

# The **GSE** REPORT™

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## Major Events

Treasury says Congress could consider the powers and resources of OFHEO and the FHFB to see if changes could improve oversight over the GSEs

Treasury says the Administration's position on the GSEs has not changed since last year

Congressman Richard Baker (R-LA) thanks Treasury for its comments and plans to hold hearings on the GSEs later this year

- Treasury Undersecretary Peter Fisher advised Congressman Richard Baker (R-LA) in a May 23 letter that “Congress could usefully consider the powers and resources of both the Office of Federal Housing Enterprise Oversight and the Federal Housing Finance Board and/or whether structural changes might improve the effectiveness of our oversight and regulation of the government-sponsored enterprises and other financial institutions.” Fisher said his July 2002 testimony summarizes the administration’s position with regard to Fannie and Freddie. “The most complete statement of this Administration’s objectives and priorities regarding government-sponsored enterprises remains the testimony that I presented to your Subcommittee on July 16, 2002 together with my subsequent colloquy with you and other members of the Subcommittee,” wrote Fisher. (*Reuters*, 5/23/03; *Treasury Undersecretary Peter Fisher’s letter to Congressman Richard Baker*, 5/23/03)
- In last year’s testimony, Fisher said the Treasury Department did not support a bill (HR 4071) by Congressmen Chris Shays (R-CT) and Ed Markey (D-MA) that would have repealed Fannie and Freddie’s exemption from SEC requirements and required the GSEs to register their debt and mortgage-backed securities (MBS) with the SEC. The Treasury Department did not support the bill, Fisher said, because it did not apply to all GSEs and they were not ready to support the repeal of Fannie and Freddie’s exemption from registering their debt and MBS with the SEC. Fisher said that Treasury was pleased with the voluntary financial disclosure agreement reached between Fannie, Freddie, the SEC, OFHEO, and Treasury, in which Fannie and Freddie agreed to voluntarily register their common stock with the SEC, while retaining their exemption from registering their debt and MBS with the SEC. The Treasury Department called on all GSEs to comply with the same voluntary financial disclosure rules agreed to by Fannie and Freddie. Fisher also testified that the Treasury Department had no position on removing the GSEs’ line of credit to Treasury and supported removing OFHEO from the appropriations process. [See July 19, 2002 *GSE Report* for more details on Fisher’s testimony, [www.gsereport.com](http://www.gsereport.com)]
- Fisher’s most recent letter was in response to an April 11 letter Congressman Baker sent to the Treasury Department, asking whether comments made by Fisher’s predecessor Gary Gensler at a March 22, 2000 Capital Markets Subcommittee hearing remained the official position of the Treasury Department on the housing GSEs. Congressman Baker asked Fisher whether there had been any changes in GSE governance policy and to explain the reasons for such modifications. Gensler testified in 2000 that the Treasury Department supported

removing the GSEs' line of credit with the US Treasury and recommended limiting the amount of GSE debt that commercial banks can hold. Gensler also noted that the US government does not guarantee Fannie and Freddie's debt. Congressman Baker's April 11 letter to Under Secretary for Domestic Finance Peter Fisher can be found at: [www.baker.house.gov/News/fisher\\_letter.htm](http://www.baker.house.gov/News/fisher_letter.htm). (Congressman Baker press release, 4/15/03) [See April 7, 2000 *GSE Report* for more information on Gensler's testimony, [www.gsereport.com](http://www.gsereport.com)]

- In his most recent letter to Congressman Baker, Fisher did not address Gensler's comments directly. (*Reuters*, 5/23/03)

Congressman Baker thanks Treasury for its comments and plans to hold hearings on the GSEs later this year

- Congressman Baker released a statement thanking the Treasury Department for its "helpful comments," which Congressman Baker characterized as "an agreement to consider structural changes in the regulation of the housing GSEs." (*Statement by Congressman Richard Baker*, 5/23/03) Treasury Department spokeswoman Betsy Holahan, however, said Fisher's letter was not an indication of support for a particular course of action. "He's not hinting at anything. He's stating that Congress, if it chooses, it could consider these issues," Holahan said. "We're not hinting that legislation is needed or that structural changes are needed. It's up to Congress to decide whether that might be appropriate." (*Dow Jones Newswire*, Dawn Kopecki, 5/27/03)
- Introducing new legislation is not on Congressman Baker's immediate agenda, Congressman Baker's spokesman Michael DiResto said. "What he plans to do right now is further the discussions, but we don't have any detailed proposal on the table," said DiResto. "I think Congressman Baker is gratified that there is public acknowledgment that there needs to be consideration of regulatory restructuring. What this will look like, he's open to suggestions." DiResto said Congressman Baker is planning to hold hearings later this year on Fannie's controversial new program, called PaymentPower™ as well as Fannie tax-exempt status in the District of Columbia. (*Dow Jones Newswire*, Dawn Kopecki, 5/27/03) [More information on Fannie's controversial PaymentPower™ program and a bill introduced by Congressman Pete Stark (D-CA) that removes Fannie and Freddie's state and local tax exemption is available in this *GSE Report*.]

<p>CBO Report says requiring Fannie &amp; Freddie to register their debt and MBS with the SEC won't harm the mortgage market as Fannie &amp; Freddie have claimed</p>
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- The Congressional Budget Office (CBO) released a May 2003 report on the effects of repealing Fannie and Freddie's SEC exemptions. The study was prepared at the request of Congressman Chris Shays (R-CT) and Congressman Edward Markey (D-MA), who re-introduced a bill removing Fannie and Freddie's SEC exemptions. The report concluded that requiring Fannie and Freddie to register their debt and mortgage-backed securities (MBS) would not disrupt the efficiency of the mortgage markets, as the companies have claimed. A

copy of the report can be found online at: <ftp://ftp.cbo.gov/41xx/doc4199/05-06-03-GSEs.pdf>

Fannie & Freddie have voluntarily complied with some of the provisions in Shays-Markey bill

- The CBO report analyzed the Shays/Markey bill (HR 4071), introduced in the 107<sup>th</sup> Congress, that would subject Fannie and Freddie to the same legal requirements that apply to other publicly traded companies and to other issuers of private MBS. The report noted that following the introduction of the Shays/Markey bill, Fannie and Freddie took steps to comply voluntarily with some of the requirements that would result from enactment. For example, last July, Fannie and Freddie agreed to voluntarily register their common stock and file quarterly and annual reports with the SEC (in compliance with the Securities Exchange Act of 1934), while remaining exempt from registering their debt and MBS with the SEC under the 1933 Securities Act. Fannie and Freddie argued that registering their debt and MBS could delay the mortgage process and make it more difficult for consumers to lock in their loans. As a result of recommendations made in a January 2003 report by the Treasury, OFHEO, and SEC, Fannie and Freddie also pledged to voluntarily disclose more information on their MBS pools including: loan-to-value ratios; borrowers' credit scores; the identities of the servicers of the loans; borrowers' use of properties; and the purpose of the loan. (*CBO report: Effects of Repealing Fannie Mae's and Freddie Mac's SEC Exemptions*, May 2003)

CBO says registering their debt and MBS would have little effect on market

- The CBO noted that Fannie and Freddie "have not elected to register their debt or MBS issues voluntarily." CBO noted, "Voluntary disclosure is not equivalent to mandatory requirements to which the GSEs would be subject under the Shays-Markey bill. That legislation would make the GSEs' debt and MBS subject to enforced disclosure requirements and fees and would reduce the enterprises' future discretion." Under the Shays-Markey bill, Fannie and Freddie would be required to pay registration fees and to disclose information about their securities (common and preferred stock, debt and MBSs). According to CBO, "[r]egistering those securities is expected to have little effect on the prices of the GSEs' stock because the enterprises were already disclosing detailed information on their overall financial condition and performance." The current market "would probably function in much the same way with registration" as it does now, the CBO said. Requiring Fannie and Freddie to register their securities could result in some increased costs for consumers, but probably wouldn't prevent consumers from locking in mortgage rates prior to closing. The report said that debt registration would not result in huge administrative fees for Fannie and Freddie because registration can be done electronically. If fees were passed on to consumers, the closing cost of a \$200,000 mortgage would probably rise by less than \$25, the report said. (*Wall Street Journal*, Dawn Kopecki and Patrick Barta, 5/7/03; *CBO report: Effects of Repealing Fannie Mae's and Freddie Mac's SEC Exemptions*, May 2003))

Congressmen Chris Shays (R-CT) and Ed Markey (D-MA) re-introduce their bill to remove Fannie & Freddie's SEC exemption

“CBO study shows the dire consequences Fannie and Freddie keep predicting won't happen,” says Congressman Shays

CCAGW and NTU support Shays-Markey bill

- Congressmen Shays and Markey introduced May 7 the “Leave No Securities Behind Act” (HR 2022), which will hold Fannie and Freddie to the same federal securities registration and disclosure requirements as all other publicly traded companies. The bill is similar to the bill (HR 4071) that the Congressmen introduced in the 107<sup>th</sup> Congress. (*Congressmen Shays/Markey press release, 5/7/03*)
- “Coming on the heels of the Treasury Department’s MBS report [finding that Fannie and Freddie disclose less information than private-label issuers and that additional disclosures would not disrupt the market], the CBO study shows the dire consequences Fannie and Freddie keep predicting won't happen,” said Congressman Shays. “Requiring these companies to register their securities will have no adverse effects and will only serve to benefit investors in the MBS market.” (*Congressmen Shays/Markey press release, 5/7/03*)
- On the continued need for legislation, Congressman Shays stated, “Every publicly-traded company has to register its securities with the SEC, and Fannie and Freddie shouldn't be treated any differently. Fannie and Freddie keep announcing new and improved disclosure practices, but they're still not on par with every other publicly-traded company. They're literally picking and choosing which federal laws they comply with.” (*Congressmen Shays/Markey press release, 5/7/03*)
- “No public company should be granted a general exemption from the registration and public reporting requirements of the federal securities laws, and all this bill does is ensure that Fannie Mae and Freddie Mac are subject to the same investor protection requirements as every other company in America...CBO has confirmed what I've believed for some time: that taking this step will not harm the markets and may well make them more efficient and transparent.” said Congressman Markey. (*Congressmen Shays/Markey press release, 5/7/03*)

#### Bill is slightly different than last year's version

- The “Leave No Securities Behind Act,” repeals Fannie and Freddie's exemptions from the Securities Act of 1933 and the Securities Exchange Act of 1934. It requires Fannie and Freddie to register their equity, MBS and debt with the SEC. The legislation differs from the version Congressmen Shays and Markey introduced in the 107<sup>th</sup> Congress - HR 4071, the Uniform Securities Disclosure Act – in three ways. First, the bill grants the SEC authority to ensure the continued smooth operation of the To Be Announced (TBA) market. Second, the bill clarifies that, in certain circumstances, approved sellers of pooled certificates would not

be considered underwriters. Finally, the bill caps the amount of fees the SEC can collect from any single company to five percent of the total fees collected for a given year. (*Congressmen Shays/Markey press release, 5/7/03*)

- Although HR 4071 did not become law, it was widely credited with stimulating debate on the issue that ultimately led to an agreement reached last July by the SEC, OFHEO and Treasury in which Fannie and Freddie agreed to voluntarily register their common stock and file quarterly and annual reports with the SEC (in compliance with the Securities Exchange Act of 1934), while remaining exempt from registering their debt and MBS with the SEC under the 1933 Securities Act. Fannie filed for the first time its Form 10 registration statement and initial Form 10-K annual report with the SEC in March 2003, providing its audited financial statements for 2002. Freddie has yet to file registration statements with the SEC. It plans to do so in June when it is finished restating earnings from previous years.

