

The **GSE** REPORT TM

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Major Events

House Financial Services Committee Holds Hearing on Administration's GSE Views

Administration Supports Strong Single Regulator, with HUD Continuing to Regulate Affordable Housing

Administration would like to eventually include FHLBanks under the single regulator

New regulator would have authority to review and change minimum and risk-based capital standards for Fannie & Freddie – no moratorium on capital

Treasury does not support requiring Fannie & Freddie to comply with the SEC Act of '33

Administration recommends elimination of Presidential appointments to Fannie & Freddie's boards

Democrats concerned that moving the GSE regulator would compromise Fannie & Freddie's mission – did not see a crisis

Treasury Secretary testifies in favor of Treasury regulating Fannie/Freddie and the FHLB system

Legislative Update

House Financial Services Committee Holds Hearing on Administration's GSE Views

- The House Financial Services Committee held a September 10 hearing on the Administration's views on oversight of Fannie and Freddie. House Financial Services Committee Chairman Michael Oxley (R-OH) chaired the hearing. Treasury Secretary John Snow and HUD Secretary Mel Martinez testified. The hearing discussed the Administration's proposal to create a strong single regulator to oversee Fannie and Freddie.
- Chairman Oxley wanted to ensure that Congress act in a "reasonable manner" to improve the regulation of the GSEs, but cautioned against any adverse impact on the housing or equity markets. In his opinion, OFHEO does not have the tools or the mandate to adequately regulate Fannie and Freddie.
- Senate Banking Committee Chairman Richard Shelby (R-AL) and Chairman Oxley released a statement shortly after the hearing announcing their intention of drafting legislation based on the Administration's principles for GSE regulation outlined at the hearing by Secretaries Snow and Martinez.

Highlights of the hearing:

1. Administration supports strong single regulator for Fannie & Freddie under Treasury - New regulator would oversee the safety and soundness and new program approval

Snow testified that there is a general consensus that OFHEO does not have the tools or the stature to deal with the large size, complexity and importance of Fannie and Freddie. The Administration recommends that Congress pass legislation to create a new federal agency to regulate and supervise Fannie and Freddie. The new regulator, in consultation with HUD, should be given the powers that are comparable in scope and force to those of other financial regulators including the responsibility to oversee new and ongoing GSE activities in keeping with the terms of the GSEs' charters. The new regulator should also be given clear specified authorities, which Snow outlined in his written testimony. Should Congress create a new regulatory agency that contains all of the standards and duties of effective financial supervision as Snow outlined in his testimony, the Administration is prepared to consider placing the agency under a cabinet department, specifically Treasury. Simply moving OFHEO under Treasury without the expanded powers is not acceptable.

The new regulator would not be completely independent from Treasury. At a minimum, the new regulator would among other things, be required to clear new regulations and congressional testimony through Treasury.

2. HUD would continue to oversee affordable housing but with enhanced powers

While safety and soundness (including new program authority) should be included under a new single regulator, the Administration supports retaining the GSEs' affordable housing goals at HUD. Martinez testified that the Administration supports increasing HUD's authority in this area. The Administration proposes (1) creating a new GSE Housing Office within HUD, independently funded by the GSEs, to establish, maintain, and enforce the housing goals; (2) institute enhanced civil penalties for failure to meet housing goals; (3) explicitly provide that the GSEs act to increase homeownership; and (4) expand HUD's authority to set housing goals and subgoals beyond the three goals currently established for moderate-income, geographic area, and special affordable housing. Martinez noted that HUD's internal studies and several independent studies have shown that Fannie and Freddie lag the market with respect to affordable housing.

3. Administration would like to eventually include FHLBanks under the single regulator

Snow testified that there is a need for the FHLBanks to be included as part of a single regulator. However, while there is a consensus with respect to creating a new regulator for Fannie and Freddie, a similar consensus may not yet exist with regard to the FHLBanks. Snow does not want the issue of including the FHLBanks to get in

the way of enacting legislation to create a world-class regulator for Fannie and Freddie. He encouraged the FHLBanks to caucus on the issue to form a consensus.

4. New regulator would have authority to review and change minimum and risk-based capital standards for Fannie & Freddie – no moratorium on capital

Snow testified that the Administration does not recommend changes at this time to Fannie and Freddie's risk-based capital standards, however, they are in no way proposing a moratorium on making adjustments to the risk-based capital standards (as was reported recently in the press). The new regulator should have more flexible authority to adjust risk-based capital standards for GSEs than what is currently provided in the law. Under questioning, Snow noted that the new regulator should have the authority to review and change the minimum and risk-based capital standards for Fannie and Freddie.

5. Treasury does not support requiring Fannie & Freddie to comply with the SEC Act of '33

Snow testified that the Administration's proposal does not include the issue of subjecting Fannie and Freddie to SEC requirements. Specifically the Administration opposes requiring the registration of Fannie and Freddie's securities under the Securities Act of 1933, because there is no evidence of fraud in the GSEs' issuance of securities and the large volume of securities issued by the GSEs would overwhelm the resources of the SEC.

6. Administration recommends elimination of Presidential appointments to Fannie & Freddie's boards

Snow testified that the Administration supports the elimination of the statutory requirement for the presidential appointment of Fannie and Freddie's board members. The President appoints five of the 18 board members on Fannie and Freddie's boards.

7. Administration testimony reaffirms that Treasury has authority to control GSEs' debt issuances.

8. Democrats concerned that moving the GSE regulator would compromise Fannie & Freddie's mission – did not see a crisis

House Financial Services Committee Ranking Member Barney Frank (D-MA) questioned the need for legislation. "I do not think we are facing any kind of crisis," he said. He believes that GSE critics have exaggerated a problem with the GSEs' safety and soundness, which has caused the companies to curtail efforts to expand affordable housing investments and activities (such as manufactured housing). He raised concerns about a new regulator within Treasury getting too much power that would reduce HUD's influence over the GSEs' affordable housing mission. (*Dow*

Jones Newswire, Dawn Kopecki and Rob Wells, 9/10/03) Cong. Frank also recommended holding more hearings on the issues.

Legislative Update

- Representative Richard Baker (R-LA), chairman of the GSE Oversight Subcommittee, and a veteran critic of the GSEs, sponsored H.R. 2575, which would shift the Office of Federal Housing Oversight from HUD supervision to Treasury's Office of Thrift Supervision...
- A companion measure, H.R. 2803, introduced by Congressman Ed Royce (R-CA), would move OFHEO and the Office of Thrift Supervision into the Office of Housing Finance Supervision, a new oversight agency in Treasury. Rep. Royce called his bill an alternative to legislation offered by Rep. Richard Baker and said he opposed combining the Office of Thrift Supervision with any new regulator of the GSEs. That position is shared by Rep. Barney Frank, the House Financial Services' ranking Democrat who opposes combining the OTS with OFHEO and was still deciding whether Fannie and Freddie should have a new regulator at all.
- Other legislation includes a bill introduced May 7 by Rep. Christopher Shays (R-CT) and Rep. Ed Markey (D-MA) requiring Freddie and Fannie to register their debt and mortgage-backed securities with the SEC. On May 15, Rep. Pete Stark (D-CA) introduced a repeal of Fannie and Freddie's state and local income tax exemption and on July 31, Senators Chuck Hagel (R-NE), John Sununu (R-NH) and Elizabeth Dole (R-NC) introduced a bill to establish a separate regulator for Fannie and Freddie under control of the Treasury, to be named the Office of Federal Enterprise Oversight. (*The American Banker*, 9/11/03)

National Association of Realtors Urges GSEs' mission remain under HUD

National Association of Home Builders says moving GSE oversight from HUD would undermine the housing finance system

Senator Shelby and Rep Oxley commit to legislate GSEs based on Snow principles

Financial Services moves quickly on Administration's GSEs proposals; hearing set for 9/18

Republican leadership urges greater disclosure requirements for Fannie/Freddie

National Association of Realtors urges GSEs' mission remain under HUD

- HUD should retain oversight over Fannie and Freddie's housing-related missions and programs while oversight of the companies' financial soundness should be transferred to the Treasury Department, the National Association of Realtors[®] urged Congress. In a letter to Chairman Mike Oxley (R-OH) of the House Financial Services Committee, NAR President Cathy Whatley said that GSE regulatory reform provides

an opportunity to reaffirm the companies' housing mission as well as their safety and soundness.

- "The administration proposal to place GSE regulatory oversight approval under the Treasury Department is a major departure from the perspective of the National Association of Realtors®. Housing policy has not been the purview or expertise of the Treasury Department; rather HUD has been central to housing issues, policy and programs. We expect that Congress will act judiciously to assure a critical role for HUD in GSE mission, program development and review. We look forward to reviewing the proposed legislation with an eye to assuring that housing not lose its prominence in the GSE safety and soundness reform debate," wrote Whatley, a partner in Buck & Buck, Inc. of Jacksonville, FL. (*NAR press release, 9/11/03*)

National Association of Home Builders says moving GSE oversight from HUD would undermine the housing finance system

- The Bush Administration's recommendation would "gut" HUD's role as the nation's primary housing advocate by removing the agency's current mission oversight of Fannie and Freddie, according to the NAHB. "This move threatens to jeopardize the success of the housing finance system and undermine the vibrant housing market that has sustained the economy in recent years," according to a NAHB press release.
- While the Treasury Department would be an appropriate agency for regulating the financial safety and soundness of Fannie and Freddie, Jerry Howard, executive vice president and CEO of NAHB, said it is imperative for HUD to retain its current status as the mission regulator for Fannie and Freddie, including approving new programs and establishing annual affordable housing goals.
- "We disagree with those who seek changes to the risk-based capital standards for Fannie and Freddie and are encouraged by statements of the House Financial Services Committee members who are urging their fellow lawmakers to proceed in a cautious, deliberative manner before enacting legislation that could radically alter the oversight and functioning of the housing finance system." The NAHB noted, "Stripping HUD of its program approval authority for Fannie Mae and Freddie Mac constitutes a devastating attack on the mission of HUD itself by removing the agency's ability to improve housing opportunities for America's working families. The proposal is an administration message that housing is not a national priority." (*NAHB press release, 9/10/03*)

Senator Shelby and Rep Oxley commit to legislate GSEs based on Snow principles

- House Financial Services Chairman Michael Oxley (R-OH) and Senate Banking Committee Chairman Richard Shelby (R-AL) jointly declared their intent to draft legislation based on the principles outlined before House Financial Services Committee by Treasury Secretary Snow and HUD Secretary Martinez on September 10th. Oxley commended the Snow/Martinez effort: "Two Cabinet Secretaries are committed to working closely with the President to achieve a world-class regulator for the housing government-sponsored enterprises." He described the joint effort as

one that would heighten regulatory oversight “that respects the critical importance of both the housing mission and the financial regulation of the markets.” Senator Shelby cited the opportunity to “produce strong, bipartisan legislation to improve the current regulatory regime.” Both members expressed commitment to conducting a bipartisan process in considering such legislation. (*U.S. Senate Banking Committee Press Release*, Chairman Richard C. Shelby, 9/10/03)

Financial Services moves quickly on Administration’s GSEs proposals; hearing set for 9/18

- The House Financial Services Committee is acting expeditiously to pass legislation creating the new GSE regulator, with a hearing scheduled for 10:00 a.m. on September 18th to focus on legislative proposals discussed by the Treasury Department at the September 10th hearing before the Committee and a bill introduced by Congressman Richard Baker (R-LA), chairman of the panel’s Capital Markets Subcommittee (H.R. 2575, the “Secondary Mortgage Market Enterprises Regulatory Improvement Act). Witnesses are expected to include representatives from OFHEO, FHFB, Fannie, Freddie, NAHB, Mortgage Bankers Association of America, Consumer Federation of America, Urban League, and Enterprise Institute.

