Realtors is what they call a ‘golden referral,’ a consumer who has gone through LendingTree filters with at least four lenders,” said Cunliffe. “Our relationship with Realtors revolves around the fact that we bring them a qualified customer ready, willing and able to purchase a home.” Those leads, some of which are pre-qualified, are then e-mailed to participating Realtors. Cunliffe notes that LendingTree offers an “incredibly valuable service to the consumer,” in contrast to the “blind and intuitive way” most consumers choose their real estate agent. (*Mortgage Technology*, Scott Kersnar, November/December 2000)

**Nation’s largest taxpayer group – National Taxpayers Union - calls for FEC investigation of Fannie & Freddie’s soft money contributions**

**NTU says hundreds of thousands of dollars of these contributions may be illegal**

**“It’s a scandal that these two government-subsidized and Congressionally-chartered enterprises are spending millions of dollars to become political players at taxpayer expense...But it is even more troubling if they are not playing by the rules of campaign finance, which would be the ultimate insult to all American taxpayers.”**

- The National Taxpayers Union (NTU) filed a complaint with the FEC based on hundreds of thousands of dollars in possible illegal political contributions by Fannie and Freddie to several national party committees. NTU based its complaint on a review of Reports and Disbursement filings from the national party committees.
- **“It a scandal that these two government-subsidized and Congressionally-chartered enterprises are spending millions of dollars to become political players at taxpayer expense,” said NTU President John Berthoud. “Taxpayers – whose dollars back these giants – have to question the appropriateness of these kinds of political expenditures.” He adds, “But it is even more troubling if they are not playing by the rules of campaign finance, which would be the ultimate insult to all American taxpayers.”**
- NTU sent a letter to the FEC asking for a full review of over \$400,000 in soft money contributions by Freddie and almost \$340,000 by Fannie. NTU also asked the FEC to examine the millions of dollars in “building fund” contributions made by Fannie and Freddie to “ensure that these political donations were not diverted to prohibited election-related nonfederal accounts.”

- NTU notes that in 1997-2000, Freddie contributed over \$2.84 million in soft money to national party committees and Fannie contributed over \$1.47 million. NTU claims that as Congressionally-chartered companies, Fannie and Freddie are strictly prohibited from making contributions to the election-related accounts of national party committees and are only allowed to contribute to the “construction or purchase” of a building by a political party. NTU notes that Fannie and Freddie contributed several hundred thousand dollars in gifts to accounts that were not for “construction or purchase” of buildings.
- NTU requested two specific FEC investigations:
  - (1) Review of the apparent contributions to political committee funds that were not for “construction or purchase” of a building by a political party.
  - (2) Examination of the building fund contributions (in excess of \$1 million by Fannie Mae and in excess of \$2.4 million by Freddie Mac) to ensure that the funds were not diverted to prohibited nonfederal accounts. NTU notes that the law specifically states that such contributions may be used only for “construction or purchase of any office facility” and not to fund the political campaigns of state and local officials or other election-related activities. (*NTU press release, 3/27/01*)
- The NTU asked for a quick review of the charges, but the FEC often takes years to resolve enforcement complaints. An FEC Spokesman said the commission routinely refuses to comment on pending enforcement matters. (*BNA Daily Report for Executives, Kenneth Doyle, 3/29/01*)

Fannie & Freddie’s response

- “We have not seen the complaint, but we are confident that our contributions followed the letter of the law,” said Fannie Spokesman Robert McCarson. “We follow the letter of the law with respect to our donations to political parties,” said a Freddie spokesman. (*American Banker, Rob Garver, 3/29/01; National Mortgage News Daily, 3/29/01*)

**Freddie eliminates appraisals on most loans with LTV ratios of up to 80%**

**The appraisals can be waived, provided a lender uses Freddie’s automated underwriting system and pays a \$50 or \$200 delivery fee to Freddie**

**Appraisal Institute calls Freddie’s program “irresponsible” and a “sleight of hand” – says it “adds significantly” to Freddie potential risk and is misleading since Freddie “seems to be telling people ‘you don’t really need an appraisal,’” while at the same time making heavy use of appraisal and public property data in its electronic valuation model**

**[Editorial Note: With just one press release, Freddie eliminates business that would otherwise go to appraisal companies. Instead, lenders are charged “delivery fees” that must be paid to Freddie.]**

- Freddie announced that it has added a new “no-appraisal” feature in its automated underwriting system – Loan Prospector. The feature becomes available April 8 for some low-risk loans sold to Freddie. The feature eliminates Freddie’s appraisal requirements for first-lien purchase money loans with total loan-to-value ratios of up to 80% and for borrowers with excellent credit histories. Freddie anticipates that approximately 40% of purchase money mortgages with downpayments of 20% or more will qualify for the “no-appraisal” option.

- For loans that qualify for the “no-appraisal” feature, lenders may either choose this option, pay a \$50 or \$200 delivery fee to Freddie, and receive waivers for the representations and warranties on property value, condition and marketability, or choose to order an appraisal and not pay a delivery fee. In place of the mandatory appraisal, Freddie will perform an electronic “collateral assessment” (Freddie’s automated valuation model) on the home to determine its approximate market value. This estimate will be computed by accessing online databases that Freddie uses for prices, appreciation rates, resale value changes and local market trends. Some of the data are publicly available while other information derives from actual appraisals. The \$50 fees will be charged when Freddie’s electronic systems indicate that the valuation data on a particular house is deep. The \$200 fees will be charged whenever there is at least some uncertainty about the degree of accuracy of the automated valuation. (*Freddie press release, 3/21/01; Washington Post, Kenneth Harney, 3/31/01*)

#### Appraisal Institute responds

- **A Spokesman for the Appraisal Institute called Freddie’s new program “irresponsible” and a “sleight of hand. The Appraisal Institute Vice President for Public Affairs Don Kelly says the new program “adds significantly” to Freddie’s potential risk. Kelly characterized the program as “misleading,” since Freddie “seems to be telling people, ‘you don’t really need an appraisal,’” while at the same time making heavy use of appraisal and public property data in its electronic valuation model. Kelly pointed out that as one option for lenders, many appraisers offer “streamlined” valuations for “half the usual cost.” Streamlined appraisals typically cost \$200 or less. (*Washington Post, Kenneth Harney, 3/31/01*)**

## ***All GSEs***

**Mortgage Bankers Association releases comprehensive housing agenda, which includes a number of proposals related to the GSEs**

**MBA supports creating a clear distinction between primary and secondary market activities, so Fannie & Freddie can focus on the missions prescribed in their charters - otherwise, consumers will be ultimate losers**

**MBA supports expansion of the FHLBanks' mortgage purchase plans (such as the MPF and MPP programs), which create competition for Fannie & Freddie in the secondary mortgage market**

**MBA opposes the privatization of Ginnie Mae and opposes using Ginnie Mae as a source of funds to satisfy other government purposes**

- The Mortgage Bankers of Association (MBA) released a “A Blueprint for Reform from the Real Estate Industry” which lays out a comprehensive housing agenda for the new Administration and Congress to increase affordable housing, expand homeownership, strengthen commercial investments in cities, and improve access to credit for all Americans. Among its agenda items, the MBA outlined a number of proposals to address their concerns with the GSEs.

### Fannie and Freddie

- In terms of Fannie and Freddie, the MBA supports the vital role of the GSEs in maintaining liquidity and stability in the secondary market. **However, the MBA believes “that it is essential that the GSEs focus on the missions prescribed in their charters and that the clear distinction between primary and secondary market activities be reaffirmed.”** The MBA notes that there is a “current ambiguity” around the GSEs’ secondary market functions and a “blurring” of the lines between the primary and secondary market. As an example, the MBA states “when the Enterprises attach conditions on the deployment of their technologies, build brand identification with consumers, and invest in primary market service providers, their activities have direct impact on primary market participants. Although the immediate casualties of Enterprise incursions into the primary market might be existing mortgage providers, MBA believes consumers will be the ultimate losers. Less competition means higher borrowing costs and fewer financing options over the long-term.” The MBA notes that it is currently working with Fannie and Freddie to develop a workable definition for the “appropriate domain of Fannie Mae and Freddie Mac.”
- The MBA supports HUD’s final affordable housing rules for Fannie and Freddie, but “had hoped HUD would have modified its proposed rule in a few key aspects.”
- MBA’s noted that its views on the affordable housing goals “are predicated on the following principles”:
  - “All sectors of the housing market — especially consumers — are served best by a competitive market for the origination of, and investment in, residential mortgages.
  - The GSEs should be encouraged to provide assistance to the secondary market for mortgages on housing for underserved persons and areas; however, they should not be

encouraged to compete in the primary market or to expand into markets currently well-served by others.

- The goals should be sensitive to market dynamics as they encourage the GSEs to ‘lead the industry.’
- The GSEs should assume some risk on their mortgage transactions and not transfer all risk to the primary mortgage market or other market participants.
- Consistent with their charters, GSEs should be encouraged to undertake ‘activities relating to mortgages on housing for low-and moderate-income families involving a reasonable economic return that may be less than the return earned on other activities.’”
- Consistent with its views on the affordable housing rules, the MBA encourages HUD to pursue its review of the GSEs’ credit enhanced transactions as proposed in the preamble to the final affordable housing rule. MBA says these additional evaluations should be conducted with the input of the mortgage finance industry and should consider whether value or liquidity are provided to the marketplace. HUD should amend the rule to reflect the results of these evaluations to assure that goals credit is provided to the GSEs “only when their activities enhance the market for goals-eligible loans.”
- In terms of safety and soundness and capital standards for Fannie and Freddie, the MBA made the following recommendations to OFHEO:
  - “OFHEO should proceed to publish a final capital rule as promptly as possible.
  - The final capital rule needs to incorporate a process for dealing with new initiatives and changed circumstances.
  - The process for determining required capital should give each GSE the ability to calculate to a reasonable degree of certainty the amount of capital required by the stress test at any given time.
  - Credit scores should be incorporated into the stress test model for single-family loans, either in the final rule, if OFHEO proposes to proceed directly to a final rule as MBA recommended, or in a subsequent rulemaking if incorporation of credit scores would delay publication of a final rule.
  - MBA urges simplification of the model and correction of distortions related to multifamily risk.
  - MBA urges OFHEO to treat Fannie Mae’s counterparty exposure to its DUS lenders as a separate category apart from generic counterparty risk.”
  - In addition, the MBA identified a number of other technical modeling concerns which were submitted to OFHEO and urged to be addressed in the final rule.