#### CCAGW endorses Shays/Markey bill

- The Council for Citizens Against Government Waste (CCAGW) [the lobbying arm of Citizens Against Government Waste] announced that it has endorsed the Shays-Markey bill. “CCAGW is delighted that Reps. Chris Shays and Ed Markey have introduced this very sensible bill. Taxpayers and investors need transparency and accountability and this bill will provide both with regard to the GSEs,” said CCAGW Special Projects Director Leslie K. Paige. “The GSEs mortgage-backed securities (MBS) portfolio has increased 437 percent, from \$171 billion in 1990 to \$918 billion in MBS in 2001. If Fannie Mae or Freddie Mac experiences an unforeseen financial shock, there is every indication that the taxpayers would be called upon to bail them out. It would be unconscionable for Congress to allow their transactions to fly beneath the radar of the SEC or any other oversight agency until some crisis occurs.”
- CCAGW noted that Fannie and Freddie, under pressure from lawmakers and regulators last year, agreed to increased disclosure for the common stock but not their MBS portfolio. The GSEs claimed that mandatory SEC registration and disclosure would negatively impact consumers, obstruct the GSEs' ability to issue debt quickly, and disrupt capital markets. However, CCAGW noted that those arguments have now been rejected by several official sources. A joint report in January, 2003 by the Treasury Department, the Office of Federal Housing Enterprise Oversight and the SEC found that enhanced disclosure in the MBS market would be feasible and justifiable, as well as improve market stability, safety and soundness. In March, Federal Reserve Chairman Alan Greenspan told Congress that changes in the GSEs' oversight procedures would do them no harm. The new Congressional Budget Office study confirmed that mandatory SEC registration and disclosure would yield more valuable information to investors than the current voluntary agreement. “These studies demonstrate that it is essential that Fannie Mae and Freddie Mac be subject to mandatory disclosure,” concluded Paige. “That's why the Shays-Markey bill should be enacted as soon as possible.” (*CCAGW press release, 5/7/03*)

### NTU supports Shays-Markey bill

- In a May 15 letter to Congressmen Shays and Markey, NTU Director of Government Affairs Paul J. Gessing, wrote that NTU offers its “enthusiastic support” for their bill repealing Fannie and Freddie’s SEC exemptions.
- The “modest and necessary reforms” contained in the bill “are an important step forward in improving the transparency” of these GSEs by “increasing the timeliness and flow of information.” Gessing noted, “In this era of heightened scrutiny of corporate governance, it is exceedingly important that GSEs at the very least conform to the same oversight regulations as companies that issue publicly traded stock.”
- “Oversight issues surrounding Fannie Mae and Freddie Mac have long been of concern to NTU. Trillions of dollars in potential taxpayer liabilities add up to one big reason for better monitoring of GSEs like Fannie Mae and Freddie Mac. Recent corporate scandals and bankruptcies ought to convince policymakers of the need for more fiscal stewardship now.”  
(*NTU letter to Congressman Shays and Markey, 5/15/03*)

Congressman Pete Stark (D-CA) introduces bill removing Fannie & Freddie’s state and local tax exemption

Lifting tax-exempt status on billions in profits would aid state fiscal crises

Fannie & Freddie and the National Association of Home Builders criticize the bill

NTU suggests ending Fannie & Freddie’s tax exemption as long as every single dollar of those new tax revenues is returned to homeowners in the form of a property tax relief

- Congressman Stark introduced May 15 the “Secondary Mortgage Market Fair Competition Act” (HR 2117) that would amend Fannie and Freddie’s tax-exempt status to allow states to tax these corporations’ pre-tax earnings as they do private mortgage companies.  
(*Congressman Stark press release, 5/15/03*) A 2001 congressional study estimated the value to Fannie and Freddie’s state and local income tax-exemption at \$761.3 million in 2000.  
(*Reuters, 5/15/03*) Stark serves on the House Ways and Means Committee, Joint Economic Committee, and Joint Taxation Committee.
- “Fannie Mae and Freddie Mac are much different today than when they were first chartered over thirty years ago,” said Congressman Stark. “They are thriving, successful private corporations that earned \$10 billion in combined profits in 2001 and made Fortune magazine’s list of most profitable companies. It is clear that Fannie Mae and Freddie Mac are strong and profitable enough to provide a steady stream of home loans without the state tax-exempt privilege that was once needed to draw investors,” said Congressman Stark.  
(*Congressman Stark press release, 5/15/03*)

- Though Fannie and Freddie pay federal taxes, they do not pay state or local corporate income taxes. “Lifting Fannie Mae and Freddie Mac’s exemption from state and local taxes would provide a much-needed revenue source [for states]. In no way would states be required to tax these corporations. They would simply be given that choice as a means to avoid cuts in basic services people rely on at a time when Fannie and Freddie are amassing billions of profits each year.” (*Congressman Stark press release, 5/15/03*) “It will also help to level the playing field for Fannie and Freddie’s competitors by eliminating this tax advantage provided to Fannie and Freddie. At a time when states are facing fiscal crises and Fannie Mae and Freddie Mac are facing healthy profits, states should be provided the opportunity to tax these corporations just as states tax their competitors.” (*Congressman Stark statement on introducing bill to allow states to draw on Fannie and Freddie’s profits, 5/14/03*)
- “The fact that Fannie Mae and Freddie Mac are doing so well is a clear indicator that they serve the home loan industry well...But these successes should not lead Congress to shelter Fannie and Freddie from the rigors of the marketplace indefinitely or prevent states from sharing in the benefits.” (*Congressman Stark press release, 5/15/03*)

#### Fannie & Freddie and the National Association of Home Builders criticize the bill

- Fannie Senior Vice President Chuck Greener said the effect of Congressman Stark’s bill was a “tax on homeownership,” and predicted little or no support for the bill. (*BNA Daily Report for Executives, 5/16/03*)
- A Freddie spokeswoman criticized the bill, saying Fannie and Freddie’s state and local tax exemption helps Freddie better assist homebuyers nationwide. (*BNA Daily Report for Executives, 5/16/03*) “When Congress chartered us they specifically created the state income tax exemption to ensure we could accomplish our mission of providing affordable mortgage capital in every state at all times,” said Freddie’s spokeswoman Sharon McHale. (*Dow Jones Newswire, Dawn Kopecki, 5/15/03*)
- Congressman Stark’s bill could harm the nation’s housing finance system and “could end up acting as a tax on housing and homeownership by driving mortgage interest rates higher,” said Jerry Howard, executive vice president and CEO of the National Association of Home Builders. “Fannie and Freddie are the lynchpin of the nation’s mortgage finance market, and this bill threatens to weaken the housing finance system.” Howard added that requiring Fannie and Freddie to pay hundreds of millions of dollars annually in taxes could adversely impact the housing financial market and the entire housing industry. “Ultimately, these expenses would be passed on to consumers in the form of higher mortgage rates. And this would harm home buyers and home builders alike.” (*PR Newswire, 5/15/03*)
- Former Treasury Department official Pat Cave said he does not think the measure has much traction this year. “The only things I see getting done this year are additional efforts by the Treasury to improve disclosures and (Rep. Richard) Baker making strides to improve safety and soundness regulation,” said Cave, who now heads the financial services lobbying business for the Federalist Group. (*Dow Jones Newswire, Dawn Kopecki, 5/15/03*)

NTU suggests ending Fannie & Freddie's tax exemption as long as every single dollar of those new tax revenues is returned to homeowners in the form of a property tax relief

- National Taxpayers Union (NTU) President John Berthoud was a guest on *WashingtonPost.com* on May 16 answering questions about taxes. When asked whether NTU would support Congressman Starks' bill that repeals Fannie and Freddie's state and local income tax exemption, Berthoud gave the following response:
- "Fannie and Freddie claim that their exemption from state and local income taxes is only fair since otherwise, they'd have to pass along the costs to homeowners. That's partly true, although some of that cost would be passed along to Fannie and Freddie employees (including their many, many six-figure salaried lobbyists and public relations people). And also remember that taxes on any business ultimately hurt that business's consumers and workers (this isn't just true for Fannie and Freddie). It's hard to see any reason why they should be tax-exempt when their competitors are not."
- "...we think the aggregate tax burden in America is too high. So we couldn't support Rep. Stark's bill that would add to the tax burden."
- "That said, it certainly would make economic sense if we could end the exemption as long as every single dollar of those new tax revenues was returned to homeowners in the form of property tax relief. With skyrocketing property taxes across America, homeowners are in much greater need of relief than Fannie and Freddie (organizations which enjoy great special benefits courtesy of the federal government). And if we want to have government tax policy help homeowners, this swap I'm suggesting (ending the tax exemption for Fannie and Freddie and having those dollars turned into property tax relief for homeowners) would be a much, much better way to do it."
- "Fannie's and Freddie's gaggle of lobbyists like to crow that all the special breaks they get from Washington are of great benefit to home buyers, but the reality is that these breaks are very inefficient in terms of delivering help for homeowners." (*WashingtonPost.com online discussion with NTU President John Berthoud, 5/16/03*)

#### Congressional Black Caucus aids Fannie in its feud with the FHLBanks

Caucus asks FHFB to consider increasing the FHLBanks' affordable housing goals in light of its Shared Funding program that competes with Fannie & Freddie

Caucus asks FHFB to provide a "profile of the loans purchased so far under the FHLBanks housing programs," to compare the FHLBanks' affordable housing goals with Fannie & Freddie

- The Congressional Black Caucus "is siding" with Fannie "in a spat" with the FHLBank System, by "criticizing a new FHLBank funding program in a letter to the Federal Housing Finance Board," according to *Dow Jones Newswire*. The letter was created "in part, with help from lobbyists at Fannie Mae." (*Dow Jones Newswire, Dawn Kopecki, 5/6/03*)

- In a February 26 letter to FHFB Chairman John Korsmo, the Caucus asked the FHFB to consider increasing the FHLBanks' affordable housing goals in light of an expanded funding program that securitizes mortgages purchased by the FHLBank of Chicago. "Absent clear and demonstrated benefits for our constituents and their mortgage needs, we see no reason for your programs to be expanded without being subject to additional housing goals comparable to those for Fannie Mae and Freddie Mac." (*Congressional Black Caucus letter to FHFB Chairman John Korsmo, 2/26/03*)
- The program in question – the FHLBanks' Shared Funding program - was approved by the FHFB in December 2002, and creates mortgage securities for investment by the FHLBanks and their members, by creating mortgage-backed certificates from conventional conforming mortgages as an alternative to agency mortgage-backed securities provided by Fannie and Freddie. Analysts view the Shared Funding program as a step towards securitization, but the Treasury Department has stopped short of asserting that. "Treasury has reviewed the Chicago FHLB's Shared Funding program and concluded that it is not a securitization plan," a Treasury spokeswoman said. (*Market News International, Claudia Hirsch, 4/7/03*) The first MPF Shared Funding transaction was completed in March. [See March 24, 2003 *GSE Report* for more information, [www.gsereport.com](http://www.gsereport.com).]
- The Congressional Black Caucus said reports suggested that the FHLBanks "are only purchasing the highest performing loans, giving rise to the question as to whether this mission expansion would service policy goals and social needs." The Caucus asked the FHFB to provide a "profile of the loans purchased so far under the FHLBanks housing programs," so that the Caucus could compare the FHLBanks' performance with Fannie and Freddie's affordable housing goals, particularly in the areas of low-and moderate-income and underserved areas. (*Congressional Black Caucus letter to FHFB Chairman John Korsmo, 2/26/03*)
- Caucus spokesman Doug Thornell said Fannie was consulted on some of the letter's content, but that the Caucus staff ultimately wrote the letter. Capitol Hill aides and lobbyists said that Fannie's lobbyists have also launched in recent months a fierce behind-the-scenes whisper campaign against the FHLBanks, seeking to discredit their operations and call into question the credibility of the system's regulator. (*Dow Jones Newswire, Dawn Kopecki, 5/6/03*) [See April 21, 2003 *GSE Report* for Western Caucus letter in opposition to the Shared Funding program, [www.gsereport.com](http://www.gsereport.com)]
- *Dow Jones Newswire* noted that the Congressional Black Caucus has been a longtime supporter of Fannie and vice-versa. For example, the Fannie Mae Foundation has contributed more than \$250,000 since 1996 to the Caucus. (*Dow Jones Newswire, Dawn Kopecki, 5/6/03*)

FM Watch announces new Chairman, new focus for organization and new name (FM Policy Focus)

Former Congressman JC Watts (R-OK) to lead the effort

Fannie & Freddie dismiss the changes

Citizens Against Government Waste applauds Watts' comments on Fox News

- FM Watch announced May 13 the appointment of a new Chairman, former Oklahoma Congressman, GOP leader and author of the American Community Renewal and New Markets Act of 2000, J.C. Watts. Watts will be overseeing the unveiling of a new, more policy-intensive focus for the organization and the changing of the name to FM Policy Focus. FM Watch was established on June 17, 1999 (*FM Watch press release, 5/13/03*) FM Policy Focus retained Watts and his new consulting firm, J.C. Watts Cos., on a part-time basis. (*Dow Jones Newswire, Dawn Kopecki, 5/13/03*)
- “I think the GSEs were established with good intentions. Unfortunately good intentions with bad models become a recipe for disappointment,” Watts said. “What I would like to see FM Policy Focus do is bring the policy that is out of focus more into focus.” (*American Banker, Rob Garver, 5/14/03*)
- Its new name is meant to signal that the group is shifting its emphasis to lobbying Congress and the White House for changes in the way Fannie and Freddie operate, Watts said. For example, the group will press for a tougher regulator – such as the Federal Reserve Board or the Treasury Department. (*Washington Post, Kathleen Day, 5/13/03*) “The focus is switching to the solutions phase,” a spokeswoman for the group, Beneva Schulte, told *Reuters*. (*Reuters, 5/13/03*) “We finished what I call Phase 1 of the job, which was to show that there is a problem,” said FM Policy Focus Executive Director Mike House. “I think everyone would agree that that message has been well received and has resonance on the Hill, with the Administration, everywhere.” The next phase is to work on a solution. (*American Banker, Rob Garver, 5/14/03*)
- Watts said his main mission with FM Policy Focus will be to steer public debate about the GSEs on the proper use of their federal charters, disclosure parity with other publicly traded companies, affordable housing goals and strengthening federal oversight. (*Dow Jones Newswire, Dawn Kopecki, 5/13/03*) FM Policy Focus Executive Director Mike House said priorities for the group would be a requirement that Fannie and Freddie secure pre-clearance of any new activities with their mission regulator (HUD), tougher affordable housing goals for Fannie and Freddie, and improved disclosures regarding Fannie and Freddie’s mortgage-backed securities. (*BNA Daily Report for Executives, Richard Cowden, 5/14/03*)