Republican leadership urges greater disclosure requirements for Fannie/Freddie

- A GOP memo issued by the Senate Republican Policy Committee (RPC) on the eve of the Snow hearing before House Financial Services Committee, calls for tighter regulation of the twin mortgage finance companies “to insure against the failure of either or both (companies), however remote it may seem.” The RPC paper estimated the potential cost to taxpayers of such a failure in the hundreds of billions of dollars, and recommends that Congress begin to consider how to “create a greater separation between the taxpayers and the business operations of these firms without causing financial dislocation or upsetting the mortgage markets.”
- The scandal at Freddie Mac, explains the RPC paper, is “a direct product of a strategy, well underway at both firms, to leverage their ‘implicit guarantee’ to accumulate larger and larger investment portfolios and increase returns to shareholders.” An unexpected move in interest rates could create significant problems of the companies that could lead to insolvency, despite their extensive employment of derivatives to shield them from that risk.
- OFHEO’s current regulations are inadequate, according to the RPC, because they only require quarterly or monthly snapshots of the companies’ market value. A better disclosure system would show daily trading revenues as well as reports that disclose “the loss in portfolio value that would arise from random interest rate shocks at random probability levels.” The RPC paper concludes that the risks posed by Fannie and Freddie are a direct result of their federal links and that Congress should move to eliminate their implicit federal guarantee, adding that Congress should “strongly consider” passing a House bill requiring the two to register their debt and mortgage-backed securities “to increase investors’ information about MBS characteristics and

gain a better understanding of how Fannie and Freddie influence the market.” (*Dow Jones Newswires*, Dawn Kopecki, 9/9/03)

IMF semi-annual report cautions on adequacy of Fannie/Freddie capital

- The International Monetary Fund in its twice-yearly Global Financial Stability Report warned that Fannie and Freddie might not have enough capital to absorb shocks from fast-moving markets. The September 9 assessment urged regulator to look closely at whether the agencies’ “capital adequacy is sufficient, especially bearing in mind the questions about internal controls that have emerged in Freddie Mac.” Recent developments, the IMF argues, offer one more reason to ask whether the two GSEs’ capital – only 3.2 percent on a core capital-to asset basis at the end of 2002 – is enough. (*BNA*, Daily Report for Executives, No. 175, 9/10/03)

Bush nominee for head regulator of Fannie/Freddie backs combined reform of twin GSEs

Brickell volunteers details on previous business dealing with Fannie, Freddie

Bush nominee for head regulator of Fannie/Freddie backs combined reform of twin GSEs

- Mark Brickell, the Bush Administration’s nominee to replace Armando Falcon as head the Office of Federal Housing Enterprise Oversight, told lawmakers that the office’s sharing of oversight duties with another agency was unusual. Currently, OFHEO supervises the safety and soundness of Fannie and Freddie, but the Department of Housing and Urban Development is tasked with ensuring the companies’ adherence to their mission as GSEs and to their charters.
- Brickell, whose nomination is pending before the Senate Banking Committee, indicates he supports consolidation of oversight or an entity that oversees the financial soundness and the housing mission of the companies. Writing in response to a question from Senator Tom Carper (D-DE), Brickell elaborated, “I worked in a federally regulated banking institution for 25 years, and it is my understanding that other federal financial regulators generally gave responsibility for both mission and safety and soundness under one roof.” Brickell added that there might be “important reasons for bifurcating regulatory responsibility” of Fannie and Freddie, and that he had an “open mind” on the issue. He declined to say whether he supported any of the bills that would combine OFHEO with other agencies into a unit of the Treasury Department and that he had had no contact with Bush Administration officials while they were developing their recommendations.
- Democrats on the Banking Committee have questioned Brickell’s suitability for the post because of his past opposition to financial regulation, but Brickell, a former International Swaps and Derivatives Association chairman and 25-year veteran of J.P. Morgan and Co., told Senators he believes regulation can boost investor confidence: “I have worked in regulated financial institutions throughout my career and understand that effective regulation can bring greater assurance to investors.”

- A spokesman for Senator Paul Sarbanes (D-MD) said the Senator would oppose a vote on Brickell's nomination until he has seen all of Brickell's responses to lawmakers. (*American Banker*, Rob Blackwell, 9/4/03, *Bloomberg News*, Al Yoon, 9/4/03; *Reuters News*, Mark Felsenthal, 9/3/03)

Brickell volunteers details on previous business dealing with Fannie, Freddie

- Brickell helped advise Freddie about its derivatives activities as part of a J.P. Morgan banker's team in 1994. Brickell said he and two others advised Freddie on its "credit, market, legal and operational risk of its derivatives activities." While chief executive of Blackbird Holdings, the electronic derivatives exchange, Brickell and other executives sought Fannie and Freddie's business, but didn't land any contracts.
- Brickell said he does not believe he advised Freddie Mac about its derivatives trading positions, nor does he recall advising Fannie Mae on derivatives hedging when he was at J.P. Morgan. Brickell left the bank in 2001 to run Blackbird Holdings. (*Dow Jones Newswires*, Rob Wells, 9/4/03)

Surfeit of Republican names surface for Freddie CEO

Freddie hires prominent headhunter Korn/Ferry for CEO search

Washington Post says, "The Next Dramatic Exit at Freddie Mac should be Board Chairman O'Malley's"

Shaun O'Malley responds to Post financial reporter Jerry Knight

OFHEO Director Falcon retroactively fires former Freddie Mac's Brendsel and Clarke, moves to strip millions of dollars in severance pay

Surfeit of Republican names surface for Freddie CEO

- Among the names of possible Freddie CEOs are former Texas Senator Phil Gramm, Bush's ousted economic advisor Lawrence Lindsey, formerly a Federal Reserve governor and a Harvard University economist, and departing Treasury official Peter Fisher, who steps down October 10th and was the New York Federal Reserve's top liaison to financial markets. Senator Gramm enjoys credibility on Capitol Hill and would have built-in allies in the Administration, Treasury and the Fed, but he could also be seen as partisan, possibly complicating the GSE regulatory debate.
- Other names include Lewis Ranieri, a pioneer in the mortgage-backed securities market, founder of asset management company Hyperion Capital Management and chairman of American Financial Realty Trust. Ranieri is credited with helping develop the securitized mortgage market. Another senior industry official and possible candidate is Angelo Mozilo, chairman and chief executive of mortgage lender Countrywide Financial. Mozilo is a past president of the Mortgage Bankers Association and serves on the trade association's board of directors.

- Two other names that have floated are former Comptroller of the Currency Eugene Ludwig, but his Democrat affiliation could hinder his chances to be offered the job. Similarly, Jim Johnson, who preceded Franklin Raines as Fannie chairman, and is a former top advisor to Vice President Walter Mondale, is a long shot—the Bush Administration will not accept Johnson, according to one politically connected mortgage executive. The search is expected to be long and wide. (*The Wall Street Journal's Washington Wire*, Jackie Calmes, 8/29/03; *The American Banker*, Rob Blackwell, 8/26/03; *Reuters*, Mark Felsenthal, 8/27/03; and, *National Mortgage News*, Paul Muolo, 9/1/03)

Freddie hires prominent headhunter Korn/Ferry for CEO search

- Freddie Mac has selected a well-known search firm, Korn/Ferry International, to help recruit a chief executive, according to board chairman Shaun O'Malley. O'Malley said the search process would take at least three months. Freddie has replaced two chief executives in less than three months in the accounting scandal backlash. Freddie rattled the markets in June when it sacked its top three executives, including former chief executive Leland Brendsel, over accounting irregularities. A report to the company's board said Freddie officials flouted accounting rules to push a tide of earnings into future periods to promote an image of stability, called "steady Freddie." Freddie replaced Brendsel's successor, Greg Parseghian, last month under pressure from federal regulators who perceived Parseghian as too close to questionable corporate transactions used to manipulate earnings. (*Reuters*, 9/3/03)

Washington Post says "The Next Dramatic Exit at Freddie Mac should be Board Chairman O'Malley's"

- *Washington Post* financial reporter Jerry Knight contends that giving chief Freddie executive Parseghian his walking papers last month was an admission of an "incredible blunder," but believe the next step ought to be the sacking of board chairman Shaun F. O'Malley, "who bears the main responsibility for Freddie's bungled response to its \$4 billion accounting scandal." Freddie Mac, Knight writes, has done to itself almost as much harm as Martha Stewart did to herself: "O'Malley is the one who announced that Parseghian was fit to be chief executive even though he knew about the billions of dollars in dubious deals that Freddie cooked up to hide profits from its stockholders. And he seemed utterly untroubled by the fact that Parseghian cashed in \$17 million worth of his Freddie stock in 2001 just a short time after the company put out inaccurate financial reports – a stock sale that apparently no one at Freddie even questioned." Freddie officials, Knight argues, "simply do not understand that after scandals at Enron Corp., WorldCom, Inc. and their own company, zero tolerance is the rule."
- Freddie, according to Knight, is today: A giant corporation facing a federal criminal investigation and an SEC accounting investigation; A company whose shareholders still have to wait another month for accurate reports; A company that has yet to explain what it is doing to improve its corporate governance; A company without a permanent chief executive; A company with a chairman who had to be told by federal regulators that keeping on a chief executive who knew about earnings manipulations

was unacceptable; A company with a chairman who does not seem to recognize that his own chances of survival are as slim as Parseghian's.

- Freddie's credibility, he concludes, cannot be restored by a chairman who advocates protecting auditors who fail to do their jobs. (*The Washington Post*, Jerry Knight, 9/1/03)

Shaun O'Malley responds to Post financial reporter Jerry Knight

- Freddie Board chairman O'Malley argues that Knight's criticism of his agency overlooked may constructive things the board has done this year:
 - In January, directing the law firm Baker, Botts to conduct an independent review of accounting issues that would require Freddie Mac to restate prior financial results, which the board made public in July and is being used to fix problems leading to its restatement.
 - Action in June to remove the company's three senior executives;
 - Formation of a committee on financial management to provide oversight of the restatement process, which meets weekly with the board's corporate governance and audit committee;
 - Hiring of dozens of accounting professionals and a corporate controller, led by a new chief financial officer, the retired lead partner for PricewaterhouseCoopers' global banking practice;
 - Retention of the immediate past director of the U.S. Securities and Exchange Commission's Division of Corporation Finance to ensure that Freddie has world-class disclosures;
 - Reluctant agreement with a directive from Freddie's federal regulator to replace its CEO, Greg Parseghian because maintaining a sound relationship with the regulator serves the best interests of the company and its shareholders.
- O'Malley claims that Freddie is flourishing in the middle of "one of the most volatile interest-rate environments in years," and is winning back customers, "and its financial risk levels remain low." (*The Washington Post*, editorial by Shaun O'Malley, 9/12/03)

OFHEO Director Falcon retroactively fires former Freddie Mac's Brendsel and Clarke, moves to strip millions of dollars in severance pay

- Falcon explained his order to the Freddie Mac Board of Directors to retroactively terminate Freddie's former chief executive Leland Brendsel and former chief financial officer Vaughan Clarke: "Sound corporate governance require a clear principle for top management: If you engage in improper conduct, you will be terminated for cause. You will not be allowed to simply resign and walk away with large financial rewards." The move to strip Brendsel and Clarke of millions of dollars in severance payments is expected to be challenged in court. The formal process began September 4, with a "show cause" letter to Freddie Mac which directs the Board of Directors to provide a written response within ten working days."