### FHLBanks

- MBA said it supports the expansion of the FHLBanks' mortgage purchase programs, such as the Mortgage Partnership Finance (MPF) and Mortgage Purchase Program (MPP), which provide "another avenue of liquidity for mortgage loans and more competition within the secondary market." However, MBA would like to see a restriction lifted to allow independent mortgage banks direct access to the FHLBank System for such programs as interim funding of mortgage originations and participation in the new mortgage purchase initiatives. The MBA notes that nearly all segments of the mortgage lending industry – except independent mortgage banks – are granted access to the FHLBanks.

### Ginnie Mae

- The MBA opposes the privatization of Ginnie Mae and opposes using the agency as a source of funds to satisfy other government purposes (examples include the selling of Ginnie Mae or an increase in the Ginnie Mae guaranty fee). The MBA supports rolling back the scheduled 2004 three basis point Ginnie Mae guaranty fee increase and eliminating the ceiling on Ginnie Mae issuance levels. (*"A Blueprint for Reform from the Real Estate Finance Industry,"* Mortgage Bankers Association, 2001)

## ***Fannie Mae and Freddie Mac***

***Banker & Tradesman* editorial says Congress should determine whether through direct or implied threats, Fannie & Freddie threatened to pull business from several major banks and financial services firms as punishment for criticizing the GSEs**

**Chief executives of Wells Fargo, American International Group (AIG), and GE Capital were all recently quoted in the *Wall Street Journal* as stating they have faced threats of retaliation from Fannie & Freddie for participating in the Fannie/Freddie watchdog group, FM Watch**

**If the allegations are substantiated, “Fannie Mae and Freddie Mac then deserve to be reeled in and placed under regulatory oversight that keeps them within the boundaries of their charters.”**

**Fannie & Freddie claim the allegations are untrue, yet the editorial asks, “What would senior executives of leading financial service corporations have to gain by falsely attributing threats of intimidation and retaliation to Fannie Mae and Freddie Mac, two companies with whom they have long-standing business dealings?”**

**Freddie Chairman Leland Brendsel writes Letter to the Editor denying that Freddie Mac threatened companies**

- **A *Banker & Tradesman* editorial says Congress should determine whether through direct or implied threats, Fannie & Freddie threatened to pull business from several major banks and financial services firms as punishment for criticizing the GSEs. The editorial was referencing recent reports in the *Wall Street Journal* about allegations that Fannie and Freddie threatened to pull business from several major banks and financial services firms as punishment for criticizing the GSEs. The *Wall Street Journal* recently reported that chief executives of Wells Fargo, American International Group (AIG), and GE Capital were all quoted as stating they have faced threats of retaliation from Fannie & Freddie for participating in the Fannie/Freddie watchdog group, FM Watch [See March 16, 2001 GSE Report for more information.]**
- **The editorial notes that Fannie’s response has been to call the allegations “rather bizarre and belied by the facts,” while Freddie’s response says this shows “the air coming out of the tires [at FM Watch].**
- **However, the editorial asks, “What would senior executives of leading financial service corporations have to gain by falsely attributing threats of intimidation and retaliation to Fannie and Freddie, two companies with whom they have long-standing business dealings?” The editorial adds, “An examination of possible motives leaves one scratching their head in bewilderment as many of these companies are significant originators of mortgages and rely upon the GSE twin giants for access to the secondary market. Unfavorable terms in a commitment to buy loans can quickly decimate an originator’s business by pricing them out of the highly competitive home mortgage market.” And, “On the back side, Fannie Mae and Freddie Mac pay out millions of dollars in underwriting fees to Wall Street firms, including some on the list of accusers.” The editorial concludes, “Advantages belongs to the GSEs all the way.”**
- **The editorial notes that “there is a need for Congress to step in and attempt to determine the validity of the claims made against Fannie Mae and Freddie Mac...If the allegations of abusing their position through direct or implied threats of retaliation against business**

**partners are substantiated, Fannie Mae and Freddie Mac then deserve to be reeled in and placed under regulatory oversight that keeps them within the boundaries of their charter.”**  
(*Banker & Tradesman* editorial, FM Static, 3/19/01)

Freddie Chairman Leland Brendsel writes Letter to the Editor denying that Freddie Mac threatened companies

- In a Letter-to-the-Editor in the *American Banker*, Freddie Chairman Leland Brendsel denied allegations of “bullying” companies for belonging to FM Watch. “Let me state unequivocally: Freddie Mac has not, does not, and will not do business this way.” He adds, “The institutions we supposedly threatened are our customers and business partners...Why the smear campaign? Because the institutions behind FM Watch cannot win the facts. Their campaign seeks to prevent Freddie Mac from fulfilling our congressional mandate to promote low-cost mortgage credit for America’s families.” Brendsel claims the members of FM Watch are objecting because Freddie is lowering costs to consumers. He refers to members of FM Watch (his “customers and business partners”) as the following: (1) “subprime lenders that are trying to preserve extremely costly and in many cases unfair way of doing business”; (2) “mortgage insurance companies that have an interest in perpetuating their inefficient, expensive products”; and (3) “megabanks that seemingly view Freddie Mac as an obstacle to their domination of the market for consumer financial services.” Brendsel said Freddie supports a level playing field for all lenders. (Letter to the Editor, Freddie Mac Chairman Leland Brendsel, *American Banker*, 3/27/01)
- **In response to Freddie’s Letter-to-the-Editor, FM Watch Executive Director Mike House said: “This is a typical GSE spin. Anytime anybody questions their business practices or their motives, or tries to have any type of legitimate debate about their proper role, they immediately go on the attack.”** (*American Banker*, Robert Julavits and Erick Bergquist, 3/27/01)

**FM Watch releases new report outlining how Fannie & Freddie’s mission creep threatens American consumers**

**FM Watch claims that “GSE mission creep, the risk it poses to taxpayers, and the benefits to GSE shareholders, are all at the expense of the nation’s homebuyers.”**

- FM Watch released a comprehensive report, “*GSE Mission Creep: The Threat to American Consumers*,” which cites several examples of Fannie and Freddie’s mission creep and expansion into the primary markets. “FM Watch decided to undertake this study, because despite their current market dominance and huge size, Fannie Mae and Freddie Mac have indicated they intend to grow at speeds private financial firms cannot even hope to approach,” said FM Watch Executive Director Mike House. “To sustain these earnings, the GSEs will have no choice but to arbitrage their capital and borrowing advantages. They must also enter new lines of business and exercise even more control in the ones in which they now engage.”
- **According to FM Watch, “GSE mission creep, the risk it poses to taxpayers, and the benefits to GSE shareholders, are all at the expense of the nation’s homebuyers.”** FM Watch adds, “Virtually all the GSEs’ ventures beyond the mission for which they were chartered are touted as being good for consumers. Even when a venture has nothing to do with homeownership, the companies defend themselves by citing the ‘American Dream of Homeownership’ and linking themselves firmly to it. However, any consumer benefits of these GSE ventures are transitory. From time to time, consumers may pay a lower price for a product or service because the GSEs have entered into a new market, but the monopoly power that these government-sponsored

enterprises wield ensures that consumers will ultimately pay more for a reduced variety of mortgages and consumer finance options once the private sector is unable to compete."

- FM Watch notes that the report focuses on the negative effects GSE mission creep has had on consumers and homebuyers. It cites specific examples of the GSEs' mission creep.
- Chapter 3 of the report, "Evidence of Mission Creep," shows explicitly how the GSEs are "expanding within and moving beyond their charters at an alarming pace." FM Watch cites the followings as examples of the GSEs' recent ventures into the primary mortgage market and their direct consumer outreach:
  - Homestore.com, a joint venture with realtors in which Fannie Mae presents consumers with the "Fannie Mae mortgage."
  - HomeAdvisor.com in which Freddie Mac, Microsoft, and certain lenders are offering a seamless channel from the point of sale of a home through to the secondary market investor;
  - 1-800-FANNIE MAE, a telephone call center in which Fannie Mae directly counsels consumers on their mortgage options.
- Other mission creep examples cited by FM Watch include: the GSEs' purchase of home equity loans, even though only about 30% are for home improvements, with the majority going for debt consolidation; non-mortgage ventures like Freddie Mac's idea of participating in "universal accounts," which aggregate all of a consumer's assets and liabilities into a single account; and last but not least, expanding into mortgage insurance with the promotion of the GSEs' "delivery fee" programs that actually increase both the cost to consumers and the GSE risk.
- Chapter 4 explains the GSEs' attempts to control the technology platform by forcing companies to use their automated underwriting system. "By seeking to force all of the loans they purchase to be underwritten through their proprietary AU systems, the GSEs are diminishing the role of existing alternative private AU systems, blocking the development of new ones and establishing exclusive criteria for lenders that may well fail to meet local borrower needs, accurately reflect the true creditworthiness of nontraditional borrowers (e.g. minorities) or provide the best price for all consumers in the long run."
- Chapter 5 explains how the GSEs use their special relationship to the Federal government to pick winners and losers in the marketplace: for example, when Fannie Mae invested in a community bank whose mission was to compete with other local financial institutions.
- Chapters 6 and 7 explain how the GSEs' ventures into new lines of business are risky for the American taxpayers and how their portfolio investments are mainly for the benefit of GSE shareholders. "As the Congressional Research Service has concluded, 'The repurchase of their own MBS (Mortgage Backed Securities) by the GSEs can be thought of as a case of repatriating interest rate risk. When mortgages are securitized and sold, the GSE retains the credit risk on the loans, but sells to investors the interest rate risk. MBS are less profitable than portfolio holdings as a result... While it is clear that this increases shareholder value, it is difficult to understand what, if anything, it does for the mortgage market.'" FM Watch's press release and report can be downloaded at FM Watch's Web site: <http://www.fmwatch.org>.