### Fannie & Freddie dismiss the changes

- “We have no doubt that as lobbyists they [FM Policy Focus] will continue to employ any tactic or argument available to protect their member companies’ interests and profits,” Fannie’s spokesman Chuck Greener said. “To date, FM Watch has failed to gain any traction or credibility because they have pursued a wholly negative agenda, which has consistently been anti-housing and anti-consumer,” he said. (*Dow Jones Newswire*, Dawn Kopecki, 5/13/03)
- “FM Watch is trying to breathe some life into the organization by changing its leadership. They can do that, but until they show they have an interest beyond the self-interest of its member organizations, I don’t think it’s going to matter who they hire,” said Freddie’s spokeswoman Sharon McHale. (*Reuters*, 5/13/03)

### CAGW applauds Watts’ comments on Fox News

- Citizens Against Government Waste (CAGW) May 15 applauded Watts for his comments about Fannie and Freddie, in an appearance on Fox News channel. In a segment of *Your World with Neil Cavuto* that discussed the proper roles of Fannie and Freddie, Watts said both organizations had exceeded the limits of their charters, and moved from the secondary lending market into primary lending.
- “J.C. Watts is correct to point out that these GSE's have strayed out of the secondary market and away from their mission,” CAGW Vice President Leslie Paige said. “Focusing on first-time homebuyers and low-income homebuyers are where their energies should lie not in chasing above-market profits. Watts will be a valuable ally in the fight to enact reforms that will promote greater competition in lending markets and aid consumers. We welcome his help in putting this very important consumer issue out in front of the public where it needs to be.”
- CAGW noted that Fannie and Freddie benefit from federal subsidies amounting to \$10.6 billion annually, and either own or guarantee more than 40 percent of the U.S. mortgage market. Both institutions are exempt from the taxes and regulations that hamper most private corporations, giving the GSEs an undue advantage in the marketplace. As a result, the Council for Citizens Against Government Waste [the lobbying arm of CAGW] has come out in favor of the “Leave No Securities Behind Act” recently introduced by Reps. Chris Shays (R-Conn.) and Rep. Ed Markey (D-Mass.). The bill would require Fannie and Freddie to disclose information to the Securities and Exchange Commission (SEC), which is required of all private companies.
- “The ‘Leave No Securities Behind Act’ is an excellent step toward making Fannie Mae and Freddie Mac more transparent organizations,” said Paige. “Now is a time when the adequacy of corporate governance and the importance of full disclosure are high on the public's agenda. Congress should pass this measure, and pursue more reforms to open up the mortgage-lending market. Perhaps in the not-to-distant future, both GSEs will be fully privatized, benefiting would-be homeowners across America.” (*CAGW press release*, 5/15/03)

FM Policy Focus asks HUD to take immediate action to block Fannie's PaymentPower™ program and establish a pre-clearance process to protect consumers

FM Policy Focus claims the program is an "entry by Fannie Mae into direct consumer loan origination" and is outside Fannie's charter

FM Policy Focus Chairman J.C. Watts says HUD should keep Fannie out of the origination business

Fannie & HUD respond to the charges

- Just days after FM Watch announced the appointment of former Congressman J.C. Watts (R-OK) as its new Chairman and announced its new name (FM Policy Focus) and new policy focus, the group formally petitioned HUD May 20 to block Fannie's new program - "PaymentPower™." Claiming that the program is an "entry by Fannie Mae into direct consumer loan origination," FM Policy Focus "urged HUD to act quickly on its petition" and to institute a pre-clearance process that will protect American consumers, stop the GSEs from further encroachments into the primary mortgage market and into the general business of providing retail financial services. (*FM Policy Focus press release, 5/20/03*)

FM Policy Focus claims the interest rate on the program is as high as 69%

- PaymentPower™ is a loan product in which a borrower may skip up to ten payments over the life of a mortgage. The principal and interest due for such skipped payments, along with taxes and insurance, are then converted into a new obligation added by Fannie to the balance of the loan principal. Borrowers pay an up-front fee for this feature or a combination of an up-front and an additional charge each time a payment is skipped. FM Policy Focus claimed that these charges can result in effective interest rates on the skipped payment as high as 69%. (*FM Policy Focus press release, 5/20/03*)

FM Policy Focus claims HUD lacks a pre-clearance process

- "While Fannie Mae's PaymentPower™ program raises many questions about the company's charter, its mission, its special privileged status, its regulators, and exactly whether or not consumers benefit, its mission regulator doesn't seem to be asking them," said FM Policy Focus Chairman J.C. Watts. "Every once in a while, someone might need a little extra cash to make ends meet. When banks enter into new lines of business to meet these needs, they must tell the Federal Reserve or other regulators what they want to do and why. There is no such check for Fannie Mae and Freddie Mac. HUD is required by law to pre-clear all new programs that the GSEs introduce, but knowing that HUD lacks a pre-clearance process, the GSEs never ask HUD for approval. There is no regulatory oversight and that's a problem." (*FM Policy Focus press release, 5/20/03*)

- FM Policy Focus noted that the problems and questions surrounding PaymentPower™ and HUD’s inability include:

PaymentPower™ is a “classic example of ‘mission creep’”:

- “Since PaymentPower™ creates a new loan obligation for the borrower, it qualifies as loan origination, an activity Fannie Mae’s charter prohibits. Fannie Mae might argue that PaymentPower™ is an insurance program rather than loan origination. The creation of a new loan obligation clearly qualifies it as loan origination, but even if PaymentPower™ were simply an ‘insurance program,’ GSEs are not subject to appropriate state insurance regulations, and their presence in the market presents an undue risk to consumers.” (*FM Policy Focus press release, 5/20/03*)

PaymentPower™ is “anti-consumer”:

- “Depending upon how they use PaymentPower™, consumers could pay interest rates as high as 69%. If banks or other lenders in certain states offered a program like this, it would trigger state usury ceilings. Such programs have been barred by the Office of the Comptroller of the Currency (OCC) as potentially predatory. In fact, if Fannie Mae was a bank, it couldn’t offer this program.” (*FM Policy Focus press release, 5/20/03*)

Consumers have other options than PaymentPower™:

- “Numerous highly-competitive products – home-equity loans, credit cards, savings accounts – exist for consumers who wish to meet unexpected financial needs or make desired purchases. Nothing in this product promotes home ownership. Indeed, the ability for consumers to improve homes or upgrade to new mortgages is adversely affected by the increased obligation (up to 8% of the original mortgage principal) incurred when full use is made of the PaymentPower™ options.” (*FM Policy Focus press release, 5/20/03*)

PaymentPower™ is against Fannie’s mission:

- “The costs of Payment Power™ are so high that the program actually undermines one express purpose of the Fannie Mae charter: to help make homeownership more affordable.” (*FM Policy Focus press release, 5/20/03*)

HUD did not review PaymentPower™:

- “In 1992, Congress mandated that Fannie Mae submit new programs like PaymentPower™ to the Department of Housing and Urban Development for review and approval *before* rolling them out.” (*FM Policy Focus press release, 5/20/03*)

PaymentPower™ is not a “pilot” program:

- “Fannie Mae is presumably avoiding a HUD review by calling this program a ‘pilot.’ But the program is being offered by at least thirteen lenders in thirteen states including California (home to more than 20% of the nation’s mortgage market), and can hardly be called a pilot. In addition, Fannie Mae reportedly plans to roll the new program out nationwide before year-end.” (*FM Policy Focus press release, 5/20/03*)

### PaymentPower™ needs HUD Attention and Action:

- “Fannie Mae’s refusal to submit this program for HUD review is hardly surprising. The GSEs have always disregarded the requirement to do so. HUD must establish a pre-clearance review process so that programs like PaymentPower™ are not presented to consumers without adequate regulatory review.” (*FM Policy Focus press release, 5/20/03*)
- For more information on Fannie’s PaymentPower™ program and FM Policy Focus’ comments, see FM Policy Focus Web site: [www.fmpolicyfocus.org](http://www.fmpolicyfocus.org)

### FM Policy Focus Chairman J.C. Watts says HUD should keep Fannie out of the origination business

- In a May 23 *American Banker* commentary, FM Policy Focus Chairman J.C. Watts urged HUD to keep Fannie out of the origination business. Watts noted that when banks want to enter a new line of business, their regulators closely scrutinize them. Watts noted, however, “[t]here is no such check on Fannie Mae. Though their regulator, the Department of Housing and Urban Development, is required to clear all new Fannie Mae programs in advance, it never, ever does. Fannie Mae is free to wander into new lines of business, like loan origination or insurance, and can do so with advantages no other company can match: an implicit guarantee from U.S. taxpayers and no regulatory oversight.”
- “PaymentPower is a clear example of Fannie Mae's straying from its congressional charter. By providing a consumer-lending vehicle outside the regulatory safeguards other entities offering the same benefit to consumers are subject to, it is clearly violating its mission. The program does nothing to promote the goal of affordable homeownership, the express purpose of Fannie Mae's massive government subsidy. To the contrary, for many consumers, PaymentPower would have the opposite effect.”
- Watts concluded, “HUD should do its job and pre-clear Fannie Mae programs, getting it back on its chartered track. Fannie Mae must focus on activities that truly promote the American dream of homeownership.” (*American Banker* commentary, J.C. Watts, 5/23/03)

### Fannie’s response

- PaymentPower™ “was developed at the request of our lender partners to provide flexibility to homeowners in managing their mortgage payments,” Fannie’s spokesman Chuck Greener said in a statement. “We’ve kept HUD apprised as we developed this initiative, and it is laughable to suggest that buying a mortgage from a lender is somehow outside our mission.” (*Bloomberg News*, Al Yoon, 5/20/03) A Fannie spokesman was mystified by how FM Policy Focus calculated the interest payment on the skipped loan amount. “I don’t know where they are coming from,” he said. (*National Mortgage News*, 5/26/03)

### HUD’s response

- HUD, in a statement, said it reviewed the program in 2002 and has begun meeting quarterly with officials from Fannie and Freddie as part of stepped up oversight. (*Reuters*, Mark Felsenthal, 5/20/03)

PaymentPower™ may cause “headaches” for FM Policy Focus, reports *American Banker*

- FM Policy Focus’ decision to use PaymentPower™ as its first criticism of the GSEs since undergoing a new makeover “may lead to as many headaches for the lobbying group as for the GSEs,” reported Rob Garver with the *American Banker*. Garver noted that several of FM Policy Focus’ complaints against Fannie’s PaymentPower™ program conflict with at least some of the business practices of FM Policy Focus members, noting that Countrywide and Hibernia, which offer the product, are members of the Financial Services Roundtable and Consumer Bankers Association, both of which belong to FM Policy Focus. Garver reported that there were also potential inconsistencies with FM Policy Focus’ comments about the OCC, adding that the OCC has not issued a rule or legal interpretation that these “skip-payment” programs are illegal for national banks. “We have no policies pertaining to skip-payment programs,” an OCC spokesman said. “Banks do offer consumers the option to skip a payment on credit card or auto loans, and we don’t have any problem with that provided they follow sound underwriting and account management procedures. I really can’t address Fannie Mae’s program. We are still looking at it.” Garver also noted that bank attorneys were “hard-pressed” to equate honoring the skip-payment option with the origination of a new loan and that sources charged FM Policy Focus as misrepresenting PaymentPower’s™ pricing strategy. (*American Banker*, Rob Garver, 5/27/03)

House Financial Services Committee approves regulatory relief bill (HR 1375), which contains provision allowing privately insured credit unions to become FHLBank members

Amendment by Congressman Paul Kanjorski (D-PA) eliminating this provision was defeated by voice vote

Manager’s amendment would make extensions on the terms of the FHLBank Directors prospective

Amendment pushed by the FDIC that would have prevented or limited the ability of the FHLBanks to collect prepayment fees on advances to institutions that have failed was not introduced

ABA, ACB and ICBA opposed the FDIC amendment

- The House Financial Services Committee approved by voice vote a regulatory relief bill (HR 1375) that would among other things, allow state-chartered, privately insured credit unions to become FHLBank members if they meet certain eligibility requirements. The Committee accepted two amendments to the legislation by voice vote: (1) a manager’s amendment offered by Chairman Michael Oxley (R-OH) that would make extensions on the terms of FHLBank Directors prospective and clarify the civil remedies that can be imposed by the FCIC in the event of a misrepresentation by an individual, corporation, or other entity of FDIC insurance coverage; and (2) an amendment that would clarify the regulatory structure for state chartered, multi-state banks. (*Financial Services Committee press release*, 5/20/03)

- Congressman Kanjorski offered an amendment that would have eliminated the section of the bill allowing state chartered credit unions from being part of the FHLBank System. However, the amendment received less than a handful of supporters on the Committee and was defeated by voice vote. (*CUNA News*, 5/20/03) The House Financial Institutions Subcommittee approved HR 1375 by voice vote on April 9.
- A regulatory relief bill (HR 3951), containing a provision that would allow privately insured credit unions to join the FHLBank System, was considered during the last session of Congress. The bill was approved by the House Financial Services Committee but never made it to the House or Senate floors. [See July 19, 2002 *GSE Report* for more information, [www.gsereport.com](http://www.gsereport.com)]