- Freddie Mac should have sacked Leland Brendsel in June rather than permitting him to resign, according to OFHEO. Firing Brendsel would have resulted in the denial of as much as \$53.7 million in severance payments according to OFHEO officials. Similarly withheld benefits of Vaughn Clarke, according to the OFHEO, are approximately \$1 million.
- Freddie's regulator also said that Freddie's chief financial officer, Vaughn Clarke, should have been fired as well. Freddie Mac never volunteered details of Clark's severance package. Freddie Mac spokeswoman Sharon McHale declined to comment on the dispute, although Brendsel's lawyer issued a statement saying that "OFHEO should understand its own authority does not include interfering with valid contracts." Bert Ely, President of Ely and Co., a banking consulting firm in Alexandria, Virginia, said OFHEO is under fire for failing to recognize the improper trades and accounting earlier and may be trying to burnish its image as a regulator, especially since Congress is considering transferring GSE oversight to the U.S. Treasury. (*Bloomberg News*, Al Yoon, 9/4/03; *The Washington Post*, 9/8/03; OFHEO News Release, 9/4/03)

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| <p>The Federal Housing Finance Board adopts proposed rule on SEC registration</p> |
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- The FHFB adopted unanimously a proposed rule to enhance the financial disclosures of the FHLBanks through voluntary registration with the SEC under section 12(g) of the Securities Exchange Act of 1934. Chairman John Korsmo declared his objective to "ensure that the Federal Home Loan Banks play their part, as government-sponsored enterprises, in contributing to the smooth functioning of the capital and mortgage finance markets...Consistent and full disclosures of these institutions' finances and corporate governance also serve the public, who stand behind their charters as government sponsored enterprises." Korsmo expressed hope that each of the twelve banks would use the 120-day comment period to work with the SEC on the steps necessary to complete voluntary registration.
- Several of the banks and their member institutions have objected strongly to the move, which was prompted largely at the insistence of the Treasury Department, which reached agreement with Fannie Mae and Freddie Mac in 2002 to voluntarily register under the 1934 Act. The banks believe the disclosure regime is inappropriate for the FHLBanks in part because their stock is not publicly traded. A number of the FHLBank officials have cited the SEC's lack of expertise in the housing finance field and consider the FHFB itself a more appropriate entity to handle a new disclosure regime.
- Chairman Korsmo said that following discussions with the SEC, the Cincinnati FHLBank's board voted in August to register voluntarily. The boards of the San Francisco and Atlanta FHLBanks in recent weeks also agreed to register voluntarily under the act "if other disclosure regimes have been precluded." Korsmo expressed hope that "the board of the Federal Home Loans Banks follow Cincinnati's example and affirmatively elect voluntary registration with this regulation as a backstop." (FHFB Press Release, 9/10/03 and BNA/Daily Report for Executive 9/12/03)

Fannie and Freddie

Trade Associations appeal to Snow to strengthen Fannie/Freddie regulation

Rep. Richard Baker makes the case for stronger regulation of the GSEs

Trade Associations appeal to Snow to strengthen Fannie/Freddie regulation

- A joint trade letter was sent to Secretary Snow on the eve of his September 10th hearing before House Financial Services, to “encourage efforts currently underway to strengthen the regulation of Freddie Mac and Fannie Mae (the ‘GSEs’). We believe it is critically important to ensure effective supervision of these massive entities. Stronger regulation, buttressed by effective capital and meaningful disclosures, are essential to ensure that home ownership is enhanced, taxpayer’s interests are protected and the financial markets remain stable.”
- The group letter advised the Treasury Secretary that “Given the size and importance of the GSEs, proper GSE regulation and oversight is absolutely critical. Recent events have demonstrated the risks presented by inadequate regulatory measures, a deficiency the U.S. Government should move quickly to reverse.”
- The letter listed specific elements of any effective reform of the GSEs, essential to safeguard the interest of taxpayers and the financial system:
 - There should be a single, independent regulator of Fannie Mae and Freddie Mac within the Department of the Treasury, which has the financial expertise to ensure that GSEs are properly and effectively regulated. To be effective, the regulator needs the full panoply of regulatory and enforcement powers. The regulator should be housed in an independent agency within Treasury. To ensure independence, the regulator’s funding must be removed from the annual appropriations process.
 - The GSE regulator must have primary control over all key GSE activities that impact their safety and soundness, their chartered mission and their affordable housing responsibilities. The GSE regulator’s authority must include approval of new GSE programs. All of the bank regulators -- the Federal Reserve, the Office of the Comptroller of the Currency and the Office of Thrift Supervision – review consequential new programs without any adverse impact on the innovativeness of the nation’s banking system or its ability to serve homeownership. The GSE regulator must have similar authority.
 - The GSE regulator must be empowered to bring the capital requirements of both GSEs to levels equivalent to those of banks for comparable risk. Moreover, new capital requirements should be structured to ensure that the risk of the mortgage market is spread beyond the federal housing entities.

- Congress should establish a clear limit on the GSEs' business activities to a strictly secondary market role that prohibits encroachment into primary market activity. Congress should also direct the regulator to place a limit on the GSEs' non-mission portfolio assets and investments.
- Legislation should require the GSEs to make effective disclosure – including full, mandatory SEC registration – to ensure that investors and risk counter parties have all the information they need to make informed judgments that, in turn, supplement supervisory assessments.
- The letter was signed by the American Financial Services Association, the Association of Financial Guaranty Insurers, the Consumer Bankers Association, the Consumer Mortgage Coalition, the Financial Services Roundtable, Mortgage Insurance Companies of America, and the National Home Equity Mortgage Association (Joint Trade Letter, 9/10/03)

Rep. Richard Baker makes the case for stronger regulation of the GSEs

- Describing Richard Baker as a driven man and firebrand, *Money* magazine writer Ron Insana says Baker's mission is to ensure that Fannie Mae and Freddie Mac are not courting disaster. Baker, an amateur astronomer and minister's son, compared the possible havoc that would ensue from inadequate oversight of the two mortgage titans to an asteroid hitting the earth. The recent internal investigation of accounting at Freddie Mac proved Baker's concerns about the company well-founded, with allegations of weak internal controls and questionable accounting manipulations.
- Speaking about this year's hope for change, Baker said he would be shocked if a new regulator is not legislated into place by the end of the Congressional session. Asked why the accounting scandal hasn't resulted in calls for civil or criminal investigations, Baker said he judged that "shareholders and analysts are looking past the reports and directly to the U.S. Treasury because there still is, in their mind, very little credit risk with these companies, even if there was business impropriety or outright illegality." Baker added that there is concern that an inappropriate regulatory action taken could hurt one of the strongest legs of the economy, the real estate boom and if homes sales slowed, it would be a "very bad political thing to do." In response to a comment about his not being popular at the White House for his stance on Freddie and Fannie, Baker said most homeowners and taxpayers aren't aware of the issue; "It's a difficult policy question with only political downside." Baker believes, however, that it is the direct responsibility of Congress to protect the taxpayers. (*Money*, Ron Insana, September, 2003)

FM Policy Focus Chairman J.C. Watts lauds Administration's enhanced GSE regulatory proposal

CAGW, a taxpayer advocacy group, sees Snow testimony as mixed bag

Countrywide Finance chief exec urges Congress to avoid micromanaging GSEs

FM Policy Focus Chairman J.C. Watts lauds Administration's enhanced GSE regulatory proposal

- Responding to testimony by the Treasury and HUD Secretaries before Congress, FM Policy Focus Chairman and former House member J.C. Watts praised the Bush Administration's proposal as serious and comprehensive: "The proposal represents a strong step forward for American taxpayers, fair competition, the safety and soundness of the American housing finance system and the interests of American homebuyers, particularly of low and moderate income." (www.fmpolicyfocus.org, 9/10/03)

CAGW, a taxpayer advocacy group, sees Snow testimony as mixed bag

- The Council for Citizens Against Government Waste (CCAAG) reacted optimistically to Secretaries Snow's and Martinez's testimony before the House, but was disappointed in the Snow's lack of enthusiasm for another key element of reform, repeal of their exemption from the nation's securities disclosure laws.
- Calling Freddie's recently revealed accounting scandal a "wake-up call," CCAAG embraced the Secretaries' call for a stronger, savvier regulator and for an end to having presidentially appointed board members for Fannie and Freddie. Abolishing this practice prevents the boards of Fannie and Freddie from "being used as a dumping ground for political cronies." The organization stated that any reform bill must include the Shays-Markey provision repealing the GSEs' exemptions from disclosure laws, including the 1933 Securities Act. The group praised Secretary Snow for "dismissing the idea of imposing an arbitrary moratorium of any length on making changes to the capital requirements for the two enterprises. Fannie Mae and Freddie Mac are highly leveraged and are among the largest traders of derivatives in the world. It would be fiscally irresponsible for the administration to foreclose any of its options to require the GSEs to hold more cash in case of emergencies. The GSEs should be legally required to hold capital much the same way banks do."
- "All in all, Secretary Snow's testimony represented a significant step towards greater accountability" for the twin GSEs. (*Citizens Against Government Waste Press Release*, 9/11/03, www.cagw.org)

Countrywide Finance chief exec urges Congress to avoid micromanaging GSEs

- Angelo Mozilo, Financial chief executive of the nation's second-largest mortgage lender is asking Congress not to make legislative changes that would produce regulatory micromanagement of Fannie Mae and Freddie Mac, especially with regard to new product development. Writing to the chairs of the Congressional oversight committees of the GSEs, Mozilo cautioned: "An overly cumbersome regulatory process that micromanages business development and innovation will reduce, or even eliminate, the incentives for the GSEs and their primary market partners to pursue such efforts." Countrywide is one of the largest seller/servicers to Fannie Mae. (*National Mortgage News*, 9/8/03)

Wall St. Journal commends “Snow’s Good Deed”

Washington Post editorial urges Fannie and Freddie aren’t broken, but need fixing

Congressional Research Service (CRS) issues report on improving effectiveness of GSE oversight

GAO disputes OFHEO’s authority to remove Fannie/Freddie officials

Senate Appropriations approves \$2.6 million hike in OFHEO FY04 budget

Wall St. Journal commends “Snow’s Good Deed”