### Fannie & Freddie respond to report

- Freddie Spokeswoman Sharon McHale said, “The products and technologies we have rolled out (that they take issue with) lower costs for homebuyers or streamline the process. And that is something that can be documented.” Fannie Spokeswoman Janice Daue said the FM Watch report is riddled with errors. “There is more competition in the market because we are in the marketplace.” (*National Mortgage News*, Brian Collins, 3/26/01)

<b>Financial services consultant Bert Ely predicts Fannie &amp; Freddie will seek privatization in the next two to four years</b>
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- Financial services consultant Bert Ely predicts that over the next two to four years, Fannie and Freddie “will take the initiative to privatize.” Speaking on a GSE panel at the National Association of Business Economists conference, Ely said “it only a matter of time” before Fannie and Freddie seek privatization. Ely explained that there is a “GSE life cycle” and that, “I suggest the time has come for Fannie and Freddie to leave the cocoon.” Ely said Fannie and Freddie will likely follow the lead of Sallie Mae, a former GSE that went private in 1996. Ely is also releasing a research paper shortly that elaborates on his privatization predictions. In his paper, which was circulated at the conference, Ely predicts Fannie and Freddie will choose to give up their federal government charters, their lines of credit with the Treasury, their tax exemptions and in return, would no longer be subject to Congressional oversight. He believes the companies will seek privatization because the current government charters restrict them from purchasing certain types of loans, which will soon hurt their ability to increase profits. **“Privatizing Fannie and Freddie is fast approaching as they exhaust their opportunities to continue growing their earnings 15% annually within the present confines of their congressional charters,”** wrote Ely in his paper. **“If they [Fannie and Freddie] are unsuccessful in expanding their charters, then they will have no choice but to quickly seek privatization in order to maintain their earnings growth, and their share prices,”** Ely wrote. “Privatization will move much faster if Fannie and Freddie initiate it rather than having it forced upon them. Therefore, the next Congress (the 108<sup>th</sup>) could be addressing Fannie’s and Freddie’s privatization.”
- Ely also questioned the efficiency of the GSEs. If the federal government wants to subsidize the housing market, then it should consider the most effective way of benefiting homebuyers, said Ely. “Do we really need Fannie and Freddie involved?” Ely quoted the 1996 CBO study, which estimated that Fannie and Freddie receive an annual \$6.5 billion in subsidies from the federal government. He also questioned whether homebuyers who can afford homes costing up to the \$275,000 loan limit purchased by Fannie and Freddie deserve a housing subsidy. Instead of giving Fannie and Freddie the preferred GSE status, Ely argued that the best way to benefit homebuyers would be for the federal government to offer a tax credit that is targeted to those “on the cusp” of homeownership. In effect, the tax credit would serve as an interest buy-down modeled on the Earned Income Tax Credit.
- Speaking on the same GSE panel, Fannie’s Chief Economist David Berson was skeptical of Ely’s privatization prediction and called the CBO study “flawed.” Berson said Fannie wasn’t similar to Sallie Mae. “Sallie Mae was a GSE that didn’t really have a public mission – that’s the reason it was privatized.” He also argued that Ely’s tax credit scheme would result in higher borrowing costs and limit borrower choice among lenders. (*Dow Jones Newswire*, Joseph Rebello, 3/26/01; *National Mortgage News Daily*, 3/26/01; *BNA Daily Report for Executives*, Adam Wasch, 3/27/01)

- Fannie Spokesman Robert McCarron called Ely’s prediction “total and utter nonsense.” He stated, “Fannie Mae and Freddie Mac are spectacular public-policy success stories, and we are widely recognized for lowering the cost of and knocking down barriers to homeownership. We have no intention of doing anything to change that.” A Spokesman for Freddie also said the company had no plans to privatize. (*Dow Jones Newswire*, Joseph Rebello, 3/26/01)

**Fannie & Freddie tell Mortgage Bankers Association that they will not expand into the primary market by vowing that they will not originate loans**

**However, as FM Watch Chairman Gerald Friedman states, “the real threat” to lenders of every size isn’t the possibility that the GSEs will become mortgage originators, but their ability to control information. “They don’t want to originate,” he said. “They want to control the gateways and establish the connections...If they control the channel, no one --- no matter how large -- will be able to compete with them.”**

**MBA and GSEs deny that their relationship is adversarial**

**MBA president notes, however, that there is a blurring of the roles of the GSEs and that there needs to be some clearly defined guidelines for the GSEs**

- Speaking to attendees at the MBA’s annual regional conference, executives from Fannie, Freddie, and the MBA denied that their relationship is adversarial. MBA President Andrew Woodward said it was “far from the truth” that the relationship between the MBA and the GSEs was adversarial, although there are disagreements at times. “We have blunt exchanges, frank exchanges with our partners,” he said. He stated, “Some have decided that MBA and the GSEs are adversaries...It’s just not true. Of course, there are things we disagree on and debate.” Woodward noted that there is a blurring of the roles of the GSEs and that there needs to be some clearly defined guidelines for them.
- Executives from Fannie and Freddie agreed with Mr. Woodward that their relationship is not adversarial, but reiterated that the GSEs do not want to originate loans. “Our partnership is founded on the principle that Freddie Mac’s role is to help lenders fulfill their mission, not for us to originate your loans. There is a bright line and that bright line is we won’t, we can’t, we won’t originate loans,” said Freddie’s Chairman and CEO Leland Brendsel. Fannie’s COO Daniel Mudd said, “our role is firmly, finally, and fully in the secondary market. One of the things we don’t do and we never will do is to originate loans.” (*National Mortgage News Daily*, 3/21/01; *Reuters*, Aleksandrs Rozens, 3/21/01; *Real Estate Finance Today*, Chris De Reza, 3/26/01)

GSEs’ statements that they will not “originate” loans does not prevent their expansion into the primary market, nor deny their ability to control the origination process

- FM Watch Chairman Gerald Friedman told participants at an annual Midwinter Conference in Park City, UT in 2000 that **“the real threat” to lenders of every size isn’t the possibility that the GSEs will become mortgage originators, but their ability to control information. “They don’t want to originate,” he said. “They want to control the gateways and establish the connections...If they control the channel, no one --- no matter how large -- will be able to compete with them.”** (*National Mortgage News Daily*, 2/07/00)
- **AEI Resident Fellow Peter Wallison and financial consultant Bert Ely note that perhaps the “greatest competitive threat” from the GSEs’ growth is in the mortgage origination business.**

“Although Fannie and Freddie vigorously deny that they have any intention to originate mortgages, pointing out that they lack the statutory authority to do so, what exactly constitutes origination of a mortgage is a matter of interpretation. If Fannie and Freddie were to open their automated underwriting facilities to direct borrower access over the Internet, it might be possible for them to provide the prospective homebuyer with a certification that his or her mortgage would qualify for purchase by Fannie or Freddie. At that point, the actual lender would have little to do except to perform the ministerial acts necessary to fund the loan and deliver it to one or another of the GSEs.” (*“Nationalizing Mortgage Risk: The Growth of Fannie Mae and Freddie Mac,”* Peter Wallison and Bert Ely, 2000)

- **During an American Enterprise Institute (AEI) Seminar on March 24, 1999 on Fannie and Freddie, Vern McKinley, a then-policy contributor to CATO, noted that Fannie and Freddie’s technology, including Fannie and Freddie’s automated underwriting systems and their direct marketing to consumers, raised questions about whether Fannie and Freddie are violating their charters by originating mortgages. It all depends on your definition of “originate.”** McKinley stated that, “originate could be narrowly defined to simply include the funding of a loan. It could also be defined much more broadly to also include steps involved in the underwriting process.” McKinley noted that the provisions in the charters prevent Fannie and Freddie from originating loans, however the provisions were added to the GSEs’ charters in 1989, and “there is very little evidence of what the Congress intended by imposing this limitation.” (*“Expanding the Empires: What Are the Housing GSEs Doing Today, and How Do These Activities Serve Their Public Purposes?,”* Vern McKinley, Policy Contributor to Cato Institute, AEI Conference Paper, 3/24/99)
- **Barbara Miles with Congressional Research noted the following: “Both Fannie Mae and Freddie Mac have invested in providing automated underwriting services to lenders and even directly to borrowers despite prohibitions on loan origination. Their provision of such financial services could ultimately do as much to undermine private mortgage insurers and other financial services providers as [Freddie’s] self-insurance plan now disallowed.** Further, the availability of the services directly to borrowers might lead incrementally to requests to lend directly to consumers, thus bypassing the primary lenders...There is no reason to believe that the allocation of resources in the economy would be improved and, to the extent that competition is reduced, the GSEs would have less market discipline to force through the full value of their charters.” (*“Government-Sponsored Enterprises: The Issue of Expansion into Mission-Related Business,”* Barbara Miles, Specialist in Financial Institutions, Congressional Research Service, 1/19/99)

***Mortgage Servicing News* column advises Fannie “to make love not war” with its business partners**

**Fannie & Freddie “face a dilemma: to continue growing at a clip that pleases its investors (and stock analysts) it has to cannibalize other pieces of the mortgage industry...Fannie faces a huge decision over the next five years: make peace with those griping about its business practices and find another way to increase earnings (is there another way?) or be prepared to experience bloodshed”**

- A recent *Mortgage Servicing News* column by Paul Muolo advises Fannie to play nice and to curb its bullying tendencies. Muolo outlines recent allegations that Fannie threatened various FM Watch members. Muolo notes that a recent press release by FM Watch Chairman Gerald Friedman

stated that board members have “been systematically approached and threatened by” Fannie and Freddie and had been subject to “attempts at intimidation and threats...In each instance the message was the same: stop supporting the activities of FM Watch or be prepared to see your business opportunities and products suffer.”