Amendment pushed by the FDIC that would have prevented or limited the ability of the FHLBanks to collect prepayment fees on advances to institutions that have failed was not introduced

- There was speculation that the FDIC might seek to include an amendment to HR 1375 that would prevent or limit the ability of the FHLBanks to collect prepayment fees on advances to institutions that have gone into receivership. The amendment was not introduced. (*American Banker*, Rob Blackwell, 5/21/03) The FDIC began pushing for the amendment after the FDIC took over the \$69 million-asset Bank of Alamo in Tennessee (which failed in November) and wanting to free up collateral for auction, it tried to repay \$6.4 million of advances to the FHLBank of Cincinnati, and was charged by the FHLBank of Cincinnati an extra \$906,000 or 14 percent, for paying the advances off early. The FDIC and the FHLBanks have been working on a compromise, but the two sides are currently deadlocked. The Federal Housing Finance Board has largely stayed out of the discussion and a spokesman said May 16 that neither the FDIC's proposed amendment nor the FHLBanks' proposal were good solutions. (*American Banker*, Rob Blackwell, 5/20/03)
- The American Bankers Association (ABA), America's Community Bankers (ACB) and the Independent Community Bankers of America (ICBA) sent a joint letter May 16 to Chairman Michael Oxley (R-OH) expressing their concerns with the amendment. The trade groups said the provision "would be detrimental to the Federal Home Loan Bank System and our members who are its stockholders." The trade groups noted that the provision "is not as straightforward as some claim," and "[in] reality it could have far-reaching, negative implications for the 8,000 member institutions of the FHLBanks and their cost of funds." The groups warned that if the provision were to become law, "the FHLBanks would have to adjust their lending practices in regard to medium and long-term advances to avoid adversely affecting their own safety and soundness. This would harm both the owners of the System and their communities by restricting the availability of this critical source of funding and/or raising the cost of medium and long-term credit for all institutions." The group also opposed language under which the FDIC would pay the costs for unwinding hedges on advances to large failed banks, but require the FHLBanks to share these costs for smaller failed banks. "This would unjustly discriminate against community banks that depend most heavily on FHLBank advances for housing and community development," said the trade groups. In

addition, the trade groups noted that the 12 FHLBanks have proposed a non-legislative compromise that would ensure that the FDIC would not have to pay full prepayment penalties, but only compensate the FHLBank for the cost of unwinding hedges that become uneconomic when an advance is prepaid. "Thus, it is premature for Congress to attempt to resolve this issue," the trade groups said. (*ABA, ACB, ICBA joint trade letter to Chairman Oxley, 5/16/03*)

AEI to hold June 9 conference to discuss whether Fannie & Freddie are meeting their affordable housing mission

- The American Enterprise Institute (AEI) is holding a June 9 conference to discuss whether Fannie and Freddie are meeting their obligations to promote minority and low-income homeownership. As GSEs, Fannie and Freddie are subject to HUD regulations that require them to foster the growth of low-income and minority homeownership. Over the years, however, many studies have questioned whether Fannie and Freddie's performance has been satisfactory. Even though an OMB analysis that accompanied the president's FY 2004 budget noted that Fannie and Freddie's support for minority and low-income housing was inadequate, Fannie and Freddie regularly advertise that they are meeting the goals set by HUD. This discrepancy may be the result in part of loosely written regulations, which are currently under review by HUD. The AEI conference will present data comparing the performance of Fannie and Freddie in assisting low-income and minority housing with their support of conventional middle-class housing. (*Invitation to June 9 AEI conference*)
- The conference will be held June 9 from 10:00 a.m.- noon at AEI's Wohlstetter Conference Center, 1150 Seventeenth Street, NW, Washington, DC 20036, 12<sup>th</sup> Floor. The schedule is as follows:

9:45 a.m.      Registration

10:00 a.m.      Introduction: Peter J. Wallison, AEI

10:15 a.m.      The Support of Low-Income and Minority Housing by Fannie and Freddie

Presenter:      Jonathan Brown, Essential Information

Discussants:    Richard A. Williams, Notre Dame University  
Peter Zorn, Freddie Mac

Moderator:     Peter J. Wallison, AEI

Noon            Adjournment

Registration can be done online at [www.aei.org/events](http://www.aei.org/events).

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

Freddie is taking immediate action to rein in the pace of home mortgage re-financings and address market share losses to Fannie

Freddie's efforts at reducing re-financings might alienate lenders and might be viewed as harmful to consumers, warn analysts

Freddie accused of "cherry picking" the best mortgages -- keeping for its own portfolio the mortgages least likely to refinance

Freddie's faster MBS prepayment speeds compared to Fannie's are blamed for Freddie's loss of market share

- Freddie is taking steps to rein in the pace of home mortgage refinancings that have turned investors away from its mortgage-backed bonds, according to Freddie's Vice Chairman and President David Glenn. Prices on Freddie's securities backed by pools of mortgages have dropped below those of similar Fannie bonds for the first time in five years, in part because the loans in Freddie's pools are being refinanced by homeowners faster than those in Fannie's. Investors typically avoid bonds backed by loans at risk of being repaid early, because they may receive their money back sooner than expected and must reinvest at lower rates. (*Bloomberg News*, Al Yoon, 5/15/03) Freddie's faster re-financings make investors less interested in buying Freddie's mortgage bonds, and lenders less interested in selling to Freddie, which is shrinking Freddie's market share compared to Fannie. (*Reuters*, Dan Wilchins, 5/22/03)
- The surge in re-financings has driven down the price on Freddie's bonds, known as "Gold Participation Certificates." A 6 percent Freddie mortgage bond with a face value of \$1 million fetches \$2,187.50 less than a comparable Fannie bond, according to Kevin Jacobs, a senior mortgage analyst at RBC Dain Rauscher Inc. That discount on Freddie bonds was as little as \$625 two weeks ago and last year, Freddie's bonds traded at a premium of as much as \$1,250 above Fannie's debt. (*Bloomberg News*, Al Yoon, 5/22/03)
- The faster prepayments may have come because Freddie tends to work with a few large lenders that aggressively encourage borrowers to refinance, an analyst said. Fannie works with many mid-sized lenders that less aggressively encourage borrowers to refinance. (*Reuters*, 5/16/03) Freddie said it is aware that its mortgages are coming from a smaller pool of sellers, and the company said it anticipates this servicing pool to increase for the balance of the year. Some MBS analysts attribute the small seller pool as a major reason why Freddie's prepayment speeds have been so high. (*Dow Jones Newswire*, Julie Haviv, 5/16/03)

- Concerns have emerged after Fannie posted April data recently showing that its outstanding MBSs grew at a compound rate of 67.6 percent, its highest rate in a decade. Although Freddie had not yet published its April data, market watchers said these figures were indicative of Freddie's declining market share. "Freddie Mac is losing a huge amount of market share," said David Montano, mortgage market strategist at JP Morgan. "Freddie Mac has been increasingly relying on a small number of mortgage servicers, while Fannie Mae represents a larger and much more diverse market segment... Unfortunately, Freddie Mac's servicers tend to be a faster prepaying market segment," said Montano. He noted that Freddie has lost over \$100 billion in 30-year MBS market share over the last seven months. "It's a phenomenal amount," he added. (*Dow Jones Newswire*, Julie Haviv, 5/15/03; 5/16/03)
- "Freddie Mac is losing market share to Fannie Mae because there is a perception that Freddie Mac MBS are paying a lot faster than Fannie Mae," said Kevin Jackson, vice president and senior bond strategist at RBC Dain Rauscher. "If people start perceiving that people are not buying their securities, Freddie Mac's stock may take a hit," said Jackson. Since Freddie owns its own MBS, the decline may also hurt the market value of Freddie's portfolio, and investors holding on to Freddie's MBS could lose money when they decide to sell the loans. (*Dow Jones Newswire*, Julie Haviv, 5/15/03) Freddie owns approximately 30 percent of its own mortgage-backed securities. (*Dow Jones Newswire*, Julie Haviv, 5/22/03)
- April's MBS prepayment data showed a huge difference in the speed at which mortgages were prepaid at Fannie and Freddie MBS, based on constant prepayment rates [CPR]. For example, Fannie's new production 15-year 6s showed a constant prepayment rate, or CPR, of 58; while Freddie's 15-year 6s had a CPR of 68. (*Dow Jones Newswire*, Julie Haviv, 5/15/03, 5/16/03) A report by Fox-Pitt, Kelton said that Freddie's market share was roughly 31 percent in April, lower than what it was in March (Freddie's traditional market share is 40 to 42 percent). (*Asset Securitization Report*, Karen Sibayan, 5/19/03)

#### Freddie's three-point strategy

- "We are taking immediate action to achieve our corporate objective that prepayment experience on Freddie Mac PCs [participation certificates] is consistent with market norms," Glenn noted May 15 in a notice posted on Freddie's Web site. (*Bloomberg News*, 5/19/03; *Freddie web site*, 5/19/03)
- Freddie laid out a three-point strategy, which includes, "[i]mmediate development of contractual incentives and penalties around sellers' prepayment experience on outstanding and new PCs." Freddie's spokesman Doug Robinson said the company will scrutinize each mortgage lender or servicer on a case-by-case basis. He wouldn't elaborate on the incentives or penalties. (*Bloomberg News*, Al Yoon, 5/15/03; *Freddie web site*, 5/19/03) In other words, Freddie will monitor the rate at which mortgages are being prepaid at its servicers, possibly trying to prompt a different kind of behavior from them if they are not reasonably in line with the speeds recorded by other servicers. "We want our servicers to understand that we expect the average mortgage to be prepaid at an average speed," said Robinson. "We don't expect the average mortgage to prepay faster than an average speed." Robinson added, "When we see the average speed coming through from a servicer looking awry, we are going

to see what is going on with that.” (*Dow Jones Newswire*, Julie Haviv, 5/16/03)

- Freddie also plans on “[r]eturning loan characteristics and seller/servicer diversity to more typical levels over the balance of the year.” (*Freddie web site*, 5/19/03)
- Finally, Freddie is removing allocation restrictions on its mortgage securities for the creation of REMICs [Real Estate Mortgage Investment Conduits]. This change is expected to expand opportunities for dealers and create demand for Freddie’s securities, said Robinson. (*Bloomberg News*, Al Yoon, 5/15/03; *Freddie web site*, 5/19/03) Previously, Freddie had been allocating a specific share of the REMIC market to the dealer community, but now it is no longer limiting the allocations, so dealers can create as many REMICs as they can without worrying about allocations. (*Dow Jones Newswire*, Julie Haviv, 5/16/03)

Freddie’s efforts at reducing re-financings might alienate lenders and might be viewed as harmful to consumers, warn analysts

- Freddie’s strategy at reducing re-financings, designed to attract support from investors, threatens to alienate lenders, particularly the large mortgage lenders it relies on for much of its volume, analysts said. Further, Freddie’s plan to incorporate prepayment risk into its loan pricing could expose the GSE to more political scrutiny, experts said. In a teleconference May 21, David Andrukonis, Freddie’s Senior Vice President for Capital Deployment in Freddie’s single-family division, noted that one way the company plans to “incent” lenders to deliver loans that pay off more slowly, is to reduce guarantee fees by 2 to 3 basis points for lenders whose portfolios have prepaid slowly. Chris Buonafede, an analyst with Fox-Pitt, Kelton Group, noted that the gap in Fannie and Freddie’s prepayment speeds “has a lot to do with customer concentration issues,” explaining that a handful of large lenders, including ABN Amro Mortgage Group, Wells Fargo & Co., and Bank of America Corp., account for about 60 percent of Freddie’s volume. For that reason, Buonafede said, he is worried that Freddie’s incentive plan will backfire. “If Wells Fargo has high prepayments, and Freddie raises the guarantee fee, isn’t that going to keep Wells away?” he said. Freddie is “digging a hole for themselves relative to what traditionally were their biggest customers.” (*American Banker*, Erick Bergquist and Marc Hochstein, 5/23/03)
- Michael J. Schroeder, the president and chief investment officer of Wasmer, Schroeder & Co., a fixed-income investment advisory firm in Naples, FL, said Freddie’s incentive plan also might be viewed as harmful to consumers. If a homeowner requests refinancing, and the banker “has a disincentive to say yes,” Schroeder said, “is that right for the consumer? I don’t think so. If my servicer is going to lose money if I refinance, is he going to tell me it’s time to refinance?” The danger is that “somebody in Congress uses this as another reason to rein these guys in.” On the teleconference, Andrukonis said Freddie’s new incentives would not raise costs for consumers, and suggested that it would even make the pricing of loans fairer to them. (*American Banker*, Erick Bergquist and Marc Hochstein, 5/23/03)

Freddie accused of “cherry picking” the best mortgages --- keeping for its own portfolio the mortgages least likely to refinance

- “Everything Freddie Mac says it’s doing to improve their bonds, it’s all smokescreens,” said

Kevin Jackson, a mortgage bond strategist at RBC Dain Rauscher. The real problem, Jackson said, is that Freddie is keeping for its own portfolio the mortgages least likely to refinance, and selling the rest to investors. "Freddie Mac is cherry picking. They take all the best mortgages for themselves," Jackson said. Freddie said that its portfolio managers do not cherry pick, and have no information that isn't available to other investors. (*Reuters*, Dan Wilchins, 5/22/03)