- A *Wall Street Journal* editorial praised Snow’s testimony as a “good first step” to rein in Fannie Mae and Freddie Mac, citing the Treasury Secretary’s testimony as a “sword pointed at the heart of Fan and Fred’s ever-growing portfolio of mortgage-backed securities. Between them, they have amassed about \$1.6 trillion in these instruments that, in turn, expose them to a wicked amount of interest-rate risk.” The Bush plan, the newspaper notes, “creates a regulator with the power to determine whether Fan and Fred are managing their portfolio risk adequately and have the ability to adjust their capital accordingly.” Snow also “pointed a sword at Fan and Fred’s immensely successful side business – political lobbying.” Franklin Raines, the editorial noted, “popped up in his usual way to take credit for most of these ideas,” and “urged that legislation be whisked to heavenly completion as soon as possible.” Raines, it speculates, may be trying to ward off more drastic action suggested by Senate Republicans, such as the removal of the GSEs’ implicit guarantee by the federal government, as discussed in a memo circulated by the Senate Republican Policy Committee. The memo warns of hundreds of billions of dollars in potential cost to taxpayers from a Fan or Fred failure and suggests ways to insulate taxpayers from a catastrophic bailout. “In a sign that the gravy times for Fan and Fred are changing,” the chair of the House Finance Committee, Michael Oxley (R-OH), “typically a sib darling,” promised to move swiftly to draft new legislation recommended by Secretary Snow...How nice then, if Mr. Snow’s good first step is not followed by the usual Congressional foot-dragging.” (*Wall Street Journal* editorial, 9/12/03)

Washington Post editorial urges Fannie and Freddie aren’t broken, but need fixing

- A *Washington Post* opinion article by Robert J. Samuelson says the GSE giants have grown so large “that if they ever experience serious financial problems, they will almost certainly have to be rescued by the government at immense cost.” The potential exposure, he notes, reflects their enormous debt: “At the end of 2002 Fannie’s and Freddie’s combined debt totaled \$1.5 trillion. This is equal to almost half the publicly held federal debt, \$3.7 billion.” While not suggesting that a bailout is imminent, Samuelson sees the danger as increasing with time, because Fannie and Freddie debt will expand by hundreds of billions.

- Samuelson credits the GSEs with advancing Congressional mandated goals of aiding the nation’s housing markets and increasing homeownership, but “paradoxically, Fannie and Freddie are no longer essential for strong housing finance.” Samuelson says if the twin GSEs vanished, mortgages would still be packaged and bought by investors just as they already buy riskier securitized credits – credit-card debt and auto loans, for example. Freddie’s latest crisis, with three executives being made to quit, he says, proves that “Big errors can go undetected by outsiders – including regulators – for long stretches.” Three thousand U.S. banks hold GSE debt equal to all their capital. Samuelson concludes that the Bush Administration will be tempted to protect the housing market and propose only modest changes in regulation, but he recommends a “blue-ribbon commission to ask how these giant enterprises should be refashioned to curb their size and special status. Unbroken they may be; but if they ever do break; the fix could cost a fortune.” (*The Washington Post*, editorial by Robert J. Samuelson, 9/3/03)

Congressional Research Service (CRS) issues report on improving effectiveness of GSE oversight

- CRS, Congress’ nonpartisan research arm, on September 8 issued a report, “*Improving the Effectiveness of GSE Oversight: Legislative Proposals*,” which provides background on the creation of the GSEs, the mission of the OFHEO, and the unique statutory benefits of the GSEs which have “enabled the enterprises to grow rapidly and gain an increasing share of the U.S. capital market.” With the recent announcement of Freddie Mac’s restatement of income, CRS notes, the adequacy of GSE regulation has become a prominent legislative issue once again. CRS points out the commonality in three bills (H.R. 2575 by Rep. Baker; H.R. 2803 by Rep. Royce; and S. 1508 by Sen. Hagel/Sununu/Dole) introduced in the 108th Congress to strengthen the current regulatory framework and improve the effectiveness of GSE supervision, and includes in its report a side-by-side comparison of these regulatory reform legislative initiatives. All three bills would:
 - Abolish OFHEO and reconstitute the GSE regulator within the Department of the Treasury;
 - Slightly increase the budget autonomy of the new office by exempting its assessments from the annual appropriations process and creating a permanent appropriation that can still be capped or limited at the direction of the appropriations committees; and
 - Enhance the safety and soundness and enforcement tools available to the new regulator. (*CRS Report for Congress/ “Improving the Effectiveness of GSE Oversight: Legislative Proposals,”* Loretta Nott and Mark Jickling, 9/8/03)

GAO disputes OFHEO’s authority to remove Fannie/Freddie officials

- A 2001 opinion letter written by the General Accounting Office states that OFHEO does not have the legal authority to remove officers and directors of Freddie Mac and Fannie Mae. The opinion contradicts OFHEO’s order to Freddie Mac’s board to remove chief executive Greg Parseghian. OFHEO Director Armando Falcon issued the removal order on August 22nd. Freddie’s board concurred with the order, but

instead of firing Parseghian, named him interim CEO, pledging to search for his permanent successor.

- The GAO opinion says OFHEO lacks the same direct removal and prohibition authorities applicable to officers and directors as the bank regulators and FHFBB. Later in the opinion, the GAO writes that “in connection with the issuance of a C&D (cease and desist) order,” OFHEO can “among other actions, direct the affected enterprise to hire a new employee to perform the job of the officer or director at issue.” However, there was no C&D issued against Freddie Mac. An OFHEO spokeswoman said the agency believes it does have authority to remove officers, citing the 1992 legislation creating the agency. The 1992 statute says OFHEO can require GSEs “to employ qualified officers or employees who may be subject to approval by the Director at the direction of the Director...and to require the enterprise to take such other action as the Director determines appropriate.” (*National Mortgage News*, 9/28/03)

Senate Appropriations approves \$2.6 million hike in OFHEO FY04 budget

- The Senate Appropriations Committee approved a \$2.6 million increase in the Office of Federal Housing Enterprise Oversight’s budget for FY04, but not without faulting the agency for failure “to identify recent accounting and management irregularities at Freddie Mac.” The Committee’s report on the VA-HUD Appropriations bill states that the members are concerned about the competency of OFHEO’s oversight of the two GSEs: “While it appears that Freddie Mac is in good financial shape, it is not clear whether OFHEO would have identified the financial irregularities if Freddie Mac had been in financial risk.” (*National Mortgage News*, 9/8/03)

Freddie gains market share in July against Fannie

Fannie repurchasing up to \$5 billion of debt; Freddie selling \$3 billion of 2-yr floating-rate notes

Merrill Lynch raises Fannie/Freddie to a “buy” from “neutral” in wake of scandal

Columbia, SC law firm named a designated counsel by both Fannie/Freddie

Freddie gains market share in July against Fannie

- Despite its recent battering in the press, Freddie made headway in regaining market share lost in previous months to Fannie. After its share of the mortgage market dropped 3 percent in June to 34.5 percent, Freddie gained ground in July, with its market share of business volume increasing to 35.7 percent. It’s historic average has been 40-50 percent, according to Fox-Pitt, Kelton, Inc., an investment bank and subsidiary of Swiss Reinsurance Co. Given the current management turmoil, prospects of Freddie’s market share recovering to historic averages is doubtful, analysts speculate. Freddie’s loss in market share first made headlines in May, when its monthly report showed it had lost about 8 percent of market share in April; that

loss was followed by a 6 percent gain in May. (*Dow Jones Newswires*, Julie Haviv, 8/8/03)

Fannie repurchasing up to \$5 billion of debt; Freddie selling \$3 billion of 2-yr floating-rate notes

- Most U.S. agencies outperformed Treasuries after Fannie Mae said it would repurchase up to \$5 billion of its debt, relieving some pressure the market is feeling from the \$10 billion in new agency issuance now in motion. Freddie is selling \$3 billion of two-year global floating-rate notes on Thursday, the Federal Home Loan Banks will sell \$3 billion of three-year notes this week and Freddie Mac will sell \$4 billion of five-year reference notes next Wednesday. (*Reuters News*, Lynn Adler, 9/3/03)

Merrill Lynch raises Fannie/Freddie to a “buy” from “neutral” in wake of scandal

- Merrill Lynch analyst Michael Hughes says the “worst may be over” for the government-chartered mortgage giants, rocked with criticism from a report released in July by Freddie Mac raising suspect accounting practices. The controversy dragged down shares of fellow mortgage services company, Fannie Mae and led to a clamor for increased GSE regulation.
- Hughes said he was encouraged by the stocks’ upward movement despite the negative news that Freddie’s Greg Parseghian will be forced to resign from the company. Hughes pointed out, “This type of trading is usually consistent with bottoms in stocks,” and that most of the bad news has been priced into the stock.
- Freddie is expected to announce in September re-audited earnings results for 2001, 2002, and possibly 2003. (*The Wall Street Journal*, Roger Cheng, 9/2/03; *Bloomberg News*, Al Yoon, 9/2/03)

Columbia, SC law firm named a designated counsel by both Fannie/Freddie

- Rogers Townsend & Thomas PC of Columbia, South Carolina, has announced it is the only law firm in the state to be named a designated counsel by both Fannie Mae and Freddie Mac. The firm said it has been selected to represent both GSEs in foreclosure and related proceedings. The selection was made from numerous law firms contending to be one of two designated counsels in the state for each GSE. The firm completed a comprehensive application based on strict criteria and responded to an extensive interview process. Rogers Townsend & Thomas PC specializes in default services, real estate and litigation. (*National Mortgage News*, 9/2/03 and PRNewswire, 9/2/03)

Fannie Mae

Raines decries SEC registration of MBS for Fannie

New Fannie loan requirements could price manufactured home buyers out of the market

Raines decries SEC registration of MBS for Fannie

- Franklin Raines, Fannie Mae's chief executive said requiring registration of mortgage-backed securities guaranteed by Fannie with the Securities and Exchange Commission could hurt the U.S. mortgage market. Addressing a Lehman Brothers conference on the financial services industry, Raines said, SEC registration "would have a material impact on the mortgage market – that would take away an efficient (hedging) tool for mortgage lenders." Currently, mortgage backed securities guaranteed by Fannie and Freddie are exempt from registration with the SEC, per the two companies' Congressional charters. Under SEC rules, securities cannot be sold and traded until prospectuses are offered and may take up to three months before they could be sold and traded, according to Raines. This time lag from SEC requirements, the Fannie chief contends, could lead to severe disruption of the U.S. mortgage market. (*Reuters*, 9/11/03)

New Fannie loan requirements could price manufactured home buyers out of the market

- In response to a rising number of delinquencies and foreclosures, Fannie is making it tougher to get manufactured home loans. The company now requires a 10% down payment for 30-year mortgages on such homes, plus a fee of 0.5% of the loan amount. In the past, those who qualified could put zero funds down, while others put down more than 3%, with no fee required. For those who cannot afford 10%, Fannie introduced a 20-year loan requiring a 5% down payment, but monthly payments are higher. Critics say the changes could price some would-be homeowners, especially low-income families, out of the market and hurt some dealers in manufactured homes, already hurt by the glut of recently built, repossessed, manufactured homes. HUD says mobile or manufactured homes, with an average sale price of \$49,000, account for one-third of all new single-family home sales, with some 7.2 million such homes, many in rural areas and the South. (*Associated Press*, Genaro C. Armas, 9/12/03)