- **Muolo notes that FM Watch Chairman Gerald Friedman deserves credit for daring to speak out against the GSEs “on the record,” since people have griped “off the record” for several years. Muolo notes that lenders, mortgage insurance executives and a host of others have complained that “Fannie Mae and Freddie Mac are slowly – and not so slowly – nibbling at their market niches, stealing business, reducing their profit margins and endangering their livelihoods, using their Government charters as a battering-ram.”**
- **Muolo writes, “the point here isn’t necessarily about this latest battle in the industry’s civil war—it’s about getting the real issues out in the open...It’s also about Fannie Mae coming to the conclusion that its business partners—and their affiliates have, in some cases, a huge problem with the way this government-chartered firm conducts business.”** Muolo continues, “what Fannie Mae leaders should also realize is that most of the griping is pointed at them, not Freddie Mac. Every time I phone Fannie Mae’s PR department to report on a ‘bullying-related’ issue their spokespeople tend to think the latest allegation is incredulous or ‘old news.’”
- Muolo concludes, **“this skirmish with FM Watch...will get uglier, especially as it pertains to the mortgage insurance sector.”** One top mortgage lender, requesting anonymity, noted that Fannie wants a huge slice of the MI sector and will not stop until it gets it. Muolo notes, however, that **“if Fannie Mae thinks the MI industry is going to roll over and play dead it is mistaken.”**
- **Muolo notes that Fannie and Freddie “face a dilemma: to continue growing at a clip that pleases its investors (and stock analysts) it has to cannibalize other pieces of the mortgage industry. Legally, Fannie may have the right to do this. But to get to the ‘low-hanging’ fruit of the MI-related earnings, there will be casualties. Fannie faces a huge decision over the next five years: make peace with those griping about its business practices and find another way to increase earnings (is there another way?) or be prepared to experience bloodshed”** (*Mortgage Servicing News*, Paul Muolo, 3/16/01)

*US News and World Report* observes that Fannie & Freddie “are in the line of fire”

Scrutiny of the GSEs is likely to continue - “For two Washington and Wall Street favorites, it’s going to be a long, hot summer”

- A *US News and World Report* article by Anne Kates Smith examines the different perceptions that surround Fannie and Freddie. Smith asks if the GSEs are **“Good Housing Samaritans who have made homeownership available to folks previously overlooked by lenders, lowering mortgage rates for us all in the process? Are they the last true Wall Street darlings, among the few corporations revising earning estimates upward, as Fannie Mae did earlier this month? Or are they bloated risk takers who could shock the global financial system should they ever stumble, putting US taxpayers on the hook for a multibillion-dollar bailout?”** Smith quotes Capital Markets Subcommittee Chairman Congressman Richard Baker (R-LA) as stating, **“Taxpayers should be forewarned...We don’t have sufficient oversight of these extremely**

**complex institutions.”** Smith also noted that Baker plans on introducing legislation in early April that would create a new regulator to monitor the GSEs.

- Smith then outlined what is known about Fannie and Freddie: they are government-sponsored but taxpayer-owned; they have a \$2.25 billion line of credit with the US Treasury; they do not have to register their stocks with the SEC; and do not pay state and local income taxes. In addition, Fannie and Freddie’s debt is held by over 70 foreign central banks and thousands of US banks **“for whom the securities represent a significant portion of required capital...Little wonder their debt is seen as the de facto substitute for increasingly scarce treasury bonds.”** Critics contend that these special privileges are a problem and allow Fannie and Freddie to grow with few of the controls imposed on other institutions. **“The market doesn’t worry about the risk because of the belief they’ll be bailed out,”** said AEI Scholar Peter Wallison.
- Smith adds, **“Their size [Fannie and Freddie] is staggering by any measure.”** The GSEs have a collective \$1.1 trillion in outstanding debt. They own or guarantee \$2.3 trillion in mortgages and mortgage-backed securities. **“Meanwhile, critics continue, the safety nets underlying this great expansion – capital in relation to either assts (mortgages) or debt, for example, or loan loss allowances – are puny in comparison with other financial institutions.”** Smith quotes banking analyst Charles Peabody as warning: **“If they miscalculate the risks, there’s no room for error.”** Fannie’s spokesperson Janice Daue denies the company’s risk by noting that stress tests have shown that Fannie could withstand a 6-point change in interest rates over a ten-year span.
- Smith concludes that scrutiny of the GSEs is not likely to wane since two critical reports about the GSEs are due to be released soon. One report assesses the risk the GSEs put on the global financial market, while the other estimates the dollar value of the GSEs’ subsidies – which some have estimated as \$10 billion annually. Smith writes, **“For two Washington and Wall Street favorites, it’s going to be a long, hot summer.”** (*US News and World Report*, Anne Kates Smith, 4/2/01)

#### **Fannie & Freddie’s subordinated debt has cheapened significantly compared to its senior debt**

- According to *Dow Jones Newswire*, the subordinated debt issues of Fannie and Freddie have cheapened significantly in the past few weeks versus their senior notes. Despite the fanfare that accompanied the subordinated debt earlier in the year, “it doesn’t seem to have a huge following,” said Joe Portera, Managing Director at Mackay Shields. On March 20, Freddie’s spread on its subordinated debt compared to its senior debt stood at about 27.5 basis points, similar to the spread that Fannie’s subordinated notes were yielding over its comparable senior debt. Several factors may have contributed to the cheapening of the GSEs’ subdebt. An effort to distribute the bonds after the Freddie Mac pricing on March 14 may have put pressure on the sector, according to Brad Stone, Director of Interest Rate Product Strategy at Goldman Sachs. “The Street wound up long [on] some of this paper,” he said. In addition, “there could be some concerns over the upcoming Baker hearing,” said Stone. Also, reports that Warren Buffet sold nearly all of his holdings in Fannie and Freddie last year “gave a bit of a jolt to other investors,” said one dealer. (*Dow Jones Newswire*, Tyler Lifton, 3/20/01)
- In related news, *Bloomberg* reported that Fannie’s subordinated dept has slumped as investors balk at the yields. Brinson Partners Bond Manager Jamie Jackson noted that the 5.96% yield on Fannie’s \$1.5 billion of 10-year subordinated debt sold in January did not entice him to buy. The

subordinated debt notes are now yielding 8 to 10 basis points more than when they were priced. Originally, they sold at only 22 basis points more than Fannie's senior debt. The original yields "seemed too tight" compared to Fannie's senior debt, he said. He noted that the subordinated notes could slump further and trade at about a 35 basis point yield difference.

- The slump of the subordinated notes means that Fannie may have to pay a higher price to attract investors in the future. The notes still yield about 40 basis points less than like-rated debt from other financial institutions.
- Traders said the subordinated debt's initial sale reflected Fannie's "AAA" rating and the lure of higher yields rather than the risk of a new, untested security [rated AA- by S&P]. In fact, strong demand allowed the company to sell the notes at a yield that was 3 basis points less than planned.
- Traders said that Fannie's subordinated notes have suffered indirectly as investment banks failed to find buyers for Freddie's subordinated debt sale on March 14. Freddie Mac's yields have risen 7 basis points from pricing to about 29 basis points, and by one estimate to 32 basis points, more than the senior debt. Merrill Lynch & Co. and Goldman, Sachs led seven other banks in arranging the Freddie Mac sale. Dan Markaity, Head of Agency Bonds at Merrill Lynch & Co. said Merrill and Goldman, Sachs & Co. bought back notes other banks couldn't sell and later sold them to investors. Goldman Spokeswoman Kate Baum disputed this interpretation. The decline in the stock market and the slumping economy damped demand for lower-rated, riskier debt, said Markaity. (*Bloomberg News*, 3/22/01)

***American Banker* reports that mortgage insiders see the GSEs as "critic-proof"**

- According to Tom Fernandez with the *American Banker*, most critics of the GSEs concede that Fannie and Freddie play a key role in providing liquidity for mortgages and have "become almost untouchable." Fernandez quotes Joe Garrett, president of Sequoia National Bank as stating, "when it comes to the periodic political sniping at Fannie Mae and Freddie Mac, anyone betting against them for the last 15 to 20 years would have lost money...They are on the side of God, motherhood, cherry pie, and the American homeowner."
- **Peter Wissinger, CEO of Wells Fargo Home Mortgage, is quoted as stating that the GSEs "provide liquidity for mortgage funds within the US," which "is a very important role." He notes, however, that the mortgage playing field is not level since Fannie and Freddie receive favorable leverage ratios and cost-of-capital advantages. He states, "With the benefits they receive through the government guarantee, nobody can compete with them...And to where the agencies would say, 'Well, banks get implied benefits from the government,' I would say, 'Anybody can get a bank charter, but not anybody can get a GSE charter.'"**
- The GSEs claim to create significant savings to homeowners. A January 2001 Freddie Mac study concluded that the GSEs generate interest-cost savings at the range of "at least \$8.4 billion to \$23.5 billion per year." Fernandez quotes Alden Toevs, vice president of First Manhattan Consulting Group as stating the GSEs shave 20 to 30 basis points off of interest rates and 10 to 15 basis points for jumbo loans. Toevs also noted that "most rational thinkers would say that the GSEs are essential...there are some that would like Fannie and Freddie's role to diminish, thinking that they would make more money as a result." Fernandez adds that, "such critics are challenging the very existence of the mortgage-backed security market."