Fannie & Freddie release their April financial information
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### Fannie

- Fannie announced that its total business volume rose to a record high of \$139 billion, up almost 28 percent from March. Fannie's book of business grew at an extremely strong compound annual rate of 36.6 percent to \$1.97 trillion. Outstanding MBS grew at the highest rate in a decade, at a compound rate of 67.6 percent. Portfolio purchases rose to \$43 billion from \$34.3 billion while liquidations rose to \$40.5 billion from \$34.7 billion, or an annual rate of 59.4 percent. The record liquidation rate, which the company began tracking in 1989, was 60.7 percent in November, said Fannie spokesman Jason Lobo. These two factors led to mortgage portfolio growth of 2.9 percent annualized rate to \$817.9 billion, compared with a 1.1 percent fall in March. Retained commitments rose slightly to \$41.4 billion (up from \$39.5 billion in March), while outstanding portfolio commitments were a strong \$72 billion at month-end. The conventional single-family delinquency rate fell two basis points to 0.57 percent. The multi-family delinquency rate rose three basis points to 0.09 percent. Fannie's duration gap averaged minus two months during April, unchanged from March. (*Fannie's Monthly Financial Summary*, April 2003; *Reuters*, 5/13/03; *Bloomberg News*, Al Yoon, 5/13/03) With on-balance sheet mortgage holdings of \$817 billion and a total book of business of \$1.97 trillion, according to *National Mortgage News's* Quarterly Data Report, Fannie has a market share of about 30 percent (assuming US housing debt totals \$6.566 trillion). (*National Mortgage News*, 5/19/03)

### Freddie

- Freddie announced that its total mortgage portfolio (the sum of its investment portfolio and the MBSs it guarantees) decreased at an annualized rate of 11.6 percent in April to \$1.294 trillion, compared with a 6.5 percent increase in March. April's shrinkage of Freddie's investment and total mortgage portfolios reflected a rise in prepayments on Freddie's MBS. This was the second time in three months that Freddie's portfolio size decreased. Freddie's Gold MBS liquidated much faster than the amount issued in April, decreasing its total Gold MBS portfolio by 21.3 percent. Freddie's retained portfolio decreased at an annualized rate of 1.2 percent in April to \$569 billion following a 17.1 percent increase in March. Freddie bought \$25.6 billion in mortgage loans and bonds for investments in April, down from March's \$30.1 billion. Freddie's retained commitments declined to \$25.2 billion, down from \$32.3 billion in March. Freddie's total PC [Participation Certificate] portfolio decreased at an annualized rate of 21.3 percent in April and its structured securitizations were \$26 billion in April, down from \$32 billion for March. Freddie's single-family non-credit enhanced delinquency rate was 29 basis points, down from 30 basis points in the prior month.

Freddie's portfolio market value sensitivity (PMVS) averaged 2.08 percent in April, down from an average of 2.82 percent for March; Freddie's duration gap was zero in April, compared to negative one month in March. (*Freddie's Monthly Volume Summary*, April 2003; *Reuters*, 5/22/03; *Dow Jones Newswire*, Julie Haviv, 5/22/03)

#### Lenders and Fannie and Freddie ease mortgage forbearance for military

- Fannie and Freddie and their lender partners have made it easier for military personnel to obtain special forbearance on paying their mortgages. Effective immediately, the lenders and Fannie and Freddie will go beyond the Soldiers' and Sailors' Civil Relief Act (SSCRA). Specifically, active duty military personnel need only to notify their mortgage servicer about their active duty orders as proof of hardship, instead of the full range of financial statements required for standard forbearance. Fannie and Freddie have also instructed their lender partners not to report the forbearance plans to credit bureaus. (*Fannie press release*, 5/7/03; *Freddie press release*, 5/7/03) Under the SSCRA, all lenders are required to reduce interest rates on loans to active military personnel to 6 percent and to forgive all interest above that amount during their time of active duty. (*Mortgage Servicing News*, Ed Roberts, 5/16/03)

### **Fannie Mae**

Fannie's Vice Chairman Jamie Gorelick to join law firm

Fannie's CFO Timothy Howard named new Vice Chairman

- Wilmer, Cutler & Pickering announced that effective July 1, Jamie S. Gorelick, Vice Chair of Fannie, will join the firm as a partner in its Washington, DC office. Gorelick, a former Deputy Attorney General and General Counsel of the Department of Defense, will join Wilmer, Cutler & Pickering's litigation practice and advise clients on matters that involve complex legal, public policy and business issues. During her first year at the firm, Gorelick said she will continue to devote a substantial amount of her time to the work of the National Commission on Terrorist Attacks Upon the United States. "I will miss Fannie Mae," Gorelick noted. "It is a great company with an important mission, but I hope and expect to remain involved in the housing industry as I return to the practice of law." Gorelick will remain on the board of the Fannie Mae Foundation. (*Wilmer, Cutler & Pickering press release*, 5/14/03)
- The Board of Directors of Fannie named May 20 Timothy Howard Vice Chairman, following his election to the Board at the company's annual shareholder meeting. Howard will continue to serve as Fannie's Chief Financial Officer. (*Fannie press release*, 5/20/03)

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

Fannie has 57 Partnership Offices open across the country

Fannie “wins the gratitude of politicians by staging local events with them, often to ‘announce’ its plans to buy local mortgages...It’s almost as if Ford or Microsoft could allow politicians to gain some credit with voters for every Escort or Windows package sold in their district.” – *Wall Street Journal*, Nicholas Kulish & Jacob M. Schlesinger, 7/5/01

#### Fannie has 57 partnership offices

- According to Fannie’s Web site, the company has 57 partnership offices open across the country (<http://www.fanniemae.com/partnerhsipoffices/index.jhtml>) 4/14/03).

#### Fannie held press opportunities with the following officials:

- (1) Senator Bob Bennett (R-UT) and Lieutenant Governor Olene Walker (*Fannie press release*, 5/19/03)
- (2) Senator Tim Johnson (D-SD) (*Fannie press release*, 5/18/03)
- (3) Congressman Tom Cole (R-OK) and Congressman Ernest Istook (R-OK) (*Fannie press release*, 5/14/03)
- (4) Congressman Charles Gonzalez (D-TX) and Congressman Ciro Rodriguez (D-TX) (*Fannie press release*, 4/22/03)
- (5) Congressman Jerry Kleczka (D-WI), Milwaukee County Executive Scott Walker, and Milwaukee Mayor John Norquist (*Fannie press release*, 5/2/03)
- (6) Congressman Steve Chabot and Cincinnati Mayor Charlie Luken (*Fannie press release*, 4/24/03)
- (7) Congressman David Scott (D-GA) and Fulton County Commission Vice Chairman William “Bill” Edwards (*Fannie press release*, 4/22/03)
- (8) Congressman Roy Blunt (R-MO) (*Fannie press release*, 5/9/03)
- (9) Congressman John Tanner (D-TN) (*Fannie press release*, 5/8/03)
- (10) Congressman Gil Gutknecht (R-MN) (*Fannie press release*, 5/5/03)
- (11) Congressman William Lacy Clay (D-MO) (*Fannie press release*, 4/24/03)
- (12) Congressman Bill Thomas (R-CA) (*Fannie press release*, 4/22/03)
- (13) Florida Lieutenant Governor Toni Jennings and Tallahassee Mayor John Marks (*Fannie press release*, 5/12/03)
- (14) Kansas Governor Kathleen Sebelius (*Fannie press release*, 5/12/03)
- (15) Philadelphia Mayor John F. Street (*Fannie press release*, 4/24/03)

## **Freddie Mac**

Freddie defers its push for federal predatory lending preemption in favor of affecting state legislation advocated by the AARP

- Freddie is deferring its push for federal preemption from state and local anti-predatory lending laws for lenders, in favor of affecting the state legislation being advocated by consumer groups, especially the AARP, said several lobbyists familiar with the negotiations, reported *Home Equity News*. The publication also disclosed that Freddie has been meeting with AARP officials with respect to the AARP's model state anti-predatory lending bill. "Freddie's new stance has the potential to stall the enactment of a federal law that would preempt all other anti-predatory lending laws," reported the publication.
- In exchange for its endorsement, Freddie is asking the AARP to alter its model state anti-predatory lending bill, especially the provisions that deal with purchasing loans already originated, or investing in securitizations backed by loans that are subject to an anti-predatory lending law. Freddie's Senior Vice President for Government Relations Mitch Delk is representing the GSE in the negotiations. "Freddie Mac and Mitch Delk have gone off the 'reservation,'" and are now contemplating an idea that many mortgage lenders are against, said one lobbyist, who asked not to be named. The head of another consumer group confirmed that negotiations between Freddie and the AARP have been ongoing for several months, and estimated a 50-50 chance at a deal being reached. "Those who advocate a national solution to the predatory lending problem, which includes most lenders, lobbyists, and industry trade groups, are concerned about Freddie Mac's change of heart because unanimity is critical to any movement to enact federal pre-emption," reported *Home Equity News*. (*Home Equity News*, 5/5/03)

Freddie is aggressively pursuing business from community banks

Freddie and ICBA sign alliance agreement

- Freddie is warning community bankers to prepare for the post-refinance boom mortgage market and to begin the process of analyzing and restructuring their mortgage portfolios for a higher interest-rate, purchase money market. Freddie's Single Family Lending Senior Vice President Dave Stevens said that he expects in the next nine to 12 months that a significant share of the whole loans on the books of community banks would be either sold or securitized. "Freddie Mac is ready to help community banks restructure their balance sheets to increase liquidity after the refi boom." (*Freddie press release*, 5/20/03) Freddie can assist these community banks "swap out" of some of the \$300 billion in whole loans now held by community lenders at locked-in low interest rates, Stevens said. Some 2,400 institutions – including banks, savings and loans, and credit unions – hold these loans, he said. Freddie can either securitize the loans or resell them on the secondary market. (*BNA Daily Report for Executives*, Marcia Kass, 5/21/03) Stevens noted that a change of 25 to 50 basis points

upward in rates could cause damage and that an increase of 100 basis points would definitely hurt these depositories. “This is something you want to avoid,” he said, adding that community banks “should get ahead of the curve.” (*National Mortgage News*, 5/26/03)

- Stevens noted that there are several strategies that community banks can use, with the assistance of Freddie, regardless of the community banks’ overall strategy. Stevens noted that Freddie can assist community banks restructure their balance sheets. For instance, community banks can package a pool of loans of practically any size for sale to Freddie. Moreover, by choosing securitization, a banker may be able to reduce the amount of regulatory capital it has to hold. Freddie’s sales team can also assist community bankers with cash portfolio sales, loan level file reviews, due diligence and other services that give mortgage portfolio managers the information they need to make the most informed business decisions possible when considering a secondary market portfolio sale. For example, Stevens noted, by identifying loans that qualify for Community Reinvestment Act (CRA) credit, community bankers can elect to retain the mortgages they need to meet their own goals, and prepare the remaining mortgages for sale to other lenders than may need more CRA mortgages to meet their own community objectives. (*Freddie press release*, 5/20/03) Asked whether Freddie would benefit from a slight mark-up of these CRA-eligible loans, Stevens conceded that it would. “There is a business focus on this,” he said. (*BNA Daily Report for Executives*, Marcia Kass, 5/21/03)
- And for community banks that want to restructure their existing long-duration mortgage securities, Stevens said that Freddie’s REMIC program could help create securities with duration that better match banks’ liabilities. In other areas, Stevens said that Freddie can assist lenders with a range of products, including hybrid adjustable rate mortgages, to mortgages designed specifically to help more low- and moderate-income borrowers. (*Freddie press release*, 5/20/03)
- Freddie sees enormous potential in consolidating an otherwise fragmented secondary market among smaller community depository institutions, which generally have less than \$500 million in assets. Freddie officials cited Federal Reserve statistics that found small depositories collectively accounted for roughly \$300 billion in mortgages generated in 2002. (*Dow Jones Newswire*, Dawn Kopecki, 5/20/03)
- Freddie has signed key alliances over the last 16 months with America’s Community Bankers, Credit Union National Association, the American Bankers Association, and now the Independent Community Bankers of America (see next story), offering free portfolio management and securitization training to bank personnel. (*Dow Jones Newswire*, Dawn Kopecki, 5/20/03)

#### Freddie and ICBA sign alliance agreement

- The Independent Community Bankers of America (ICBA) and Freddie signed an agreement May 19 that gives ICBA member banks enhanced access to the secondary mortgage market through Freddie and specific products and services designed to help them reach more borrowers in their communities. The agreement gives ICBA members the tools to sell

mortgages to Freddie and leverage incentives, technology, training resources and capital markets expertise to grow their mortgage business.