Ellen Lazar appointed to Fannie Foundation as Sr. VP for Housing/Community Initiatives

- Fannie Mae announced the appointment of Ellen Lazar, previously with Neighborhood Reinvestment Corporation as executive director, as Senior Vice President for Housing and Community Initiatives. Lazar begins work with the Fannie Mae Foundation on October 14th. The Foundation's President and CEO, Stacey Stewart, said, "We are very fortunate to have an accomplished and committed leader like Ellen Lazar join our team," commending her "extensive and impressive background in housing and community development." Lazar's will be responsible for the Foundation's grant-making efforts nationally, including five regional offices in Dallas, Philadelphia, Pasadena, Atlanta and Chicago. Prior to joining NRC, Lazar served as Director of the Community Development Financial Institutions Fund in the

Treasury Department, and as Executive Director of the National Association of Affordable Housing Lenders and Vice President and General Counsel of the Enterprise Foundation. (*PR Newswire*, 9/12/03)

New York State Realtors combines with Fannie on “Borrow with Confidence”

Baltimore City, Fannie, and Cento de la Comunidad sponsor bilingual workshop

Fannie launches Los Angeles project to boost home buying for Spanish speakers

Fannie infuses \$35 billion into Bay Area, doubling earmarks from four years ago

Colorado’s Smart Commute Initiative boosted by Fannie

PMI Mortgage Insurance Co., Fannie and First Mortgage Co. launch fund for Oglala Sioux

Fannie and Tennessee realtors kick off “Borrow with Confidence”

New York State Realtors combines with Fannie on “Borrow with Confidence”

- U.S. Representative John Sweeney (R-NY) joined with representatives from The New York State Association of Realtors (NYSAR), local REALTOR, associations, participating lenders and Fannie Mae, to announce the Borrow with Confidence campaign and the Housing New York’s Workforce course to assist realtors in helping home buyers get the best mortgage financing for which they qualify and expanding homeownership opportunities. Housing New York’s Workforce is a three-hour, continuing education course focusing on the changing demographics and the impact of the role of the REALTOR, and the benefits of Fannie Mae’s suite of affordable mortgage products through Fannie Mae-approved lenders. Congressman Sweeney propounded the benefits of the effort, “When working families throughout New York State are faced with the high cost of housing, it’s important for them to know they can secure low-cost loans for their largest expense...The Borrow with Confidence campaign and the Housing New York’s Workers course will go a long way in helping more families make informed decisions about the affordability of homeownership.” (*Fannie Mae News Release*, 9/12/03)

Baltimore City, Fannie, and Cento de la Comunidad sponsor bilingual workshop

- The City of Baltimore, Maryland, Fannie Mae and the Latino organization, Centro de la Comunidad, will sponsor a bilingual workshop on home buying next weekend for Hispanic buyers in the Baltimore area. To capitalize on the expanding base of minority homeowners and potential customers, several lenders have joined with Freddie Mac and Fannie Mae to tailor programs for various ethnic groups. The Baltimore seminar was 9:30 a.m. to noon on September 7 at St. Patrick’s Hall, 1728 Bank Street. (*The Baltimore Sun*, 8/31/03)

Fannie launches Los Angeles project to boost home buying for Spanish speakers

- Fannie has developed a three-year program with Charo Community Development Group and Nationwide Advantage Mortgage Co. to provide free homebuyer education in Spanish and at least \$20 million in affordable mortgage financing. The latest effort to increase homeownership among Latinos in Los Angeles, “Home Expo en Espanol” is a pilot project that could assist about one hundred Spanish-speaking homebuyers. Minorities and immigrants are expected to comprise more than 60% of first-time homebuyers nationally during the next decade. Charo plans to host six home buying expos with members of the Congressional Hispanic Caucus throughout the L.A. area to provide home buying education in the Spanish language. (*The Los Angeles Times*, 8/31/03)

Fannie infuses \$35 billion into Bay Area, doubling earmarks from four years ago

- Fannie Mae announced an additional \$35 billion into affordable housing in the Bay Area, “to fill the affordability” gap because of higher costs of housing, more than double the amount earmarked for such initiatives four years ago. Fannie also extended the project’s reach beyond the nine Bay Area counties to include Monterey, San Benito and Santa Cruz counties. With the new funding, Fannie will offer low-interest loans to developers of affordable housing projects, buy municipal bonds for redevelopment of existing rental units and – in a relatively new approach, work with public housing authorities in the Bay Area to help low-income families purchase home using Section 8 rental assistance vouchers. Fannie recently completed a similar \$16 billion program that it says served more than 135,000 Bay Area residents. With the new program, Fannie plans to help some 200,000 residents buy homes or rent apartments over the next five years. The *San Francisco Chronicle* points out, however, that “as home prices continue to rise, it is unclear whether such programs will do much to improve affordability.” According to Fannie Mae’s director of the Bay Area Partnership Office, Santa Cruz recently passed San Francisco as one of the least affordable counties in the nation.” (*San Francisco Chronicle*, Kelly Zito, 8/26/03)

Colorado’s Smart Commute Initiative boosted by Fannie

- Representative Diana DeGette (D-CO), Tony Hernandez, Director of Fannie Mae’s Colorado Partnership Office, along with Regional Transportation District General Manager Cal Marsella, and Jay Wilson, state manager of National City Mortgage, released details of Fannie’s new Smart Commute Initiative in the Denver area. Colorado is the 13th state to launch the program, which Fannie started in July 2003, designed to promote homeownership near public transit. Buyers within a half-mile of light rail or a quarter mile of a bus stop typically will be able to qualify for a mortgage 6-8% larger than they would otherwise, Fannie Mae’s Hernandez explained. The Smart Commute program is now open to homebuyers in Adams, Arapahoe, Boulder, Broomfield, Denver and Jefferson Counties. Although there is no guarantee that a person living near public transport will use it, Hernandez noted that lenders that make the loans will see how much borrowers are spending on car payments: “If you have loans on three cars, you’re not going to be riding the bus or light rail, and you won’t qualify for a loan under this program.” (*Rocky Mountain News*, John Rebchook, 8/26/03)

PMI Mortgage Insurance Co., Fannie and First Mortgage Co. launch fund for Oglala Sioux

- PMI Mortgage Insurance Co., First Mortgage Co. and Fannie Mae announced the launch of Gateway Initiative specifically for the use of the Oglala Sioux Tribe, during a wall-raising ceremony on the Ogalala Sioux Tribe Partnership for Housing construction yard. This initiative will provide a revolving fund in the amount of \$175,000 that the tribe will draw upon to build new homes or purchase and rehabilitate existing homes on the Pine Ridge Reservation. As each housing unit is finished, the fund will be reimbursed from proceeds of sale, providing an opportunity for the Oglala Sioux to start a new project and work with the next designated family to make its dream of affordable homeownership a reality.
- PMI Chairman and CEO Roger Haughton described the venture as “important to PMI because it is an affirmation of our basic corporate mission to expand homeownership opportunities. It is also a demonstration that the private sector is able to meet the needs of underserved segments and do so in a sound business-like fashion.” Senator Tim Johnson (D-SD) was the guest speaker for the event. (*Business Wire*, 9/2/03)

Fannie and Tennessee realtors kick off “Borrow with Confidence”

- The Knoxville Area Association of Realtors and the Tennessee Association of Realtors (TAR) have teamed with Fannie Mae to initiate “Borrow with Confidence,” a multi-faceted campaign aiming to help area homebuyers to get the best mortgage financing they qualify for and to promote responsible lending. Fannie said BWC was launched here in conjunction with the National Association of Realtors following success of the first BWC campaign introduced in Texas earlier this year.
- According to Fannie, BWC will try “to debunk many of the myths that surround the home buying process,” ensure that realtors are committed to offering competitive rates and know about available low-cost flexible mortgage loans. Using TAR and Fannie resources, the BWC campaign will provide realtors with mandatory continuing education training on various affordable mortgage products that assist borrowers whose barriers to homeownership may consist of lack of down payment funds, blemished credit and excessive debt. (*National Mortgage News*, 9/1/03)

Freddie Mac

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| Freddie boss urges no double jeopardy for new oversight board |
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- Freddie Mac’s Chairman Shaun O’Malley warned the new U.S. accounting oversight board to avoid applying a form of “double jeopardy” on auditors who also might face discipline from the Securities and Exchange Commission. In July, the oversight board proposed rules to allow it to investigate and sanction accountants who commit fraud or violate the board’s regulations.

- O'Malley, former chairman of PricewaterhouseCoopers LLP, who became Freddie's chairman in June, wrote the Public Company Accounting Oversight Board on August 14 to say that while he generally agreed with the proposed rules, the board should coordinate with other regulators so auditors are not subjected to multiple layers of punishment, recommending the oversight board and the SEC coordinate their disciplinary actions.
- O'Malley headed a task force that sought more regulation of the accounting industry in 2000. O'Malley's position has been criticized by others who believe his letter sends the wrong message when the oversight board is setting up an enforcement division to examine accounting failures like the one at Freddie Mac, which may have understated earnings by as much as \$4.5 billion. (*Bloomberg*, 8/27/03)

Freddie Mac Duration Gap in July at +1 Month vs. June at zero

Moody's claims Freddie Mac's solid Mid-Mgmt supports ratings

Fitch ratings downgrades Freddie Mac

Freddie contemplates ratings mandate for subprime ABS transactions

Freddie Mac Duration Gap in July at +1 Month vs. June at Zero

- Freddie Mac announced that its average duration gap for July widened to positive one month from zero in June. The duration gap measures how well cash flows from Freddie's assets and liabilities match up in its portfolio. A positive duration gap suggests cash flows from its assets will outpace the stream of payments it owes debt holders. The duration gap first came to markets' attention a year ago, when Fannie Mae reported a record negative 14-month crack in its mortgage portfolio.
- In its monthly summary assessment, Freddie noted its total mortgage portfolio decreased at an annualized rate of 14.5% in July, while its retained portfolio increased at an annualized rate of 18.1%. Freddie's retained commitments decreased to \$44 billion from \$63.5 billion. The company's total PC portfolio decreased at an annualized rate of 19.5% in July. Structured securitizations were \$30.6 billion in July, up from \$23.5 billion in June. The single-family noncredit enhanced delinquency rate was 28 basis points, unchanged from June. (*Dow Jones Newswires*, Julie Haviv, 8/26/03)

Moody's claims Freddie Mac's solid Mid-Mgmt supports ratings

- Moody's Investor Service says it is comforted by the current middle-level management running the day-to-day business of Freddie Mac and by the mortgage agency's government sponsorship. Moody's reiterated its double-A-2 rating on Freddie's subordinated debt despite the removal of Freddie CEO Greg Parseghian by regulators after only three months on the job. Moody's rating for Freddie's subordinated debt is one notch above that of the other two major rating agencies, Standard & Poor's Corp. and Fitch Ratings. All three ratings agencies have a triple-A

rating for Freddie Mac's senior debt, reflective of its GSE status. (*Dow Jones Newswires*, 8/26/03)