- In addition, the GSEs continue to court new “industry big shots” to “their corner.” Fannie released the roster of its National Advisory Council, an “all-star line-up” of mortgage industry players, prominent politicians, CEOs and a former cabinet member. (See [p. 38](#) in this *GSE Report* for more information.)
- Despite their all-star advisors, the GSEs have faced recent criticism from mortgage executives who asserted in a recent *Wall Street Journal* article that Fannie and Freddie have threatened to withdraw business from their companies unless they end their affiliation with FM Watch. Currently analysts are divided about the effects that these charges will have on the market. Gary Gordon of UBS Warburg stated, “so far, we’d say that the credibility goes to the GSEs. But we’ll stay tuned.” **However, Chad Yonker an analyst from Fox-Pitt Kelton noted that “It’s a very different situation for Fannie and Freddie than it ever has been in the past...It would be imprudent to say that all the political issues arising are just noise.” Since “very influential CEOs are willing to talk” against the GSEs, the allegations have a “heft” that is difficult to ignore, he said.** (*American Banker*, Tom Fernandez, 3/22/01)

<p><b>Under non-risk based capital rules, OFHEO announces that Fannie &amp; Freddie have met their minimum and critical capital levels</b></p>
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- OFHEO announced that both Fannie and Freddie were adequately capitalized at December 31, 2000. OFHEO determined that Fannie’s minimum capital requirement was \$20.293 billion and critical capital level was \$10.337 billion at December 31, 2000. Fannie’s core capital of \$20.827 billion on that date exceeded the minimum capital requirement by \$533.30 million and exceeded the critical capital level by \$10.490 billion. Freddie’s minimum capital requirement was \$14.178 billion and critical capital level was \$7.240 billion at December 31, 2000. Freddie’s core capital of \$14.380 billion on that date exceeded the minimum capital requirement by \$201.92 million and exceeded the critical capital level by \$7.140 billion.
- Fannie and Freddie's safety and soundness regulator - OFHEO- was established by the Federal Housing Enterprise Financial Safety and Soundness Act of 1992 and charged with the responsibility of implementing a ten-year stress test to determine the amount of risk-based capital needed to protect the GSEs during periods of severe economic conditions. Nine years later, OFHEO has not finalized the legally required risk-based capital standard for Fannie and Freddie. OFHEO announced that it had completed its work on the risk-based capital rule in December 2000 and it was sent to the OMB for its review and final clearance. The rule is not expected to be issued and published in the *Federal Register* for at least a few months, and will not be enforceable until one year after publication.
- While Congress waits for a risk-based capital standard, Fannie and Freddie have been able to operate under "minimum capital standards." On February 13, OFHEO announced that it would start issuing critical capital levels as part of its quarterly reports. The critical capital level is the amount of core capital below which an Enterprise must be classified as critically undercapitalized and generally must be placed in conservatorship. (*OFHEO press release*, 3/15/01)

## *Fannie Mae*

### **Fannie starts buying back its own debt to arbitrage profits**

**Jim Kellerman with Criterion Investment Management Co. wonders, “where the money is coming from for these buybacks.” Presumably, he states, Fannie will fund the program by issuing new debt**

**Fannie declined to comment on how the company is funding its debt buyback**

**The Fannie program could also place a price bottom under the securities and increase the borrowing activity of securities issues by Freddie unless Freddie implements a similar program**

**As Dow Jones Newswire reports, “one key difference between Fannie’s buyback and those of the US Treasury is that, while Uncle Sam is aiming to pay down its debt, Fannie Mae is actually increasing its amount of bonds outstanding.”**

- On March 27, Fannie announced that it had bought back \$410 million of long-term maturity debt, its first-ever buyback of older benchmark debt. Fannie bought back \$300 million of 6.25% issues maturing in May 2029, \$85 million of its 7.125% bonds maturing in January 2030, and \$25 million off its 7.25% bonds maturing in May 2030. The respective issues now have \$3.95 billion, \$4.739 billion and \$4.475 outstanding. The dollar amounts given are based on the original value of the bonds when they were sold. **Fannie did not provide what it actually cost the company to buy back the bonds or how the buyback was funded.** Fannie was seeking to buy back as much as \$600 million of bonds maturing in May 2029, January 2030, and May 2030, according to traders handling the transaction.
- Fannie announced on March 23 that it may begin periodically repurchasing its off-the-run Benchmark Notes and Benchmark Bonds for asset/liability management purposes. The company said it won’t buy back more than 20% of any outstanding issue and will not allow issues with a maturity of less than 10 years to slip below \$3 billion in size and issues with a maturity of more than 10 years to fall below \$2 billion in size. Initially, the housing agency will conduct its buybacks through one or more of its 11 core benchmark dealers. There will be no buybacks conducted within two weeks prior to a scheduled benchmark announcement if the maturity of the bond targeted for repurchase is similar to the non-callable benchmark scheduled to be sold. Subordinated benchmarks are excluded from the buyback program.
- By cutting available supply, Fannie may be able to raise the market value of its other outstanding debt. **Fannie’s debt repurchase program could help Fannie capture an arbitrage by allowing it to buy back a portion of its older securities more cheaply while securing stronger prices for the new issues.** Indeed, Fannie’s notes and bonds rallied after the company announced that it would start buying back older securities from its benchmark notes and bonds program. Traders said their yields narrowed as much as 5 basis points relative to Treasury yields. Investors are betting that as Fannie buys back debt, their scarcity will make them more valuable. Like many newer Treasuries, newer “on-the-run” Fannie benchmark debt, which is not subject to buybacks, is often priced slightly higher than “off-the-run” debt because it is easier to trade. Analysts noted that Fannie’s repurchasing of its debt may lower its overall debt costs and boost profits. **While Fannie said the repurchases are aimed at helping it manage its mortgage portfolio, the buyback plan**

could allow it to profit from arbitraging off-the-runs against on-the-runs. (*Bloomberg News*, 3/23/01; 3/27/01; *Dow Jones Newswire*, 3/23/01, 3/26/01; *Reuters*, 3/27/01)

- **Besides creating an arbitrage, market professionals said that Fannie’s debt repurchase program could place a price bottom under the securities and increase the borrowing activity of securities issues of other housing agencies, including Freddie – unless Freddie implements a similar program.** A Spokeswoman for Freddie said the company has no immediate plans to implement a buyback program. The possibility of Fannie entering the market to buy back bonds “puts a (price) floor on off-the runs,” said Jim Kellerman, Director of Portfolio Management for Criterion Investment Management Co. **Debt professionals are unsure how much debt Fannie might repurchase. “What we’re trying to figure out is where the money is coming from for these buybacks,” said Criterion Investment’s Kellerman. Presumably, the program will be funded by issuing new debt, he said.** Fannie’s Vice President for Debt Funding John The Losen declined to comment on how Fannie plans to fund its debt buybacks. *As Dow Jones Newswire reports, “one key difference between Fannie’s buyback and those of the US Treasury is that, while Uncle Sam is aiming to pay down its debt, Fannie Mae is actually increasing its amount of bonds outstanding.”* (*Dow Jones Newswire*, Tyler Lifton, 3/26/01)

**Bowing to pressure from critics and negative publicity, Fannie says it will stop collecting its controversial fees (“equity shares”) from borrowers as part of the company’s reverse mortgage program (targeted to senior citizens)**

**Critics charged that the effective interest rates on some of these reverse mortgages exceeded 30-40% a year**

- The *Washington Post* reported that Fannie bowed to pressure from the AARP and other housing advocates and stopped collecting controversial “equity shares” attached to certain reverse mortgages in their “Home Keeper” program. According to the *Washington Post*, Fannie Mae’s reverse mortgage loan program allowed seniors age 62 and above to use their house for collateral for a cash loan. The cash is usually doled out in one lump sum, periodic payments, or a credit line. While the loan payment plus interest and fees typically are not repaid until after a senior dies or sells their home, there was also a controversial “equity share” option which allowed for a higher initial cash payment in return for an equity share of a borrower’s home. Under Fannie’s program, seniors who took out “reverse mortgages” through Fannie owed the company interest on the loans as well as a portion of the appreciated resale value of the properties. The 10 percent equity share provided Fannie the right to collect thousands of dollars in extra loan fees – especially in high-cost, high-appreciation markets. Critics charged that the effective interest rates on some of the loans could exceed 30 to 40 percent a year.
- In addition to the controversial extra fees, Fannie has also faced criticism for the nature of the loan program. Housing and senior advocates have charged that Fannie’s program includes a provision for a big jump in loan fees immediately after the two-year anniversary of a closing. The *Washington Post* quotes the National Center for Home Equity Conversion as reporting that a 75-year-old woman with a \$200,000 home who paid off early in the third year of a Fannie “Home Keeper” loan would end up with an effective interest rate over the loan term of nearly 35% per year.
- **The *Washington Post* claimed that as Fannie found themselves reaping in far larger equity shares than expected, the company took a second look at the program’s fairness to borrowers**

**and its “appropriateness for a congressionally chartered private financial institution.”**

Fannie asked participating lenders to forgo collection of further home equity shares as part of loan payoffs and to immediately inform current borrowers of the change in policy. Fannie estimates that it owns about 3,000 reverse mortgages with the equity-sharing feature. In its letter to lenders, Fannie explained that “since the equity share feature was offered, the market has changed in many ways. Home price appreciation has been greater, interest rates have fluctuated, and in some cases, loans have prepaid earlier than expected.”