- "This alliance provides ICBA members with easier access to the secondary market so they have the funds, mortgage products and technology tools to help meet the residential mortgage lending needs in their communities." said Dave Stevens, senior vice president for Single Family Lending at Freddie.
- Some specific features of the alliance include:
  - Guaranteed rural housing loan product that helps bankers reach more borrowers in rural communities and offers various funding options, no mortgage insurance and no down payment.
  - Affordable lending mortgage products to help bankers serve more low- and moderate-income borrowers and meet Community Reinvestment Act requirements.
  - Technology advantages using Freddie's Loan Prospector automated underwriting service, the Mortgagebot with Loan Prospector online lending solution and Freddie's servicing technology tools.
  - Customized, instructor led training sessions for numerous Freddie products and services.
  - Increased access to capital markets and portfolio management experts. (*ICBA/Freddie press release, 5/19/03*)

## **Federal Home Loan Banks**

FHFB Chairman Korsmo asks each FHLBank to meet with the SEC to discuss the FHLBanks' voluntary registration with the SEC

Korsmo continues to push to have all 12 FHLBanks voluntarily register with the SEC

FHLBanks of Cincinnati and Chicago have had meetings with the SEC

- FHFB Chairman John Korsmo wrote a May 9 op-ed for the *American Banker* urging each FHLBank to meet with the SEC to discuss the FHLBanks' voluntary registration with the SEC under the 1934 Securities Exchange Act.
- Korsmo said he has asked the 12 FHLBanks to meet with the SEC staff "to address whatever questions or concerns both sides might have about the FHLBanks joining Fannie Mae and Freddie Mac as voluntary registrants under the Securities Exchange Act of 1934. So far, two Banks have done so, and their executives told me the sessions were very valuable. The remaining Banks should now follow suit. By sitting down with the SEC staff to discuss voluntary registration, the Banks will serve their member institutions as well as taxpayers and the capital markets. An open discussion will address questions and misconceptions, while providing the SEC with a better understanding of the particular characteristics of the Federal

Home Loan Bank System.”

- Korsmo noted that the SEC and the Administration believe that the FHLBanks should join Fannie and Freddie as voluntary '34 Act registrants to ensure continued stability, resiliency, and growth in the mortgage finance and housing sectors. “In short, Fannie Mae and Freddie Mac now play by the rules for public securities issuers. So why not the FHLBanks?”
- “In July of last year, an expert hired by the FHLBanks warned of the consequences of differing disclosure regimes for the three housing GSEs...It is troubling that so many FHLBanks nonetheless resist engaging in serious discussions with the SEC about how Banks can voluntarily adopt the '34 Act standards accepted by their peers.” Korsmo concluded, “It is time that all FHLBanks accept that the size, sophistication, and role of their publicly endowed business monopolies require them to take up responsibilities not contemplated in 1932. We can begin by introducing the 12 FHLBanks to the SEC.” (*American Banker op-ed by FHFBC Chairman John Korsmo, 5/9/03; FHFBC press release, 5/9/03*)
- The Treasury Department and FHFBC Chairman Korsmo have been pushing the FHLBanks to comply with the same financial disclosure rules agreed to by Fannie and Freddie last July. Until recently, all 12 FHLBanks had been opposed to registering their stock with the SEC. However, in March, breaking ranks from the other 11 FHLBanks, the board of directors of the FHLBank of Cincinnati voted unanimously to begin registering its stock with the SEC. The SEC has called for greater financial disclosures by the FHLBanks and said that registration of FHLBanks' securities with the SEC would not impede the markets. HUD is undecided on whether the FHLBanks should register their stock with the SEC.
- In a May 8 e-mail to chairs and vice chairs of the FHLBanks, FHFBC Chairman Korsmo encouraged the FHLBanks to meet with the SEC to discuss voluntary registration under the '34 Act. Korsmo said, “I believe that good faith, results-oriented discussions between each Federal Home Loan Bank and the SEC will lead to successful resolution of issues of concern about voluntarily '34 Act registration that have been raised by the Banks.” Korsmo said in his e-mail that “it strikes me that the best way to avoid the supposed pitfalls of SEC registration is to determine whether those pitfalls are real or imaginary...And that determination can only be made after each Bank has conducted a direct, individual, no commitment meeting with the SEC staff aimed at satisfying itself as to whether or not real, insurmountable obstacles that would prevent voluntary registration under the '34 Act do or do not exist.” (*Dow Jones Newswire, John Connor, 5/9/03*)
- Korsmo noted that a committee of FHLBank presidents is scheduled to meet with the SEC soon, but said that “I am hopeful that meetings with individual Banks as potential registrants will follow quickly, because I believe that endless speculation serves no one's best interests.” To date, he said, only the FHLBanks of Cincinnati and Chicago have had meetings with the SEC of the sort he is advocating. (*Dow Jones Newswire, John Connor, 5/9/03*)

FHFB Chairman Korsmo would like to conduct a joint study with HUD to compare the affordable housing goals of Fannie, Freddie, and the FHLBanks

- FHFB Chairman John Korsmo would like to conduct a joint study with HUD to compare the affordable housing goals of Fannie, Freddie, and the FHLBanks. “HUD is quite receptive, but we have no final agreement yet,” a FHFB spokesman told *MortgageWire*. (*National Mortgage News Web site*, 5/7/03)

FHLBank of Atlanta to offer Mortgage Purchase Program (MPP), a competitor to Fannie & Freddie in the secondary mortgage market

FHLBank of Atlanta is the only FHLBank to offer the MPP and MPF programs to its members

FHLBanks should be allowed to securitize mortgages and compete more directly with Fannie & Freddie, says FHLBank of Atlanta President

- The FHLBank of Atlanta received approval from the FHFB to purchase loans under the MPP program. The FHLBank of Atlanta will continue to also purchase loans under the Mortgage Partnership Finance (MPF) program, which it has been doing for four years – making it the only one of 12 FHLBanks participating in both programs. FHLBank of Atlanta President Raymond Christman said he could not guess how the bank’s purchase volume would be allocated between the two competing programs but that approximately 150 members “are primary targets” to sign up for one of them. (*American Banker*, Marc Hochstein, 5/12/03)
- Christman thinks that some day the FHLBanks should be allowed to securitize mortgages and compete more directly against Fannie and Freddie. (*National Mortgage News Weekend Edition*, May 10-11, 2003)

FHLBank of New York joins the Council of FHLBanks

Council now represents 11 of the 12 FHLBanks

- The Board of Directors of the FHLBank of New York unanimously voted May 20 to join the Council of FHLBanks to strengthen the industry’s lobbying on Capitol Hill, reported Dawn Kopecki with *Dow Jones Newswire*. The FHLBank of New York was one of two holdouts, along with the FHLBank of Chicago, that refused to join the Council of FHLBanks, and instead, represent itself on Capitol Hill. With the addition of the FHLBank of New York, the Council now represents 11 of the 12 FHLBanks and more than 90% of the System’s assets. (*Dow Jones Newswire*, Dawn Kopecki, 5/20/03)

## FHFB names Anthony Cornyn as Senior Advisor in Office of Supervision

- Stephen M. Cross, director of the Office of Supervision at the FHFB, announced the hiring of Anthony “Tony” Cornyn as senior advisor. Cornyn’s duties will focus on market risk modeling and off-site monitoring of financial data from the 12 FHLBanks. From 1989 to 2002, Cornyn worked for the Office of Thrift Supervision, first as the Director of risk management (interest rate risk program) and then as the Director of risk management and industry analysis. Previously, he served as the Director of capital markets at the Federal Home Loan Bank Board and as an assistant director in the division of bank supervision at the Federal Reserve Board. (*FHFB press release, 5/6/03*)

## **Farm Credit Administration/Farmer Mac**

*Wall Street Journal* analyzes whether Gotham Partners’ research on Farmer Mac was correct

- One year ago, Gotham Partners Management Co. began making bearish bets on Farmer Mac, hiring publicists to press its case, retaining Washington lobbyists to promote its views, and creating critical research reports that were posted on the Web and sent to media organizations and the SEC. The comprehensive effort had one aim: to bring down the share price of Farmer Mac, reported Henry Sender with the *Wall Street Journal*. Gotham’s “trumpeting” of its research report showed a new zeal among hedge funds to press their views. New York State Attorney General Eliot Spitzer is investigating the firm’s Farmer Mac campaign in response to complaints from the GSE. “But lost amid the rancor is an important question: Was Gotham’s research correct?” The *Wall Street Journal* concluded that while the GSE has twice announced quarterly net-income results below expectations and the stock is down 44 percent since April 26, 2002 (just before Gotham’s campaign began), “Gotham’s most important conclusions don’t hold up very well under scrutiny.” For example, the “main prediction – that Farmer Mac would face a cash crunch that would cripple it – hasn’t happened and doesn’t look likely anytime soon.” As Gotham pointed out, the absolute level of Farmer Mac’s delinquencies are growing, however, at the same time, because the total book of loans by Farmer Mac and guarantees it had made on other farm lenders’ loans swelled 37 percent, the percentage of loans on which borrowers delayed making payments dropped to 1.54 percent from 1.7 percent.
- Gotham predicted that Farmer Mac had inadequate reserves for losses on its loan books and that by adjusting the reserves to more appropriate levels, most of the company’s book value would be wiped out, “making it subject to receivership and bankruptcy.” Gotham also noted that Farmer Mac’s reserves are less than those of comparable farm lenders, which the Journal noted might be true. However, while Farmer Mac’s reserving policy may be aggressive, it isn’t evident that establishing bigger reserves would produce a bankruptcy-court filing anytime soon, some Wall Street analysts noted. Gotham also predicted that Farmer Mac’s charge-offs would rise. “Technically, Gotham was correct: Charge-offs rose. But the

increase doesn't demonstrate the sort of financial stress the report predicted." (*Wall Street Journal*, Henry Sender, 4/11/03)

FCA asks for comment on whether to revise its regulations on credit for borrowers who farm, fish, or ranch

- The Farm Credit Administration (FCA) issued an advance notice of proposed rulemaking May 2 to consider whether to revise its regulations governing the eligibility and scope of financing for farmers, ranchers, or harvesters who borrow from Farm Credit System institutions that operate under titles I or II of the Farm Credit Act of 1971, as amended. The FCA is also considering whether to revise its regulatory definition of "moderately priced" rural housing. Comments are due by July 31, 2003. The FCA started the rulemaking in response to several petitions. FCA wants to know if the definition of a bona fide farmer, rancher, or aquatic producer should be changed and is investigating whether limits should be placed on lending for producers' other credit needs, and how access to these needs should be regulated. The FCA is scheduled to hold a public meeting June 26 on the rulemaking. (*BNA Daily Report for Executives*, Marcia Kass, 5/2/03; *Federal Register*, pages 23425-23427, 5/2/03)

## **Postal Service**

Postal Rate Commission (PRC) approves first negotiated service agreement (NSA) – the deal is the first time the Postal Service has offered reduced rates for just one customer

Agreement is between the Postal Service and Capital One

More agreements are expected to follow

- The PRC has approved the Postal Service's first NSA. The agreement is between USPS and Capital One, the Postal Service's fourth largest customer and the nation's largest producer of First-Class Mail. The PRC's opinion and recommended decision now goes to the Postal Service Governors for consideration. The Postal Service Governors are expected to consider the PRC's opinion in early June. (*PRC press release*, 5/15/03) The deal is the first time the Postal Service has offered reduced rates created for just one customer, but already postal officials have held talks with at least 10 other financial-services companies interested in their own arrangements. (*Wall Street Journal*, Rick Brooks, 5/20/03) "We've heard from every credit card company we can think of," said Mike Plunkett, the Postal Service's Manager of Pricing Strategy. (*American Banker*, W.A. Lee, 5/21/03)
- NSAs are targeted pricing initiatives to encourage greater efficiencies and to take advantage of the Postal Service's existing pricing flexibility. Under the agreement with Capital One, for the next three years the company is eligible for volume discounts if first-class bulk volume

exceeds 1.225 billion pieces. And, as part of the deal, the Postal Service will provide information on undeliverable first-class mail electronically rather than returning the actual mailpieces, reducing the Postal Service's processing costs. The agreement offers discounts ranging from three to six cents an item, increasing as Capital One's annual volumes increase. Capital One currently pays about 29 cents an item for each mailing. The Postal Service will avoid 20 cents for each piece it does not have to return. The Postal Service expects to avoid returning approximately 80 million mail pieces per year to Capital One during the course of the NSA. (*PRC press release, 5/15/03; Wall Street Journal, 5/20/03*)

- To assure that other mailers are not harmed by this arrangement, the Commission imposed a three-year limit of \$40.6 million on the total discounts Capital One is eligible to receive. The Commission said it could give "no reasonable assurance that the Postal Service will not lose money on the deal." (*PRC press release, 5/15/03; Wall Street Journal, 5/20/03*) "Because the evidentiary record contains no plausible estimate of the volume of first-class mail that Capital One would send during the term of the [agreement] if no discounts were made available, a significant risk exists that discounts to Capital One could exceed costs avoided by the Postal Service," the PRC said. "Under that circumstance, other mailers' rates would have to increase to make up the difference." (*BNA Daily Report for Executives, Derrick Cain, 5/21/03*) The PRC recommended the \$40.6 million cap, figuring that the Postal Service would save \$42 million over three years from Capital One's agreeing that letters with undeliverable addresses be returned electronically. Any similar arrangements with mass mailers would have to include the same provision, Plunkett said. (*American Banker, W.A. Lee, 5/21/03*)
- The PRC ruling sets the stage for the Postal Service to pursue NSAs with other mailers. "Numerous businesses are expected to seek to negotiate similar agreements," said PRC Chairman George A. Omas. "And the Commission will begin immediately to develop procedures to expedite this process." Some mailers expressed concern that future arrangements of this type could unfairly benefit one mailer over another. In the ruling, the PRC emphasized that the Postal Service had committed to extending like discounts to similarly situated mailers. (*PRC press release, 5/15/03*)
- The Direct Marketing Association said it was pleased that the PRC endorsed the basic concepts of the agreement and hoped it would lead to more system-wide use of such arrangements with the Postal Service. "I think it's great," said Gene Del Polito, president of the Association for Postal Commerce. "The USPS has made an agreement with a company that uses a lot of first class mail for its marketing and billing and I hope we see more." (*Direct, Larry Riggs, 5/15/03*)