Fitch ratings downgrades Freddie Mac

- In response to recent leadership problems, Fitch downgraded its ratings on Freddie Mac's subordinated debt and preferred stock to double-A-minus from double-A. The ratings changes do not impact Freddie's more important AAA senior debt rating, which allows the GSE to borrow money cheaply. Freddie uses this kind of debt for most of its financing and has \$720 billion in outstanding senior debt. Fitch said that Freddie has depth in accounting and risk management, but the latest management transition introduces more risk and warned ratings could be cut further. Fitch's managing director in financial institutions, Eileen Fahey, warned that Fitch has been in discussions with Freddie since the beginning of the accounting announcement and the GSE has been "...more challenged than we originally expected." (*Wall Street Journal Abstracts*, 8/26/03, *The Financial Times*, 8/26/03 and *Reuters*, 8/25/03)

Freddie contemplates ratings mandate for subprime ABS transactions

- Freddie is considering requiring that each of the three major rating agencies rate a subprime asset-backed transaction before it will participate in the deal. Byron Boston, Vice President of mortgage portfolio management, says he is concerned that competition among rating agencies to get their names on asset-backed deals can be fierce, allowing bankers to shop for the highest possible ratings for a deal and opening the door to a relaxation of standards. These factors could hurt investors, particularly in the subprime market where accurate reflection of risks to the underlying collateral is even more important. Boston said Freddie was "kicking around" the potential requirement and does not have imminent plans to impose it. He said the levels of disclosure in new subprime deals often revolve around the ratings agencies, and by making their participation contingent on a third rating, investors would be able to expose more transparency on the underlying collateral. Currently, Freddie requires that two agencies sign off on a subprime ABS transaction before participating. Boston says he hopes to spark discussion in the investor community about whether rating agencies are properly serving investors, and adds Freddie is thinking about the issue because volumes in mortgage-related sectors have reached new highs and he expects the subprime market to experience a hiccup at some point because it is on the "fringe of consumer lending." (*Bond Week*, Scott Goodwin, 7/30/03)

Despite turmoil, Freddie acquires record \$80 billion in mortgages during month of July

- Despite a record \$80 billion mortgage acquisition in July, Freddie's purchase commitments, a barometer of future activity, fell to \$44 billion in July, a 20% decline from the previous month and Freddie's lowest reading since April.
- When Freddie fired three officers in June, some seller-servicers used the opportunity to slam the company for past business practices, especially a g-fee floor of 16 basis points that it established in late 2001. Some seller-servicers hope the company might provide "guarantee fee" discounts to entice mortgage bankers away from Fannie Mae.

Freddie Mac's board has been concerned that it has lost market share to Fannie.

- The liquidation rate on Freddie's portfolio hit a stunning 87.5% during the month of August, but is expected to slow as interest rates climb. Smith Barney analyst Matt Vetto notes, "We expect liquidation rates to fall in the coming months, which should mitigate the pressure on the company's MBS portfolio growth." Smith Barney adds that once the company finally restates earnings, it may have a new estimated book value of \$31 to \$36 per share. Late last week, the stock traded at about \$50 a share. (*National Mortgage News*, 9/1/03)

MBS prepayments bite into Freddie's portfolio

Freddie prevails in Tax Court ruling on \$146.5 million in taxes assessed by IRS

Freddie postpones 3.5 billion Euro-denominated note sale

Freddie changes strategy for marketing floating-rate bond issues

Freddie Mac's board of directors announces quarterly dividend of \$0.26 per share

MBS prepayments bite into Freddie's portfolio

- Freddie Mac's mortgage portfolio, which includes the securities it guarantees and other investments, shrank last month at an annual rate of 14.5% to \$1.29 trillion, because of rapid prepayments of mortgage-backed bonds. Its investment portfolio, however, which does not include securities it guarantees that are held by others, grew at an annual rate of 18.1%, to \$595.2 billion, according to the GSE. A record \$44.3 billion of purchases retained by the mortgage finance giant for the portfolio more than offset the liquidations in its holdings. (*American Banker*, Jody Shen, 8/27/03)

Freddie prevails in Tax Court ruling on \$146.5 million in taxes assessed by IRS

- Freddie Mac prevailed in a decision in federal tax court that may help it avoid \$146.5 million in taxes assessed by the U.S. Internal Revenue Service. Judge Robert P. Ruwe ruled that the IRS applied the wrong standard for valuing intangible assets owned by Freddie, after it switched from a government entity to a private, taxpaying company in 1985. "Congress provided a special adjusted basis for purposes of determining any gain" on Freddie Mac property held on January 1, 1985, wrote Judge Ruwe, who determined Freddie should have been permitted to use a favorable tax basis for its intangible assets. The ruling on the case, filed in 1999, is good news for Freddie, since back in January it restated earnings for the previous three years because of accounting errors mounting to as much as \$4.5 billion. The intangible assets that are subject of the ruling did not include information leases, debts and Freddie's list of mortgage sellers. The court did not determine whether Freddie is permitted to amortize the intangible assets or, the amount of any deductions Freddie may be entitled to – those are issues still to be litigated, according to Ruwe. (*Bloomberg News*, Bob Van Voris, 9/8/03)

Freddie postpones 3.5 billion Euro-denominated note sale

- Freddie Mac postponed a 3.5 billion euro-denominated note issue as it prepares to restate earnings for the past three years. The issue scheduled for the week of September 22 will be rescheduled at some future date, according to the company in a press release. (Bloomberg News, Al Yoon, 9/5/03)

Freddie changes strategy for marketing floating-rate bond issues

- Louise M. Herrie, its treasurer and a vice president, announced that Freddie is changing its strategy for marketing floating-rate bond issues. Formerly, the GSE would wait for investors to show interest in this type of debt to Wall Street dealers, which would then advise Freddie to go ahead with a bond offering of a specific size and maturity. Ms. Herrie said that from now on Freddie will initiate the process, working with dealers to identify opportunities. Under the old set-up, Freddie felt it was out of touch with investor sentiment, Herrie pointed out: “We were not presenting ourselves to the market in a controlled fashion, because we were not involved in the dialogue.”
- This new strategy will help Freddie better analyze how much supply the market can absorb so it can “right-size” bond issues. Its floating-rate offerings will likely come less frequently but will be bigger and more liquid, according to Herrie.
- Freddie announced plans to sell this week at least \$3 billion of two-year floating-rate debt pegged to the three-month London Interbank offered rate. For the rest of this year, it plans to issue up to \$15 billion. Freddie’s cost to service the debt issued this week would increase if rates continue to rise. Herrie said demand for floating-rate bonds has surged recently, making it the right time to sell them, and noted: “We’re hearing from investors that they’re more interested in defensive products.” (*The American Banker*, 9/4/03)

Freddie Mac’s board of directors announces quarterly dividend of \$0.26 per share

- Freddie’s board of directors announced a quarterly dividend of \$0.26 per share on the corporation’s voting common stock.
- The board also declared the following preferred stock dividends per share: \$0.22 on its 1996 and 1998 variable-rate stock; \$0.7675 on its 6.14% stock; \$0.72625 on its 1997, 2001, and 2002 5.81% stock; \$0.625 on its 5% stock; \$0.6375 on its 1998 and 1999 5.1% stock; \$0.6625 on its 5.3% stock; \$0.72375 on its 5.79% stock; \$0.74625 on its 1999 variable-rate stock; \$0.2075 on its January 2001 variable-rate stock; \$0.14567 on its March 2001 variable-rate stock; \$0.1975 on its May 2001 variable-rate stock; \$0.75 on its 6% stock; and \$0.7125 on its 5.7% stock. The dividends will be payable on September 30 to stockholders of record as of September 15. (www.freddiemac.com)

What if Freddie's stock comes back? – Majority of Analysts rate it as “strong” buy

- The company is being sued in the wake of the accounting scandal by shareholders angry about their holdings being hammered earlier this year (52 week low of \$46; high of \$64) and the ouster of three top officers. The share price of the company is now around \$54. Paper losses could be transferred into profits if it restates past earnings upwards of \$4.5 billion and its stock jumps? Roughly 19 equities analysts follow Freddie's stock. Four rate it a “strong buy,” six a “buy,” and nine a “hold.” Twenty-two analysts cover Fannie. Eight analysts rate it a “strong” buy, eight a “buy,” and six a “hold.” (*National Mortgage News*, Paul Muolo, 9/6-7/03)

Treasury says it played no role in Parseghian's ouster

- U.S. Treasury General Counsel David Aufhauser denied Treasury was involved in the OFHEO's decision last week to call for the firing of Freddie Mac chief executive Greg Parseghian. Aufhauser, Treasury's top lawyer, told reporters asking if Treasury took part in the decision, “The answer to that is a no... That's an OFHEO jurisdiction, an OFHEO decision, an OFHEO action.” (*Dow Jones Newswires*, Rebecca Christie, 8/25/03)

MGIC/Freddie to insure mortgages under Mississippi Home Corp's Get on Track

Freddie Mac links up with the Cuban American National Council

City of Riverside joins with Freddie to help community police and firefighters

MGIC/Freddie to insure mortgages under Mississippi Home Corp's Get on Track

- Mortgage Guaranty Insurance Corporation (MGIC) announced it will insure mortgages under the Mississippi Home Corporation's Get on Track (GOT) program, a statewide program enabling people with impaired credit to move into an affordable home and get their finances in order during a lease period before becoming a homeowner. GOT was introduced a year ago when Governor Ronnie Musgrove announced that the state had made \$25 million available to fund mortgages under the lease-to-own initiative. Freddie has agreed to buy the mortgages. Effective immediately, MGIC will insure GOT mortgages and waive a premium adjustment typically applied when the mortgagor is not a property's occupant. The waiver of the so-called “investor loan” pricing adjustment will result in an annual reduction of GOT mortgage costs by \$140 per \$100,000 of debt. GOT is the first program of its type to be offered statewide. Lease-to-own initiatives typically are offered by city or county housing authorities in a small geographic area, but interest in lease-to-own is rising as housing officials nationwide look for ways to help people avoid turning to high-cost lenders and entering costly mortgages that may ultimately exacerbate their credit problems. (*PR Newswire*, 8/18/03).