- Roy Green of the AARP praised Fannie for “taking the high road.” One mortgage industry source noted, “It’s clear to me that [Fannie Mae] looked at the option of dealing with borrowers one by one,” but the potential legal complications and bad publicity were too large.” (*The Washington Post*, March 17, 2001)

**Fannie says it will work more closely with smaller lenders**

**Fannie wants to help smaller lenders create “virtual” mortgage businesses to compete against large lenders**

- In a speech to the Independent Community Bankers of America, Fannie’s Chairman Franklin Raines says the company will make smaller lenders “a new priority.” Raines says the company plans to increase its business with small banks by at least 20%. “We want to help the small community lender build a successful mortgage business that can compete with any big bank in the country,” said Raines. He claims that through e-commerce, Fannie can assist small lenders in creating a “virtual” mortgage business without having to hire mortgage experts, build a back office, overload your portfolio or take all the risks. With Fannie’s technology and mortgage products, Raines claims that any small community bank in America can give its customers the same mortgage services they could get at any large metropolitan bank in the country.
- Such moves, several sources said, could mean that Fannie and Freddie do not think they can achieve their desired growth from exclusive deals with large lenders and that they must now court a patchwork of smaller lenders nationwide. One source noted that “Effectively, Fannie Mae is competing with the large wholesalers to see who the smaller companies will be the customer of.” (*Fannie Chairman Franklin Raines speech to the ICBA*, 3/8/01; *American Banker*, Robert Julavits, 3/14/01; *Dow Jones Newswire*, John Connor, 3/9/01)

**Fannie names new members to its National Advisory Council**

- Fannie named 23 new members to its National Advisory Council. Council members meet three times a year with Fannie’s senior management. The council has 48 members. The members serve two-year terms with approximately half of the membership rotating off at the end of the year.
- The incoming 2001 National Advisory Council chair is Ron McCord, chairman of First Mortgage Company and Holliday American Mortgage Company. Mr. McCord is a former president of the Mortgage Bankers Association of America (MBAA).

The following new members have been appointed to serve until October 2002:

- (1) Stephen E. Adamo, president and chief operating officer of Citizens Mortgage Corporation, East Providence, Rhode Island.
- (2) The Honorable Clarence E. Anthony, mayor of South Bay, Florida.

- (3) David M. Applegate, president and chief operating officer of GMAC Residential Holding Corp., Horsham, Pennsylvania.
- (4) Harley D. Bergmeyer, chairman of the Board of Saline State Bank, Wilber, Nebraska.
- (5) The Honorable Henry Cisneros, chief executive officer and chairman of American CityVista, San Antonio, Texas. Previously, Mr. Cisneros was president and chief operating officer of Univision Communications in Los Angeles, and from 1993-97 he served as secretary of the U.S. Department of Housing and Urban Development.
- (6) C.R. "Rusty" Cloutier, president and chief executive officer of MidSouth National Bank. Lafayette, Louisiana.
- (7) Martin Edwards Jr., partner at Colliers Wilkinson Snowden, Inc., a commercial and industrial real estate firm located in Memphis, Tennessee. Mr. Edwards is the 2001 president-elect of the NATIONAL ASSOCIATION OF REALTORS®.
- (8) Terence "Terry" W. Edwards, president and chief executive officer of Cendant Mortgage, Mt. Laurel, New Jersey.
- (9) Joseph L. Falk, president of Irian Mortgage Services, a consulting firm specializing in mortgage brokering, regulatory compliance, and governmental affairs located in Coconut Grove, Florida. Mr. Falk also is the current president-elect and serves on the Board of the National Association of Mortgage Brokers. He will take office as national president in June 2001.
- (10) William A. Fitzgerald, chairman and chief executive officer of Commercial Federal Bank, FSB, Omaha, Nebraska. He is the immediate past chairman of the America's Community Bankers (ACB).
- (11) F. Gary Garczynski, president of the National Capital Land Development Company, Woodbridge, Virginia. Mr. Garczynski also is the first vice president of the National Association of Home Builders.
- (12) Robert A. Goethe, chairman and chief executive officer of Regions Mortgage Inc., Montgomery, Alabama.
- (13) Jack R. Gravo, president and chief executive officer of FirstMerit Mortgage Corporation, Canton, Ohio.
- (14) William F. Hofmann III, executive vice president and treasurer of Provider Insurance Group Inc., Belmont, Massachusetts. Mr. Hofmann was installed as president of the Independent Insurance Agents of America (IIAA) in October 2000.
- (15) The Honorable Glenda E. Hood, mayor of Orlando, Florida.
- (16) John B. Johnson, president and chief executive officer of MortgageAmerica, Inc., Birmingham, Alabama. Mr. Johnson currently serves as a member of the Board of Directors of the Mortgage Bankers Association of America and vice chairman of its Residential Board of Governors.
- (17) Ron J. McCord, chairman of First Mortgage Company, L.L.C and Holliday American Mortgage Company, Oklahoma City, Oklahoma. Mr. McCord is a former president of the Mortgage Bankers Association of America (MBAA).
- (18) Mark O'Brien, president and chief operating officer of Pulte Homes Inc., Bloomfield Hills, Michigan.
- (19) Jose "Tony" A. Rey, president of Rey Homes, Orlando, Florida.
- (20) J. Ronald Terwilliger, national managing partner of Trammell Crow Residential, Atlanta, Georgia.
- (21) Catherine B. Whatley, broker/owner of Buck and Buck, Inc., Jacksonville, Florida. Ms. Whatley is the 2001 first vice president and will become president of the NATIONAL ASSOCIATION OF REALTORS® in 2003.
- (22) Frank P. Willey, vice chairman of Fidelity National Financial, Inc., Santa Barbara, California, the nation's largest title insurance organization. Mr. Willey is president-elect of the Board of

Governors of the American Land Title Association (ALTA) and will be installed as ALTA's president in October 2001.

(23) Tom Wind, president and chief operating officer of CitiMortgage.

Returning members of the National Advisory Council include:

- (1) David Bochnowski, chairman and chief executive officer of Peoples Bank, SB, Munster, IN;
- (2) Stephen Brobeck, executive director of Consumer Federation of America, Washington, DC;
- (3) The Honorable Lee P. Brown, mayor of the City of Houston;
- (4) Diana Bull, broker/owner of RE/MAX Santa Barbara/Montecito, Santa Barbara, CA;
- (5) Ernest Clark, Jr., president of Seville Real Estate, Oakland, CA;
- (6) Dennis R. Cronk, broker/owner of Waldvogel, Poe & Cronk Real Estate Group, Inc., Roanoke, VA;
- (7) Craig S. Davis, president, Home Loans & Insurance Service of Washington Mutual, Seattle, WA;
- (8) Frank P. Filippis, chairman and chief executive officer of Radian Guaranty Inc., Philadelphia, PA;
- (9) Renee Lewis Glover, executive director of The Housing Authority of the City of Atlanta, Atlanta, GA;
- (10) Terry C. Havens, chairman and chief executive officer of Reilly Mortgage Group, McLean, VA;
- (11) William J. Inman, president of NVR Mortgage, McLean, VA;
- (12) Louis W. Jennings, executive vice president of mortgage operations for Navy Federal Credit Union, Vienna, VA;
- (13) Susan C. Keating, president and chief executive officer of Allfirst Financial Inc., Baltimore, MD;
- (14) Stanford L. Kurland, president and chief executive officer of Countrywide Home Loans, Inc., Calabasas, CA;
- (15) Zoila Levis, president and chief operating officer of Doral Financial Corp., Puerto Nuevo, PR;
- (16) Regina M. Lowrie, president and chief executive officer of Gateway Funding Diversified Mortgage Services, Fort Washington, PA;
- (17) Stewart Morris Jr., president of Stewart Title Company, Houston, TX;
- (18) James M. Murphy, founding principal and president of New England Realty Resources, Inc., Boston, MA;
- (19) Jeff L. Plagge, president and chief executive officer of First National Bank of Waverly, Waverly, Iowa;
- (20) The Honorable Paul Schell, mayor of the City of Seattle;
- (21) A. William Schenck, president and chief executive officer of Tradenable, Redwood Shores, CA;
- (22) Bruce C. Smith, president of Smith Quality Homes, Alamo, CA;
- (23) Donald W. Sowell, president and chief executive officer of Don Sowell Interests, Inc. – DSI, Prairie View, TX;
- (24) Debra M. Warren, president and chief executive officer of First Union Mortgage Corporation, Charlotte, NC;
- (25) Lawrence P. Washington, senior executive vice president of First Nationwide Mortgage Corporation, Frederick, MD. (*Fannie press release, 3/20/01*)

**Fannie further expands its political reach by including Federal and State officeholders in its press conferences and press releases and increasingly using its Partnership Offices in press events**

**Fannie has 44 Partnership Offices open across the country**

**Financial consultant Bert Ely believes Fannie's media events raise ethical questions. "This is an extension of not only their lobbying but also their political action committee contributions," he said. "Everybody knows what they're doing. It's something that many of us find offensive, but that's how they play the political game."**

**Fannie claims its partnership offices were created "to get away from Washington," yet *Real Estate Finance Today* reports that during the first eight months of 2000, Fannie held no fewer than 87 media opportunities across the country with Congressional Members**

Fannie claims its partnership offices were created "to get away from Washington," yet Fannie and its partnership offices hold numerous press conferences with Congressional Members