Congressman Tom Davis (R-VA) says postal reform could move ahead if it had strong White House backing

Senator Susan Collins (R-ME) says Postal Service still faces serious problems

- Postal reform could move ahead provided it receives strong backing from the White House, Congressman Davis told attendees at the Direct Marketing Association's 2003 Government Affairs Conference. "If the White House is not willing to go with it, I just think it's going to be very difficult [to get a bill passed] on the Hill... Without them pushing it, without our leadership response to that, you're just not going to get Congress eager to make decisions [such as closing] post offices and to start angering interest groups." (*DM News*, Melissa Campanelli, 5/14/03) "We don't know what the [President's Postal] commission is going to say, or how serious the administration is going to be about tackling it," Congressman Davis said. "If the President says, 'I want this as part of my legacy,' we'll have a bill," he said. (*Direct*, Ray Schultz, 5/14/03)
- Congressman Davis was a key player regarding the Civil Service Retirement System legislation, recently signed by President Bush, which reduced the amount the Postal Service pays into the CSRS fund and enabled the Postal Service to avoid rate increases for three years. He noted, however, that there are several issues that need to be reopened. One was the question of what the Postal Service will do with its surpluses after 2006. Another is the requirement that the Postal Service pay for its employees' military retirement benefits. "No other agency in government is responsible for paying the military retirement for their [employees] under CSRS expect for the Postal Service," he said. The billions of dollars at stake could wipe out the Postal Service's debt, he added. Congressman Davis said he and Congressman Henry Waxman (D-CA) wanted to add an amendment to the CSRS legislation on the subject, but decided against it because they did not think the bill would have passed with the amendment. (*DM News*, Melissa Campanelli, 5/14/03; *Direct*, Ray Schultz, 5/14/03)
- Senator Collins acknowledged that a "perfect" postal reform bill is unlikely, given the many opposing groups. "We need a strong post office with universal service," she said. Senator Collins, Chairman of the Senate Governmental Affairs Committee, plans to conduct hearings on the President's commission's findings this fall. (*Direct*, Ray Schultz, 5/14/03) Senator Collins discussed the importance of the CSRS legislation but noted that the Postal Service still faces serious problems. "The Postal Service is mandated by law to break even, but the fact is [it] is simply not generating significant revenue to cover its operating expenses and its capital needs, both of which continue to grow," she said. Another problem is that the Postal Service is fast approaching its \$15 billion statutory borrowing plan," and that it faces "enormous unfunded liability, including the tune of nearly \$6 billion for workers comp, \$5 billion for retirement comp and as much as \$45 billion to cover retiree healthcare costs." (*DM News*, Melissa Campanelli, 5/14/03)

Seniors group joins CAGW and NTU in calling for FTC to investigate the Postal Service's ad campaign

- In a letter to the Federal Trade Commission (FTC), James Martin, President of the 60 Plus Association, urged the FTC to investigate the Postal Service's advertising campaign touting its Priority Mail as a "reliable '2-day' delivery service." The seniors group believes that the ads may be "misleading consumers and in particular seniors, as to the performance and value of Priority Mail as a 2-day service." Martin noted that the ads claim Priority Mail as comparable to "other 2-day services," which offer consumers a money-back guarantee. However, Martin pointed out that Priority Mail does not offer such a delivery guarantee and does not reliably achieve delivery within two days. "Seniors may be particularly vulnerable to deceptive advertising practices, especially when the ads are touting a government entity that they have come to trust over the years... With many seniors living on modest fixed incomes, coaxing seniors into spending nearly ten-times more to send an urgent letter via Priority Mail is a particularly egregious failing of the Postal Service's public responsibilities." (*The 60 Plus Association letter to FTC, 5/8/03*)
- The Council for Citizens Against Government Waste (CCAGW) [the lobbying arm of Citizens Against Government Waste] and the National Taxpayers Union April 18 called on the Federal Trade Commission (FTC) to investigate whether the Postal Service's promotions of its Priority Mail delivery service violate the nation's "truth in advertising" laws. CCAGW and NTU wrote letters to Mary Engle, the FTC's Associate Director in the Division of Advertising Practices, requesting the investigation. (*CCAGW press release, 4/18/03; NTU press release, 4/18/03*) Another watchdog organization, PostalWatch, released an April 18 study accusing the Postal Service of running ads that misrepresent priority mail as a 2-day delivery service. [See April 21, 2003 *GSE Report* for more information, [www.gsereport.com](http://www.gsereport.com)]

CAGW responds to latest developments in calls for the removal of the Postal Service's Inspector General (IG)

IG defends tactics, costs

- Citizens Against Government Waste (CAGW) Vice-President Leslie Paige released the following statement May 5 regarding reports that the Postal Service's Board of Governors does not plan to remove USPS IG Karla Corcoran from her position until it receives the results of an ongoing investigation being conducted by the President's Council on Integrity and Efficiency (PCIE):
- "According to one news report, the USPS Board of Governors has apparently decided to defer a decision on whether to replace Ms. Corcoran as USPS OIG until the Governors have an opportunity to review the PCIE's final report, which isn't expected until late May. However, CAGW calls upon the Board to put Ms. Corcoran on administrative leave until a

decision is made. There have been credible reports that Ms. Corcoran continues to abuse her authority and misuse her staff. For example, Friday, May 2, criminal investigators in the IG's office were told by the IG's management team, presumably under the supervision of Ms. Corcoran, to report to work armed and that their assignment for that day was to ensure that no media crews gained unauthorized access to the building. They were told to have any unauthorized media personnel removed from the building if they refused to leave. This behavior borders on the bizarre. The IG's criminal investigators are professional law enforcement officers whose job it is to investigate waste, fraud and mismanagement and make cases. They are not Ms. Corcoran's personal security force, nor do their job descriptions include protecting the building from the media. Ms. Corcoran has a fully-staffed public affairs and media department to handle media inquiries.”

- “CAGW continues to be concerned about mismanagement and abuse in Ms. Corcoran's office, particularly the treatment of whistleblowers who continue to work in the IG's office. It is not clear whether the dozens of employees who are cooperating with both the PCIE and Sen. Charles Grassley's (R-Iowa) investigation are eligible for whistleblower protection under either the Whistleblower Protection Act or the Inspector General Act. Ms. Corcoran and her entire management team ought to be placed on administrative leave and a credible acting IG should be brought in from another federal law enforcement or IG office in order to prevent any retaliation against employees and to begin to restore some semblance of professionalism in the USPS IG's office. Such a decision would also prevent any further misuse of personnel and IG funds pending a final outcome of the PCIE investigation.” (*CAGW press release, 5/5/03*)
- As noted in the May 5, 2003 *GSE Report*, Senators Byron Dorgan (D-ND) and Ron Wyden (D-OR) called on the Postal Service's Board of Governors to fire Inspector General Karla Corcoran, saying she has frivolously spent her office's funds rather than weeding out waste in the Postal system. (*Wall Street Journal, Sarah Lueck, 5/1/03; Senator Dorgan and Wyden letter to Postal Service Board of Governors Chairman David Fineman, 5/1/03*) The Postal Service's Board of Governors told Senators Wyden and Dorgan that it would not consider removing Corcoran until it received a government report on the issue in late May. (*BNA Daily Report for Executives, Derrick Cain, 5/5/03*) Corcoran has also been under investigation by Senator Chuck Grassley (R-IA) and the President's Council on Integrity and Efficiency (a panel of presidentially appointed IGs) since last October. Senator Grassley, however, has not yet joined his colleagues' call for Corcoran's resignation and is awaiting the results of the investigations before taking any course of action. (*The Washington Times, James Lakely, 5/3/03*) Corcoran's seven-year term ends in January. She has indicated that she will not seek another term. (*Washington Post, Christopher Lee, 5/27/03*)

#### IG defends tactics, costs

- Corcoran accused Senator Grassley of unfairly disclosing details of his investigation to the media. “He has not waited to get all the facts,” Corcoran, who faults disgruntled employees, said in a recent interview with the *Washington Post*. “I'm an open book. The thing that concerns me is that I'm being tried in the media.” Corcoran defended her management style, saying that her controversial “team-building” exercises helped to build trust and morale and

identify employees' strengths. Her approach, unusual for government, is common in some private companies, she said. "We've done a lot of things very, very differently," she said. "I would say that 75 to 80 percent of the people here are really concerned because they think that this is an agency that...is the best agency they've ever seen...Now it's being pulled down not by legitimate issues but by reports in the press" and by detractors. An aide for Senator Grassley stated, "We don't mind different. We just mind different in the sense that it detracts from what you are supposed to be doing." (*Washington Post*, Christopher Lee, 5/27/03)

"Has the traditional USPS productivity slide begun again?" asks the Lexington Institute

- In a Lexington Institute briefing paper, former Postal Service economist Charles Guy stated, "There are troubling signs in the Service's most recent public financial data (covering the period from February 22 to March 21) that seem to show that Postal Service productivity is slipping backward once again. Spending for supplies and services, the largest non-labor cost aside from transportation, which includes contract support, advertising and building maintenance, declined only 0.3 percent in this period, and is down only 9.6 percent year-to-date. These expenditures declined 18.6 percent during FY 2002."
- Guy added, "Recent productivity gains, of 3.4 percent for the 2001-2002 period and 3.8 percent through the second quarter of 2003, were achieved, once again, by labor force attrition and delayed expenditures for supplies and services. Now that the financial pressure on the Postal Service has been temporarily reduced, the significant slippage in the most recent data could be the first signal of the Service's traditional productivity givebacks."
- Guy concluded, "The Postal Board of Governors...must pursue an active role to see that productivity gains are the result of meaningful plans to achieve sustainable labor force reductions. Spending reductions must be planned as permanent changes in operations, not merely expenditure delays, if they are to have lasting value." (*Lexington Institute Issue Brief*, Charles Guy, 5/13/03)

Presidential Postal Reform Commission to hold next meetings May 28-29 in Washington, DC

Commission expected to hold two more meetings prior to releasing its report on July 31

- The Presidential Postal Reform Commission will hold two days of public meetings on Wednesday, May 28 and Thursday, May 29 at the Hart Senate Office Building (Room 216) in Washington, DC. (*President's Commission on the US Postal Service web site*) The Commission has posted several papers requested by the Commission and its subcommittees on its web site (<http://www.treas.gov/offices/domestic-finance/usps/documents.html>) The Commission has also posted several consulting report projects prepared on behalf of the Commission on its web site (<http://www.treas.gov/offices/domestic-finance/usps/projects.html>)

- The Commission is expected to hold two more meetings before July 31 – the date the Commission is expected to release its recommendations for the Postal Service. (*BNA Daily Report for Executives*, Derrick Cain, 5/9/03)

AEI holds April 30 session on Postal reform as part of its Postal Reform Initiative

Future session to be held June 2

AEI also releases two papers on postal reform

- AEI is sponsoring a Postal Reform Initiative – a series of conferences and publications to assess the mission and operations of the Postal Service, propose a vision of a modern postal industry, and suggest how the US could arrive at this destination. President George W. Bush recently established the Commission on the United States Postal Service, whose final report in August 2003 may lay the groundwork for the first major reform of the U.S. Postal Service in thirty years. Mirroring the administration's initiative, AEI is sponsoring its own Postal Reform Initiative. The Initiative, led by Rick Geddes, an AEI adjunct scholar, parallels the work of the Presidential Commission. The March 17 opening session of the Initiative discussed key objectives that the President's Postal Reform Commission should strive for and how those objectives can be realized. AEI held its second session on April 30 to focus on the mission of the Postal Service, how technology has affected this mission, and the meaning of universal service.