Freddie Mac links up with the Cuban American National Council

- Freddie Mac has teamed with a Miami nonprofit, the Cuban American National Council, to offer free classes in Miami on financial issues related to homeownership and higher education. The classes are part of Freddie's CreditSmart Espanol

program, which it started rolling out last December, and will all address consumer credit and money management issues. (*American Banker*, 9/2/03)

City of Riverside joins with Freddie to help community police and firefighters

- Freddie Mac, the City of Riverside and Provident Bank Mortgage announced a zero-down payment mortgage to help Riverside's police, firefighters, and other safety officials own a home in the community they protect. The goal of the program, the Riverside Neighborhood Safety Initiative, is to help public safety personnel buy homes in the Riverside area, one of the nation's fastest growing areas, through Freddie's Affordable Gold 100 mortgage, developed by Freddie Mac and the California Housing Agency (CalHFA). Riverside public service employees annually earn an average of \$38,350, about half the income needed to afford a median-priced Riverside home of \$222,340. Under the new initiative, no borrower cash is required for down payment or closing costs. For borrowers with impaired credit, Provident Bank Mortgage is also making available Freddie's Flexible Community Gold® mortgages, which enables borrowers to buy a home with as little as \$500 of the minimum three percent down payment coming from their own funds. Freddie plans to purchase, and CalHFA will insure, up to \$5 million of eligible mortgages originated by Provident Bank Mortgage, ensuring a continuous supply of mortgage funds for additional homebuyers. (*PR Newswire*, 8/26/03)

Federal Home Loan Banks

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| Senate Banking Committee holds Federal Home Loan Bank Oversight Hearing |
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- The Senate Banking Committee's Financial Institutions Subcommittee held a September 9 hearing on oversight of the FHLBank System. Financial Institutions Subcommittee Chairman Robert Bennett (R-UT) chaired the hearing. The following individuals testified:

Panel 1

Treasury Assistant Secretary for Financial Institutions Wayne Abernathy
FHFB Chairman John Korsmo

Panel 2

Norman Rice, President and CEO of the FHLBank of Seattle
Terry Smith, President, FHLBank of Dallas
David Hemingway, EVP, Zions First National Bank of Salt Lake City, UT
Mike Middleton, President and CEO, Community Bank of Tri-County
Sheila Bair, Dean's Professor of Financial Regulatory Policy, Isenberg School of Management – University of Massachusetts

- Senator Bennett felt it was Congress' duty to hold periodic reviews of the oversight of the FHLBank System. This was the first hearing since the passage of the Gramm-Leach-Bliley Act in 1999 that expanded the powers of the FHLBanks. He thought

that Freddie's current accounting troubles were a "hiccup" for the GSEs in general. Senator Bennett said he was holding the hearing as part of Congress' oversight duty and was not any indication of problems at the FHLBanks. Since Gramm-Leach-Bliley, Senator Bennett's main concerns with the FHLBanks are: (1) whether the FHLBanks should voluntarily register with the SEC under the Securities Exchange Act of 1934; (2) whether the FHFBS has the authority to approve FHLBank multi-district membership (allowing a bank or thrift to belong to more than one FHLBank); (3) what level of participation in the secondary mortgage market is appropriate for the FHLBanks (i.e., FHLBanks' mortgage purchase programs and potential securitization); and (4) whether a single housing GSE regulator for Fannie, Freddie, and the FHLBanks is appropriate.

- The Senators repeatedly asked Abernathy and Korsmo to comment on whether the FHLBanks should be included in proposals to create a single independent regulator for Fannie and Freddie under Treasury. They declined to comment until Treasury Secretary John Snow testifies on the issue September 10 in the House Financial Services Committee.

Highlights of the hearing:

1. FHFBS expected to re-issue proposed rule on FHLBanks' mortgage purchase programs

The FHLBank System currently has two mortgage purchase programs (the Mortgage Partnership Finance Program (MPF) and Mortgage Purchase Program (MPP) that compete with Fannie and Freddie in the secondary mortgage market. The FHFBS unanimously adopted and published for public comment a proposed revision to the FHLBanks' mortgage purchase programs that FHFBS Chairman Korsmo noted would clarify and simplify the current rule but has been misunderstood as expanding or altering the fundamental structure of the programs. Korsmo will ask the FHFBS to withdraw the proposed revision at its September 10 meeting and revise and clarify the proposed regulation. If approved by the FHFBS at a subsequent meeting, the revised proposed regulation will be published for a 90-day comment period.

2. Treasury questions the FHFBS's legal authority to approve FHLBank multi-district membership

Treasury Assistant Secretary Abernathy testified that Treasury believes a plain reading of the law leaves little room to conclude that the FHFBS has the legal authority to approve FHLBank multi-district membership. There are compelling arguments on both sides of the issue, however, it is up to Congress to consider these arguments and consider where any changes in the statute will need to be made. Treasury believes that "if multi-district membership is considered, it should be considered within the context of evaluating the Federal Home Loan Bank System's charter."

3. FHFBS has no plans to move forward on FHLBank multi-district membership

FHFB Chairman Korsmo said he is neither an advocate nor an opponent of multi-district membership. In his opinion, however, the FHLBank Act both empowers and obligates the FHFB to continue regulating the terms of FHLBank membership. There is currently disagreement among the FHLBanks as well on the issue and the FHFB has no plans to move forward on FHLBank multi-district membership.

4. Treasury conducting an overall study of the FHLBanks

Treasury is currently conducting an overall study of the FHLBank System to consider the effect of the changes enacted as part of the Gramm-Leach-Bliley Act. Treasury is close to completing the first phase of the study.

5. Treasury raises concerns about allowing privately insured credit unions to join the FHLBank System

Abernathy raised concerns about a legislative proposal regarding the membership of privately insured credit unions to join the FHLBank System (contained in a regulatory relief bill). Under the proposal private insurers of credit union deposits would among other things be required to submit annual audit reports to the National Credit Union Administration (NCUA). “We are concerned that the provisions related to the NCUA could give the false impression that the NCUA has oversight authority over the private deposit insurers of credit unions and that the Federal government somehow stands behind the private insurers.”

6. Treasury encourages FHLBanks to register with the SEC

Treasury continues to urge the FHLBanks and all GSEs to voluntarily comply with the Securities Exchange Act of 1934. The Treasury Department is pleased that Fannie has complied with the request and is disappointed that Freddie may not register until sometime in 2004. The differences between the FHLBanks and other GSEs should be taken into account, however, the differences do not change the fact that the FHLBanks are significant participants in the capital markets and investors should have the same information regarding the FHLBanks as they do other significant capital market participants.

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| Treasury has no qualms on “shared funding” according to Treasury Assistant Secretary Abernathy |
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- The Treasury Department’s Assistant Secretary, Wayne Abernathy, relayed to the Senate Banking Subcommittee on Financial Institutions that the FHLBanks are cooperatives whose members are served by innovative programs, such as “shared funding transactions” in which FHLBank members securitize mortgages and sell the high-rated securities to an FHLBank, which can turn around and sell them to other members. Abernathy said these innovative programs “provide an important source of liquidity to member banks.” He did caution that the Treasury would have a problem

with the shared funding program if the FHLBanks sold the securities to other parties outside the FHLBank system. In March, three FHLBanks purchased the first shared funding transaction, a \$475 million security. (*National Mortgage News*, 9/20/03)

Korsmo reverses stand on multidistrict proposal

- Federal Housing Finance Board Chairman John Korsmo flipped his position on a promise to propose broad rules laying out how financial institutions may join more than one of the dozen FHLBanks. Korsmo before a Senate Banking subcommittee hearing said, “No action by the Finance Board in this area is planned...No broad rule is forthcoming, and Home Loan Banks must re-file requests to accept members from other banks’ district.” FHLBank officials indicate they are unlikely to re-file the requests, mainly because the system has so many other pressing problems. Assistant Treasury Secretary for Financial Institutions, Wayne Abernathy, made it clear in his testimony that the Department does not believe the Finance Board has the power to permit multi-district memberships, forcing Korsmo’s hand. Four Home Loan banks are leading the campaign for multi-district membership. Currently, a financial institution may belong to only one of the 12 Home Loan banks. Abernathy said that a “plain reading” of the law “finds little room to conclude that the Finance Board has the legal authority” to approve any such arrangement. Abernathy said the Congress would have to decide any change in the statute and that there are compelling arguments on both sides of the question with regard to the advisability of multi-district membership.
- Senator Paul Sarbanes (D-MD) agreed with Abernathy that the board cannot act without a statutory change from Congress. The Senator also released a GAO study at the hearing which was generally critical of the Finance Board, saying it needs to collect more and better data to assess the 12 banks’ health and that this weakness “could limit FHF’s ability to monitor current and emerging trends within the system.” (*The American Banker*, Rob Blackwell, 9/10/03)

FHFB FY04 budget increases spending on safety and soundness oversight

- The Federal Housing Finance Board unanimously adopted a FY2004 budget of \$31 million, marking a \$4 million increase over the current year budget, permitting a substantial strengthening of the FHFB’s ability to oversee the FHLBanks for safety and soundness, according to Finance Board chair John Korsmo: “Combined with the rigorous approach the agency takes toward Bank examinations, these increased resources will enable the Finance Board to do the job that Congress created it to do – ensure that the 12 Federal Home Loan Banks are operating in a safe and sound fashion.”
- The new budget contains a \$4.3 million increase dedicated to the FHFB’s supervisory capacity, including additional staff, and acquisition of more powerful financial risk models and expanded programming support. Excluding the Office of the Board of

Directors, fully 80% of the Finance Board's FY04 staff and resources will support the Office of Supervision, a 10% increase over the current year.

- The FY04 budget anticipates eight additional bank examiners, increasing the FHFB's total examination staff to 34 by the end of the next fiscal year. It also anticipates added accountants, mortgage specialists and bank analysts to support the examination and supervision of the 12 Federal Home Loan Banks. (*Federal Housing Finance Board Press Release*, 9/11/03 or <http://www.fhfb.gov/pressroom/press/PR03-34.htm>)

Farmer Mac

Farm Credit Administration Board holds Closed Session Meeting

- The Farm Credit Administration Board met on August 14, 2003 in a Closed Session to review, among other issues, the Baker-Botts Review of Freddie Mac and Related Issues. (*Federal Register*, Vol. 68, No. 155, 8/12/03)
- Although, the Farm Credit System and its regulator, the Farm Credit Administration, or FCA, have kept a lower profile than Fannie Mae, Freddie Mac, and the FHLB system, the U.S. Treasury has included the Farm Credit System in its calls for better GSE disclosure. "In July 2002, Peter Fisher, the Treasury's undersecretary for domestic finance, wrote Reyna asking for an agreement on SEC registration for Farm Credit System members." The FCA indicated that it is reviewing its disclosure policies, but has no immediate plans to change them. (*Wall Street Journal*, Rebecca Christie, 9/4/03)
- The Farm Credit System, America's oldest GSE, has launched an effort to be able to lend to anyone, for any purpose, anywhere. This expansion of its powers, to be accomplished by regulatory fiat, would violate congressional intent and raises serious questions about the ability of the system's regulator, the Farm Credit Administration, to rein it in. "Eventually, Congress should fully privatize the Farm Credit System, since every square mile of rural America is amply served by private-sector lenders. In the meantime, while Congress is restructuring GSE regulation, the FCA should put the "farm" back in the Farm Credit System." (*American Banker*, Bert Ely, 9/5/03)

Ginnie Mae

Ginnie Mae to Start Guaranteeing Hybrid ARM Pools

- Ginnie Mae has announced that it will guarantee pools of Federal Housing Administration and Department of Veterans Affairs hybrid adjustable-rate mortgages starting October 1. "Ginnie Mae will guarantee pools of FHA 3, 5, 7 and 10-year hybrid ARMs and VA 3-year and 5-year hybrid ARMS," according to a Ginnie Mae memorandum. Hybrid ARM products will be eligible for securitization as multiple

issuer loan packages under the Ginnie Mae II mortgage-backed securities program. It is unlikely the FHA will be ready to insure hybrid ARMs anytime soon since it is still drafting final regulations for the new loan product. VA officials maintain they are almost ready to launch their program: “We are confident we will be guaranteeing hybrid ARMs on October 1,” a VA official remarked. (*National Mortgage News*, 8/28/03)