- Fannie's Betsy Hildebrandt claims that Fannie's media events with Congressional Members "are not directed from Washington." She said most of the events happen in their Partnership Offices and "are basically product introductions where the member of Congress has asked us to participate in a program." She claims the Partnership Offices were created to develop relationships in local communities. "The idea of the Partnership Offices was to get away from Washington," she said. "It's been a wildly successful initiative."
- Research by *Real Estate Finance Today* found that during the first eight months of 2000, Fannie held no fewer than 87 media opportunities across the US with Congressional Members. This compares with 60 media events in all of 1999. The events in both years have involved 29 members of the Senate (of whom 12 were up for re-election in 2000) and 95 Members of the House (most of whom face contested re-election bids). Since 1999, Fannie has held media events with at least 13 Members of the House Banking Committee and seven Members of the Senate Banking Committee. (*Real Estate Finance Today*, Michael Sorohan, 9/11/00)

Fannie's media events raise ethical questions

- Financial consultant Bert Ely said that while Fannie's media events demonstrate the company's influence with Congress, they also raise ethical questions. "This is an extension of not only their lobbying but also their political action committee contributions," he said. "Everybody knows what they're doing. It's something that many of us find offensive, but that's how they play the political game." (*Real Estate Finance Today*, Michael Sorohan, 9/11/00)

Fannie has 44 partnership offices

- According to Fannie's Web site, the company has 44 partnership offices open across the country ([http://www.fanniemae.com/contact/partnership\\_offices.html](http://www.fanniemae.com/contact/partnership_offices.html), 3/23/01)

Cong. Melissa Hart (R-PA) and Pittsburgh Councilwoman Valerie McDonald

- Fannie held a press conference with the above named officials to announce a new \$5 million "Women-Headed Households" initiative in the Pittsburgh area. The officials were named co-chairs of the initiative. McAuley Institute is working with Fannie as part of its national Make It Your Own™ Women's Homeownership Campaign. The initiative is targeted to those living in

Allegheny, Beaver, Butler, Fayette, Washington and Westmoreland Counties. Through the campaign, McAuley will provide low-interest loans to finance affordable home development through a revolving \$12.1 million loan fund. In addition, McAuley will conduct focus groups among women to learn more about the kinds of resources needed in order to bridge the homeownership gap. Fannie intends to purchase up to \$50 million in affordable mortgage products in connection with the Make It Your Own Campaign as a first step under its national Women-Headed Households Initiative. The lender partners are Fidelity Bank, Mellon Bank and Three Rivers Bank. (*Fannie press release, 2/21/01*)

#### Cong. Lee Terry and Omaha Mayor Hal Daub

- Fannie held a press conference to announce the grand opening of the newly renovated Farnam Building Apartments. The \$4 million renovation of the 30-unit affordable housing development includes 18 two-bedrooms and 12 three-bedroom apartments. In addition, more than 6,000 square feet has been set aside for commercial use, including a new US Postal Service station. Fannie made an equity investment of \$536,000 in the Farnam Building Apartments. (*Fannie press release, 2/20/01*)

#### Cong. Stephanie Tubbs Jones (D-OH)

- Fannie held a press conference with Cong. Tubbs Jones to announce that Fannie agreed to purchase \$100 million in affordable housing loans in the next three to five years for low-to-moderate income families from Bank One, Charter One, Dollar Bank, First Merit, Huntington, KeyBank, and Ohio Savings. (*Fannie press release, 2/23/01*)

#### Cong. Julia Carson (D-IN) and Indianapolis Mayor Bart Peterson

- Fannie held a press conference with the above named officials to announce the opening of the first mixed-rate affordable housing development in the city of Indianapolis – the Davlan Apartments. Riley Area Development Corporation is the owner and developer of the property. Alliant Capital, the City of Indianapolis, First Indiana Bank, the Indiana Housing Finance Authority, Indianapolis Neighborhood Housing Partnership, and the National City bank of Indiana provided funding for the Davlan Apartments. Fannie made a \$3.9 million Low-Income Housing Tax Credit equity investment in the property through its partner Alliant Capital. More than 13,000 square feet of the building has been set aside for commercial use. (*Fannie press release, 2/23/01*)

#### Cong. Charlie Norwood (R-GA)

- Fannie held a press conference with Cong. Norwood to announce the grand opening of Wedgewood Park Apartments – a newly constructed 200-unit apartment complex. Fannie committed to provide \$5.5 million in mortgage debt financing. (*Fannie press release, 2/23/01*)

#### Cong. J.C. Watts (R-OK) and Comanche County Commissioner Larry Buchwald

- Fannie held a press conference with the above named officials to announce a \$14 million mortgage revenue bond issued by the Comanche County Home Finance Authority. Fannie agreed to purchase \$11.4 million of the bonds, which will be used to provide below market mortgage financing for more than 250 Comanche County families. Bond proceeds will be made available through participating lenders Countrywide Home Loans, BankOklahoma Mortgage, and Local Federal Mortgage. Qualifying borrowers will be eligible for loans offered at a fixed-rate of 6.96 percent for 30-year terms with down payment and closing cost assistant grant equal to 4 percent of the loan amount. (*Fannie press release, 3/12/01*)

Cong. Lincoln Diaz-Balart (R-FL)

- Fannie held a press conference with Cong. Diaz-Balart to announce the construction of a new affordable housing apartment tower in downtown Miami. Fannie made a \$12 million Low-Income Housing Tax Credit equity investment in the property through its partner Alliant Capital and Fannie agreed to purchase the \$4.9 million in mortgage debt originated by ARCS Commercial Mortgage. (*Fannie press release, 3/19/01*)

Cong. Harold Ford (D-TN)

- Fannie held a press conference with Cong. Ford to announce Fannie's \$200,000 CDFI deposit investment in MemphisFirst Community Bank, a minority owned lender. (*Fannie press release, 3/13/01*)

**Fannie Mae Foundation holds Capitol Hill press conference with lawmakers to distribute checks to homeless service providers**

**Fannie Mae Foundation launches national spring advertising campaign to consumers**

**There's a "perception in Washington that the company's philanthropy is calculated to reward friends, punish enemies, curry favor with key members of Congress and brand its name with the public through an expensive television advertising campaign." – *St. Petersburg Times***

**"It's clearly used as hush money to buy silence of groups that might otherwise be critical of Fannie Mae," said Bruce Marks, one of the housing activists whose criticisms of then-Fannie Mae CEO James Johnson at a conference years ago resulted in a tiff over a grant.**

***St. Petersburg Times* notes that "at the very least, the foundation's long reach can call into question the objectivity of the affordable housing organizations that rally to Fannie Mae's side."**

- The Fannie Mae Foundation held a press conference on February 21 to distribute more than \$6 million raised from the Help the Homeless Campaign and Walkathon to 205 homeless service providers in the Greater Washington area. The Foundation also presented Good Neighbor awards to three individuals and to the Downtown DC Business Improvement District. The press conference was held in the Russell Senate Office Building. According to an announcement about the event, the following Congressional members were invited: Cong. Constance Morella (D-MD), Cong. Albert Wynn (D-MD), Delegate Eleanor Holmes Norton (D-DC), Cong. Thomas Davis (R-VA), and DC Council members Linda Cripp and Sandra Allen. (*FNS Daybook, 2/21/01; Washington Post, 2/22/01; Fannie Mae Foundation press release, 2/21/01*)
- The Fannie Mae Foundation launched its spring advertising and consumer outreach campaign on March 19 to help educate families and individuals about all aspects of the home-buying process. Each ad will include a toll-free number for viewers to call (1-800-688-HOME or 1-800-688-4663) to order the Foundation's free home-buying guides, which are available in nine languages. In addition to advertisements on national cable and broadcast network television, the campaign will include a 30-minute educational program called "Borrowing Basics: What You Don't Know Can Hurt You," airing on Black Entertainment Television (BET) began March 25. The program will run every Sunday through June 17. Spanish-language advertising will run on Latino cable stations Univision and Telemundo. The Foundation also plans to mail 2.43 million pieces of direct mail to the general public. (*Fannie Mae Foundation press release, 3/19/01*)

St. Petersburg Times questions the Fannie Mae Foundation's contributions and advertising to consumers

- **As reported in the August 18, 2000 GSE Report, Mary Jacoby reported in the *St. Petersburg Times* that the Fannie Mae Foundation has come under fire by critics who charge that the Foundation awards grants and donations to Fannie-friendly politicians and groups, and conversely, will deny grants to groups that criticize Fannie Mae.** Jacoby reported that John Taylor, President of the National Community Reinvestment Coalition, faced a situation where the Fannie Mae Foundation had promised his group a grant of \$65,000 only to rescind their offer after Taylor criticized the GSE at a housing conference. Jacoby quotes Taylor as stating, “the next day I was informed they had run out of money. There was no doubt (the loss of the grant) was connected to the criticism.” While the grant was eventually made, Jacoby notes that **“the incident reinforced a perception in Washington that the company’s philanthropy is calculated to reward friends, punish enemies, curry favor with key members of Congress and brand its name with the public through an expensive television advertising campaign.”**
- **Jacoby noted that there is nothing wrong with a company making charitable contributions toward causes to use as positive public relations. However, “Fannie Mae is not just any corporation. It is a quasi-governmental financial behemoth that sits at the crossroads of national politics and high finance. And it is playing for enormously high financial stakes.”**
- **Jacoby noted that Fannie’s philanthropy has become “a political cauldron” in which Fannie uses its Foundation as a tool to aggressively lobby Members of Congress and other potential critics. “It’s clearly used as hush money to buy silence of groups that might otherwise be critical of Fannie Mae,” said Bruce Marks, one of the housing activists whose criticisms of then-Fannie Mae CEO James Johnson at a conference years ago resulted in a tiff over a grant.**
- **Jacoby notes that while Fannie claims its philanthropy is a separate entity it clearly has close ties to its namesake. The foundation is located on the Fannie Mae campus in Washington, DC and Fannie’s CEO Franklin Raines and Vice Chairman Jamie Gorelick are top officers of the Fannie Mae Foundation, while another director, Berry Zigas, has been a registered lobbyist for Fannie. What’s more telling is the company’s financial records -- making \$33 million in direct charitable contributions and grants in 1998 (the last year tax returns are available) while simultaneously spending over \$43 million on a controversial TV and direct-mail ad campaign. While Fannie claims the ads are “educational outreach,” critics disagree. “It’s branding the Fannie Mae name,” said FM Watch Executive Director Mike House.**
- **In addition, Fannie Mae critics accuse the GSE of using its foundation to make grants to curry political favor. Peter Wallison of the American Enterprise Institute is quoted as stating, “they use the foundation by making contributions to community groups in the states and districts of members of Congress who can be helpful, especially to community groups that are favorites of the congressmen or senators.” Jacoby added that the *St Petersburg Times* did a brief analysis of the company’s 1998 grants, which echoed Wallison’s analysis.**