#### Michael Crew, Rutgers University

- Crew noted that although there are advantages to the Postal Service's universal service obligation (USO), such as creating brand name recognition and economies of scale, the associated costs and obligations present a burden. For example, postal offices cross-subsidize between high-cost and low-cost routes, and without some form of protection (such as regulatory intervention), postal offices will be subject to competition along the low-cost routes, leaving them with insufficient revenue to support the high-cost routes. A regulatory framework could administer the USO by balancing the rights of the customers and competitors while protecting the obligation to serve. Contrary to popular belief, privatization and the USO are not necessarily inconsistent, as evidenced by privatization efforts in the Netherlands and Germany, which did not adversely affect universal service. However, whether the USO is worth retaining at all remains an open question. (*Summary of AEI April 30 Postal Reform session*, <http://www.aei.org/events/eventID.277/summary.asp>, AEI intern Adelene Tan) A copy of Crews' remarks may be found online at: [http://www.aei.org/docLib/20030421\\_Crew.pdf](http://www.aei.org/docLib/20030421_Crew.pdf)

#### Damien Geradin, Harvard University

- The European Union began liberalizing its postal services many years ago, a process which is still in progress. The European Union's reasons for liberalizing its public monopolies, including the postal service, include: (1) poor performance of its monopolies; (2) industry pressure; (3) incompatibility of monopoly rights with the European single market; and (4)

successful market-opening reforms in some member states (e.g., Great Britain and Sweden). The obstacles to postal liberalization in the European Union include: (1) opposition of some public postal operators to reform themselves; (2) highly unionized and thus politicized sector; (3) fear that market-opening reforms will lead to major job losses; and (4) fear that liberalization will have a negative impact on universal service. The future of postal workers is a sensitive political issue and the potential threat to the employment of large numbers of civil-service employees has slowed liberalization in some countries. Postal employees' wages represent a large proportion of the total cost of the USO, and member states that have liberalized their postal services report that, once modern technology has been implemented to improve efficiency and productivity, post-liberalization wages form a smaller proportion of the total cost of the USO compared to pre-liberalization wages. Some challenges faced by the European postal sector in liberalization include substitution caused by increasing reliance on e-mail services, limited development of e-commerce relative to the US, failed strategies of diversification, and labor movement. (*Summary of AEI April 30 Postal Reform session*, <http://www.aei.org/events/eventID.277/summary.asp>, AEI intern Adelene Tan) A copy of Geradin's remarks may be found at: [http://www.aei.org/docLib/20030429\\_Geradin2.pdf](http://www.aei.org/docLib/20030429_Geradin2.pdf)

#### Robert Cohen, United States Postal Rate Commission

- The core meaning of universal service is ubiquity, where everyone receives mail and has reasonable access to collection and counter service. The cost of universal service is the cost of those services that would not be provided in a competitive market.
- Some speculation about which services may be eliminated to increase the efficiency of the Postal Service are:

#### Core Elements:

1. Eliminate unprofitable delivery routes.
2. Close many small post offices.
3. Abandon Alaska Air subsidy.
4. Curtail expansion of delivery network.

#### Non-core Elements:

5. Reduce number of delivery days.
  6. Convert park and loop routes to curb routes.
- Potential savings from core universal service elements could reach \$3.12 billion, or 5 percent of total cost. Potential savings from non-core universal service elements would be as much as \$3.36 billion, or an additional 5.3 percent of total cost. Inefficiencies that plague the Postal Service include a high wage premium (12 to 20 percent of total cost), overstaffing, the ease of implementing rate increases that exceed the rate of inflation, and low productivity increases (only 9.2 percent from 1970 to 1999). As illustrated by Germany, Great Britain, New Zealand, and Sweden, liberalization reduces inefficiencies. Work forces in those countries were reduced by between 15 and 40 percent after liberalization. (*Summary of AEI April 30 Postal Reform session*, <http://www.aei.org/events/eventID.277/summary.asp>, AEI intern Adelene Tan) A copy of Cohen's remarks may be found at:

[http://www.aei.org/docLib/20030429\\_Cohen.pdf](http://www.aei.org/docLib/20030429_Cohen.pdf) A copy of Cohen's Draft April 28, 2003 paper on "*The Cost of Universal Service in the US and its Impact on Competition*," can be found at: [http://www.aei.org/docLib/20030429\\_Cohen2.pdf](http://www.aei.org/docLib/20030429_Cohen2.pdf) A copy of Cohen's February 2001 paper, "*The Impact of Using Worksharing to Liberalize a Postal Market*," can be found at: [http://www.aei.org/docLib/20030428\\_impact.pdf](http://www.aei.org/docLib/20030428_impact.pdf)

Third session to be held June 2 on competition in the postal industry

- AEI is holding a June 2 session to examine competition in the postal industry. In order to solve the problems that have bedeviled the U.S. postal industry, AEI plans to examine the potential of modern communications technology and a more open and competitive market environment and review the experiences of other countries that have enacted postal reform in recent years. With last year's U.S. court decision finding that the U.S. Postal Service is subject to federal antitrust law, the USPS can no longer claim sovereign immunity to defend itself from accusations of anticompetitive behavior. This third session of AEI's Postal Service Initiative will focus on the antitrust (or competition) issues that may arise under postal reform. (*AEI invitation for June 2 session*)
- The following is the schedule for the June 2 session:
  - 9:30 a.m. Registration
  - 10:00 Introduction: Rick Geddes, Cornell University
  - Speakers: Bill Kovacic, Federal Trade Commission  
David Sappington, University of Florida  
J. Gregory Sidak, AEI
  - Moderator: Rick Geddes, Cornell University
  - 11:00 Discussion
  - 12:00 Adjournment
- To register for the session: [http://www.aei.org/events/eventID.325,filter./event\\_detail.asp](http://www.aei.org/events/eventID.325,filter./event_detail.asp)  
(*AEI notice for June 2 session*)

AEI also releases two papers on postal reform (Geddes and Sidak)

Rick Geddes, Cornell University

- AEI released the second issue of AEI's Postal Reform paper by Rick Geddes on April 29 – "*The Structure and Effect of International Postal Reform*." The complete paper and summary can be found online at: [http://www.aei.org/include/pub\\_print.asp?pubID=17066](http://www.aei.org/include/pub_print.asp?pubID=17066)
- Geddes reviewed the effects of postal reform in several countries, which provides several lessons for postal reform in the US. First, substantial reform has taken place in many other countries, which indicates that meaningful reform in the US is politically feasible and in concert with other countries' policies. Second, postal reform has typically included a major change in the delivery monopoly, either through its outright elimination or through price limits on the scope of reserved service, usually defined as multiples of the stamp price. Indeed, it does not appear that any country has privatized, without also eliminating or limiting

its postal monopoly. Third, reform has frequently involved important changes in the universal service obligation. Many governments have removed the burden of providing universal delivery service from the postal service itself and shifted it to another entity, such as the regulator. Fourth, postal reform in some countries has included changes from government to private ownership, and sales of equity to the public have been successful, and have resulted in modern, dynamic, commercially oriented postal services. Finally, preliminary evidence suggests that international postal reform has had positive effects. There is no evidence of price spikes, and some postal services have even lowered their basic postage rate. Although labor relations have been problematic in some countries, many posts were able to reduce their workforces without major layoffs, instead relying on attrition. (*The Structure and Effect of International Postal Reform*, Summary, Rick Geddes, 4/29/03)

J. Gregory Sidak, AEI

- If postal reform is to proceed incrementally in the form of an improved government agency, Sidak identifies two broad goals for postal reform that must be adopted. “The first is to define the Postal Service’s mission in terms of remedying conditions of market failure. This goal encompasses universal service, quality of service, and reasonableness of rates. The second broad goal is to avoid competitive distortions through the pricing and product offerings of the Postal Service. This goal entails avoiding government production in markets that are or can be served satisfactorily by private firms, as well as avoiding discrimination among mailers and among competitors in secondary markets.” Sidak then makes specific recommendations that will advance these two broad goals. Those recommendations include costing, universal service, rate design and mail classification, the postal monopoly, and market entry and exit. (*Improving the US Postal Agency as a Public Service Government Agency*, J. Gregory Sidak, AEI, May 2003) A complete copy of the paper can be found at: [http://papers.ssrn.com/sol3/delivery.cfm/delivery.cfm/SSRN\\_ID397080\\_code030513560.pdf?abstractid=397080](http://papers.ssrn.com/sol3/delivery.cfm/delivery.cfm/SSRN_ID397080_code030513560.pdf?abstractid=397080)

Government Reform Subcommittee holds hearing on anthrax at postal facilities

Scientists recommend anthrax retests for post offices

- The National Security, Emerging Threats and International Relations Subcommittee of the House Government Reform Committee held a May 19 hearing titled “Stamping Out Anthrax in USPS Facilities: Technologies and Protocols for Bioagent Detection.” (*CQTodayDaybook*, 5/19/03)
- Witnesses on the first panel included: Keith A. Rhodes, chief technologist, General Accounting Office; Robert G. Hamilton, director, Dermatology, Allergy and Clinical Immunology, Johns Hopkins University; Colonel Erik A. Henschel, commander, US Army Medical Research Institute of Infectious Diseases. (*CQTodayDaybook*, 5/19/03)
- Witnesses on the second panel included: Thomas G. Day, vice president of engineering, US Postal Service; William Burrus, president, American Postal Workers Union; Captain Kenneth

Martinez, engineer, Centers for Disease Control and Prevention; James L. Hadler, chief epidemiologist, Department of Public Health, State of Connecticut; R. Davis Layne, deputy assistant secretary, Occupational Safety and Health Administration. (*CQTodayDaybook*, 5/19/03)

- The GAO's chief technologist, Keith Rhodes, told the Subcommittee that the Postal Service should retest as many as 261 post offices nationwide for anthrax. The post offices that should be retested are "those facilities deemed free of anthrax based on a single dry swab," said. "That's the least effective form" of testing, he said. While no one should assume that there is anthrax in those facilities, "we really don't know whether those facilities are clean," said Dr. Richard Hamilton, Johns Hopkins University. (*Associated Press*, 5/19/03; *FederalTimes.com*, Stephen Losey, 5/20/03)
- In 2001 postal officials tested a mail facility in Wallingford, CT with dry cotton swabs and no contamination was found. However, when the Centers of Disease Control and Prevention tested the facility using wet wipes and a high-efficiency particulate air vacuum, it found more than 3 million anthrax spores. Levels between 8,000 and 10,000 spores are considered harmful. Postal officials said they did what they could to protect their workers and customers. (*Associated Press*, 5/19/03)
- Rhodes and other experts also recommended at the hearing that the Homeland Security Department take the lead in bioterror response in order to avoid confusion and ineffectual tests such as those performed in Connecticut. Having one agency in charge of bioterror response would let it set standards for anthrax testing and other biological weapons, said Robert Hamilton, Johns Hopkins University. (*FederalTimes.com*, Stephen Losey, 5/20/03)
- Postal spokesman Gerry Kreienkamp said agency officials are evaluating recommendations offered at the hearing. (*FederalTimes.com*, Stephen Losey, 5/20/03)
- An April 2003 GAO report recently criticized the Postal Service for delaying anthrax test results to employees. The report found that Postal Service officials violated Occupational Safety and Health Administration rules and undermined the credibility of management when they delayed the report of anthrax test results to employees at the contaminated mail facility in Wallingford, CT. (*Washington Post*, Christopher Lee, 4/22/03) See May 5, 2003 *GSE Report* for more information on the GAO report, [www.gsereport.com](http://www.gsereport.com)) The *GAO Report*, "US Postal Service: Better Guidance is Needed to Improve Communication Should Anthrax Contamination Occur in the Future," (GAO-03-316, April 2003) can be found online at: [www.gao.gov/cgi-bin/getrpt?GAO-03-316](http://www.gao.gov/cgi-bin/getrpt?GAO-03-316)

Postal Service offers online bill payment for businesses
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- The Postal Service is now offering its business customers a new online service – USPS Online Payment Services™ Business Edition – which allows usps.com users to electronically make bill payments to those they would ordinarily send checks. The service is offered in partnership with CheckFree Corporation. Subscribers to USPS Online Payment

Services™ Business Edition can enter invoice information- including adjustments and credits – to be sent along with their bill payments. They can also set access privileges for multiple employees. Additional features include the ability to schedule recurring payments for fixed amounts and to receive electronic bills from credit card, insurance, and utility companies. (*USPS press release, 5/15/03*)

#### Postal Service merges customer care centers

- The Postal Service expects to save up to \$137 million over a decade with an integrated customer care management network that it plans to complete by the end of the year, a Postal Service project manager said. The new system merges seven customer contact centers into two and provides a toll-free, one-stop number for all postal information. It is part of a cost reduction effort mandated by the deputy postmaster general in April 2001. Covergys Corp. of Cincinnati will automate the customer relationship management portion of the Postal Service's online and phone transactions with customers. The contract, awarded in January, has a potential value of \$700 million over 10 years. (*Government Computer News, 5/14/03*)

### **TVA**

#### TVA's inspector general appointed for the first time by the president

- Richard Moore was sworn in Friday, May 9, as TVA's first Presidentially appointed Inspector General. The Senate on May 1 confirmed the appointment of Moore. TVA's Inspector General is independent and subject only to the general supervision of the TVA Board. Moore previously served as Assistant US Attorney in the southern district of Alabama and was the Anti-Terrorism Task Force Coordinator in the district. Senator Jeff Sessions (R-AL) recommended Moore to President George W. Bush. TVA's board traditionally chose the agency's inspector general. Senator Bill Frist (R-TN) and then-Senator Fred Thompson (R-TN) successfully pushed legislation to create greater independence for the TVA inspector general by making the office an appointee of the president instead of the board of the agency the IG is supposed to monitor. (*Associated Press, 5/2/02; TVA news, 5/14/03*)

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