Postal Service

Senate oversight Committee cancels postal reform hearing

USPS to hold public briefing on proposed merger of two major data reporting systems

Lawmakers mull postal reform

Senate oversight Committee cancels postal reform hearing

- The Senate Governmental Affairs Committee canceled its scheduled hearing for September 3, “U.S. Postal Service: What Can be Done to Ensure Its Future Viability?” The hearing was intended to discuss postal reform and changes to the U.S. Postal Service proposed by the Presidential Reform Commission. Witnesses were to be James A. Johnson and Harry Pearce, co-chairs of the commission, pursuant to the Commission’s report from July recommending sweeping changes including increased automation, fewer employees, changes to the collective bargaining system and increased authority to shutter unprofitable post offices. (The Senate Governmental Affairs Committee subsequently rescheduled the hearing on postal reform for Wednesday, September 17, at 10:00 a.m. in Dirksen 342.)
- The hearing postponement, due to the illness of one witness, sparked some concern that other pressing issues before Congress could push postal reform off the legislative agenda. As Neal Denton, executive director of the Alliance of Nonprofit Mailers, explained, “Those interested in postal reform are fighting the clock for this session.”
- Jack Estes, executive director for the Main Street Coalition for Postal Fairness, was assured the hearing would be held in about 10 days, but shared the concern that Congress may push the possibility of a reform bill into next year. The House Government Reform Committee’s special panel on postal reform, which includes House members John McHugh (R-NY) and Danny Davis (R-IL), is expected to meet and discuss the presidential commission’s recommendations in about three weeks. Both McHugh and Davis have been active in postal reform legislation. (*DMNews*, Scott Hovanyetz, 9/3/03 and 9/4/03 and www.nonprofitmailers.org/news.html, 9/12/03)

USPS to hold public briefing on proposed merger of two major data reporting systems

- The USPS will present a briefing, which will be open to the public, on September 17 at 2:00 p.m. in the Postal Rate Commission's hearing room on the proposed merger of two major data reporting systems. The systems affected by the merger are the Revenue, Pieces and Weight (RPW) system and the Origin Destination Information System (ODIS). (www.nonprofitmailers.org/news.html, 9/12/03)

Lawmakers mull postal reform

- Congressman John McHugh (R-NY), who has sponsored Postal Service modernization in the past, predicted the complexities of postal reform will keep legislation from becoming law this year. McHugh described the undertaking as an "uphill climb," adding that he and Henry Waxman (D-CA), the ranking Democrat on the Government Reform Committee, have been working for eight years on overhauling the nation's postal system. McHugh said he is looking anew at all the issues in the wake of the Presidential Commission's report of July 31, and vowed, "At this point, I would not rule out anything the commission has put forward." Senator Tom Carper (D-DE) introduced a Senate version, S. 1285, in June that is similar to McHugh's past legislation. (*Congressional Quarterly Today*, 9/4/03)

Postal Service shrinks operation hours in cost-cutting attempt

USPS ends year with surplus

Unions blast Bush postal panel plans; mailers question labor's role in reform

Postal Service shrinks operation hours in cost-cutting attempt

- Amidst a growing slump in first-class deliveries, the U.S. Postal Service has begun reducing its hours of operations at some post offices. About half of the post offices in the State of Maine have scaled back operations in the past few months, with similar move underway in other parts of New England, such as Vermont and upstate New York. Postal Service managers nation-wide are evaluating the merit of additional cutbacks. The Postal Service said the reduction in hours of service is being made based on the time of day when fewer customers buy stamps or mail packages and that customers are being informed in advance of the changes. The moves are part of Postmaster General John Potter's belt-tightening efforts to reduce costs without eroding the quality of service. Potter's efforts in the Postal Service's top job for more than two years has resulted in a cut of six percent, or almost 47,000 full-time jobs, eliminated through attrition. (*Dow Jones Newswire*, 9/2/03)

USPS ends year with surplus

- The embattled U.S. Postal Service expects to finish this fiscal year with a \$4.2 billion surplus, its first since 1999, according to its chief financial officer, Richard Strasser. Although the Postal Service's revenue this year was \$1.5 billion lower than expected, at \$68.9 billion, its expenses were \$1.8 billion less than predicted. The agency plans to reduce its debt from \$11.1 billion to \$7.3 billion and hopes to shrink it further thanks to a predicted net income of \$2.1 billion in Fiscal year 2004, which begins October 1. Volume fell from a high of 208 billion pieces in 2000 to 202 billion in

200. The slowdown is attributed both to email and other online services, as well as the anthrax attacks, which cut volume and cost billions in cleanup costs. Strasser warned that the Postal Service needs modernizing: “The adjustment in retirement payments gives us breathing room, but in the long term, the operational and business model needs to be reviewed.” (*The Washington Post*, Tania Branigan, 9/10/03)

Unions blast Bush postal panel plans; mailers question labor’s role in reform

- The nation’s postal unions criticized the Administration’s panel’s reform recommendations, which they believe will weaken or destroy collective bargaining rights for the nation’s 500,000 some U.S. Postal Service employees. Letter Carriers President William H. Young said the Bush panel’s counsel “would render Letter Carriers and other postal employees second-class citizens.” Postal Workers President William Burrus agreed, vowing his union would lobby hard against the Bush panel’s proposals. The unions plan to lobby against the proposal, coupled with the AFL-CIO whose Executive Council voted in early August to join the postal worker unions’ effort. (*Workday Minnesota*, 9/1/03)
- Mailing industry groups embraced the President’s Commission’s findings, but remain uncertain as to whether organized labor will be willing to further postal reform. The reaction of the National Rural Letter Carriers Association was more moderate than other labor groups, with NRLCA spokesman Ken Parmelee responding: “We believe that, in general, the recommendations could improve labor/management relations, notably by encouraging more negotiated settlements.” Neal Denton, executive director of the Alliance of Nonprofit Mailers, supported the Commission’s recommendations, but said the \$10,000 question is whether the President will support its findings. (*Direct*, Larry Riggs, 9/1/03)

Cornell professor and author argues to think outside the mailbox to save the mail system

Association for Postal Commerce head advocates for postal service to keep costs down, embrace information technology

Heritage Foundation calls for Postal Service compliance with SEC requirements

Cornell professor and author argues to think outside the mailbox to save the mail system

- Rick Geddes, an assistant professor in Cornell University’s Department of Policy Analysis and Management, notes that the postal service has sizeable cracks in its foundation. According to Geddes, the decline in the USPS’ first-class mail volume – a core revenue source -- is the largest drop in 30 years. Individual letters sent are plummeting, largely because of e-mail. Accordingly, the Postal Service’s liabilities are skyrocketing, says Geddes, with its debts and unfunded obligations now totaling around \$90 billion, causing the GAO to place the Postal Service on its list of “high-risk” institutions because of its fiscal problems and raising the specter of a taxpayer bail-out.

- Geddes also acknowledges the Postal Service’s unusual attributes which may impede reform, among them, it is not subject to antitrust law, has legal monopolies over letter mail delivery as well as the use of your mailbox, but competes with the private sector in some services; it is government-owned, therefore paying no taxes. It can borrow from the Treasury, has its own police force and doesn’t pay parking tickets, and its regulator can’t control it.
- With the last major post reform accomplished back in 1970, communications technology has brought in vast economic changes. The Postal Service’s recommendations, to preserve mail service to all addresses (universal service), retain monopoly powers at least in the near-term, stick to its core role, enhance financial transparency through compliance with the Securities and Exchange Commission’s disclosure requirements, and strengthening the Postal Service’s regulators, should serve as the basis for legislative action. Geddes points out the most important recommendation in the report- the authority for the regulatory board to revisit the Postal Service’s monopoly power “when the evidence shows that suppression of competition is not necessary to the protection of universal service without undue risk to the taxpayer.” Some countries, notes Geddes, with remote areas already have eliminated their postal monopolies and universal service has continued, and universal service is a valued business asset to any delivery company, so companies have an incentive to provide it. Finally, statistical studies of the U.S. market show that rural routes are profitable, so firms in a competitive environment would have an incentive to cover those routes. (*Newsday*, Rick Geddes, 9/3/03) (The American Enterprise Institute published Rick Geddes’ “The President’s Commission on the Postal Service, An Assessment,” as part of its Postal Reform Papers on 9/1/03; available online)

Association for Postal Commerce head advocates for postal service to keep costs down, embrace information technology

- Gene A. Del Polito, President of the Association for Postal Commerce in Arlington, Virginia, points out the \$2 billion a year available for the balance of the decade, to the USPS from its civil service retirement system payment reform, should use every dollar it can to hold postal rates steady for as long as possible. While others would like to see USPS use the extra revenue to pay some of its liability for postal retiree health care or building and renovating postal facilities, not spending it on staving off rate increases will mean a return to the round of rates hikes that have lessened mail’s value in business communications. A secondary use would be to dedicate this money to development and implementation of a comprehensive postal information technology infrastructure. United Parcel Service, Del Polito notes, has spent billions over the years putting into place electronic tools to allow them to know where every driver, truck and parcel is at any given time. These innovations enabled UPS to beat competitors. (*Direct*, 9/1/03)

Heritage Foundation calls for Postal Service compliance with SEC requirements

- The Heritage Foundation’s Backgrounder, “USPS (Non)Disclosure: Time to Bring in the SEC,” points out that the U.S. Postal Service accounts for 0.75 percent of the U.S.

gross domestic product and is the second largest civilian employer. Due to increasing use of e-mail and other electronic options, USPS mail volume is declining, leading to financial trouble for the Postal Service. Heritage's Backgrounder raises the comprehensive GAO report from November 2000, which found significant problems in the Postal Service's financial reporting, and urges that the USPS be required to comply with SEC reporting requirements as a useful near-term step.

- The think tank draws an analogy between the USPS and accounting scandals in the corporate world, from Enron and WorldCom to Tyco International and Global Crossing, which resulted in swift enactment of the Sarbanes-Oxley Act to toughen accounting regulations and require – among other things, that firms' chief executives personally vouch for the firm's financial statements. These regulations, Heritage notes, only applied to the private sector and publicly traded firms. Firms that are owned by the government may be even more susceptible to accounting woes, given the lack of stockholders to keep management honest. Ultimately, the report asserts, reform will require substantial structural changes, including privatization and elimination of the Postal Service's monopoly on letter mail. (*Heritage Foundation Backgrounder*, No. 1685, Douglas K. Adie and James L. Gattuso, 9/4/03)

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| Postal Service Board of Governors meets |
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- Under the requirements of the Sunshine Act, the Postal Service Board of Governors published a notice of its meeting on Monday, September 8, at 11:00 a.m. and Tuesday, September 9, at 8:30 a.m. at U.S. Postal Service Headquarters. The first meeting is closed and the second meeting is open. In the closed meeting on September 8, the Governors deliberated upon the Office of Inspector General FY02 budget, heard a financial update and a FY04 Integrated Financial Plan. (*Federal Register*, Vol. 68, No. 168, 9/29/03; and, (www.nonprofitmailers.org/news.html, 9/12/03)

Canfield & Associates, Inc.
801 Pennsylvania Ave., NW, Suite 625
Washington, DC 20004
Phone: (202) 661-2100
Fax: (202) 661-2101
www.canfieldassoc.com