- **Jacoby writes, “at the very least, the foundation’s long reach can call into question the objectivity of the affordable housing organizations that rally to Fannie Mae’s side.” At a Subcommittee hearing last year, Cong. Paul Kanjorski (D-PA) referred to a number of letters from housing groups opposing Cong. Baker’s GSE bill to strengthen regulation of the GSEs. Jacoby noted that “Many were recipients of Fannie Mae Foundation grants.”** (*St. Petersburg Times*, Mary Jacoby, 7/17/00)

## ***Freddie Mac***

<b>Freddie is investing in Islamic “no interest” loans</b>
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- Freddie announced that it is investing in home financing contracts that are acceptable under both Islamic and American law. Freddie has invested an estimated \$1 million in contracts from American Finance House – LARIBA under an agreement that makes it the nation’s first Islamic financial institution to achieve Freddie Mac Seller/Servicer status.
- Observant American-Muslim families require a special housing contract because Islamic religious law prohibits the payment of interest on mortgages and other types of debt. American Finance House – LARIBA developed a Home Finance model for the American-Muslim community.
- The Islamic housing finance model uses standard real estate financing documents, in accordance with state and local law, and is serviced like a conventional mortgage. The key to the model is an agreement between American Finance House – LARIBA and the prospective homeowner that establishes jointly negotiated maximum monthly payments based on the property’s sale price and fair rental value that mark the property to the market. American Finance sidesteps interest by entering a partnership with customers to buy a home. The customer acquires the home through a lease-to-own arrangement. Their monthly payment includes two components: repayment of the lender’s contribution to the purchase price and fair-market rent. The deal also gets translated into the conventional lending documents to conform to US real estate laws. At that point, the numbers in the Islamic deal are translated into a conventional house deal, interest rate and all. Islamic lenders call this an “implied interest rate” and borrowers have a sum that Yahia Abdul-Rahman, an adviser to American Finance House – LARIBA, says may be deducted as mortgage interest for income tax purposes. An IRS spokesman said the agency has never ruled on the legitimacy of such deductions. Abdul-Rahman says under the new agreement with Freddie, required down payments have been halved to 20% and maximum repayment periods tripled to 30 years. (*PR Newswire*, 3/28/01; *USA Today*, Thomas Fogarty, 3/28/01)

## ***Federal Home Loan Banks***

### **FleetBoston applies for dual FHLBank membership**

**FHLBank of New York supports FleetBoston's request for dual FHLBank membership**

**FHFB is also considering Washington Mutual's request for dual FHLBank membership**

**The FHLBanks of Atlanta, Boston, Des Moines, and San Francisco object to Washington Mutual's application – ask FHFB to issue a broad rule on the issue of dual membership instead**

**FHFB is drafting an advance notice of proposed rulemaking on dual membership**

- FleetBoston Financial Corp., currently a member of the FHLBank of Boston, has applied to become a member of the FHLBank of New York – now that its acquisition of Summit Bank is complete. Summit Bank was a member of the FHLBank of New York. Alfred DelliBovi, the President of the FHLBank of New York, is welcoming FleetBoston “with open arms.” Mr. DelliBovi noted “consolidation is having an impact on the system,” and argued that it is outdated to expect large banking companies to confine themselves to the regional boundaries of the 12 FHLBanks. He said that FHLBanks could lose members if current rules, which prohibit membership in multiple districts, are not adjusted.
- Mr. Dellibovi said the FHLBank of New York is expected to approve FleetBoston's application in May, and he urged the FHFB to approve the FleetBoston and Washington Mutual's pending application soon. The FHFB already has a dual membership application by Washington Mutual Bank under consideration. WaMu is requesting to join the FHLBank of Dallas while retaining membership in the San Francisco FHLBank. WaMu wants to join the FHLBank of Dallas because it recently acquired Bank United, which was a member of the FHLBank of Dallas. The FHLBanks of Atlanta, Boston, Des Moines, and San Francisco and World Savings object to Washington Mutual's application and instead would like the FHFB to issue a broad rule on the issue of dual membership. Other FHLBanks have urged the FHFB to do a rule-making process to address the issues of dual membership prior to making any decisions. Mr. DelliBovi said WaMu's application should be approved because without its biggest customer (Bank United), the Dallas FHLBank will have problems serving its smaller members. Bank United held 25% of the Dallas FHLBanks' capital stock and 18% of its outstanding advances.
- FHFB Spokesman Bill Glavin said the FHFB is drafting an advance notice of proposed rulemaking that would deal with the systemwide implications of dual membership. Mr. DelliBovi considers it a good sign that the FHFB is drafting an advance notice of rulemaking. “The fact that they are doing a rulemaking suggest that they believe very strongly that they have the power to do this.” (*National Mortgage News Daily*, 3/21/01, 3/26/01; *National Mortgage News*, 3/26/01; *American Banker*, Jennifer Gordon, 3/21/01, *American Banker*, 3/30/01)

**Florida lawmakers are considering a bill that would allow small banks and thrifts to pledge FHLBank letters of credit as collateral on public deposits**

**Tennessee and a few other states have passed similar bills**

- The *American Banker* reported that the Florida Bankers Association is pushing a bill that would allow small banks and thrifts to pledge FHLBank letters of credit – instead of more tangible assets - as collateral on public deposits. Laura Thompson with the *American Banker* explains that many states, including Florida, require that banks pledge bonds or other assets as collateral on government deposits that exceed the \$100,000 FDIC insured limit. Bankers say many small banks have trouble meeting the requirement and are thus excluded from bidding on public deposits. The Florida Bankers Association is pushing the bill because many banks are struggling to attract funds and they would like to encourage more banks to participate in public deposit programs. Similar bills have passed in Tennessee and other states. (*American Banker*, Jennifer Gordon, 3/21/01)

***Farm Credit System/Farm Credit Banks***

**Farm Credit Administration (FCA) delays the comment period on its controversial national charter proposal**

- The FCA announced that it is extending the comment period for 30 more days on its national charter proposed rule. The previous deadline for comments was March 19, 2001. The new deadline for comments is April 20, 2001. (*Federal Register*, page 15814, 3/21/01)

Background on the proposal

- Traditionally, institutions in the Farm Credit System have been limited to certain geographical regions. Under the controversial proposal, individual farm credit lending institutions would be able to apply for a national charter, which would let them lend beyond their current regional geographic boundaries. The FCA adopted the proposed rule at a January 11, 2000 meeting. In May 2000, the FCA issued a booklet to all system institutions providing guidance on applying for national charters. Several parties, including former House Banking Committee Chairman Jim Leach and the GAO raised procedural concerns that the FCA bypassed the formal rule-making process when issuing the rule. Responding to criticisms, in July 2000, the FCA published the booklet in the *Federal Register* for public comment. On January 11, 2001 the FCA adopted the proposed rule and sent it to the House and Senate agriculture committees for a 30-day review. The proposed rule was published in the *Federal Register* on February 16, 2001 for a 30-day comment period.
- Both the Senate and House Agricultural Committees held recent hearings on the FCA's controversial national charter proposal. During the February 26 Senate Agricultural Committee hearing, **Former House Banking Committee Chairman Cong. Leach (R-IA) testified that the proposal, if adopted, would “expand to 34 the number of government sponsored enterprises operating in the American economy and each of these new GSEs will have power greater than that of Fannie Mae or Freddie Mac.” He called the proposal “the single greatest act of administrative arrogance I have ever seen” and believed that the proposal “should be absolutely rejected.”** (*BNA Daily Report for Executives*, 3/22/01)

## *Ginnie Mae*

<b>President Bush names Ronald Rosenfeld as President of Ginnie Mae</b>
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- President Bush announced that he intends to nominate Ronald Rosenfeld to be President of Ginnie Mae. Rosenfeld was most recently the Secretary of Commerce for the State of Oklahoma and served as the Deputy Assistant Secretary of the Treasury for Corporate Finance from 1992 to 1993. He served at the Department of Housing and Urban Development from 1989 to 1991 in several positions including Federal Housing Commissioner and Deputy Assistant Secretary for Single Family Housing. Rosenfeld is a graduate of the University of Pennsylvania and received his J.D. from Harvard University. Rosenfeld's appointment is still subject to Senate approval. Ginnie Mae has been without a President for several years. Ginnie Mae Executive Vice President George Anderson has been running the program. (*White House press release, 3/26/01; National Mortgage News Daily, 3/29/01*)

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