

The **GSE** REPORT™

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Major Events

Subprime mortgage market in the news:

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key terms in mortgage disclosures

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Federal Reserve holds hearing on subprime mortgage practices

- On June 14th, the Federal Reserve held a nearly eight-hour hearing on the agency's authority to curb abusive mortgage lending, just a day after the Fed was vilified in a House Financial Services Committee meeting for “standing by” while millions of consumers took out loans that they did not understand or could not repay. Federal Reserve Governor Randall Kroszner, acting as moderator for the Fed hearing, maintained his neutrality on the issues discussed, as he and other agency representatives asked a wide range of questions to lenders and consumer activists on escrow accounts, prepayment penalties, and low-documentation and no-documentation loans. Noting that regulators “must walk a fine line” between curtailing unfair practices and preserving legitimate lending business, Kroszner said, “We must determine how we can help to weed out abuses while also preserving incentives for responsible lenders.” He noted that while improved information disclosures for consumers might alleviate some of the problems in the mortgage market, “we also recognize that disclosures may not always be sufficient to combat abusive practices.” Kroszner added, “Because some bad lending practices may require additional measures, the Federal Reserve will seriously consider how we might use our rulemaking authority to address abusive practices without restricting consumers' access to beneficial financing options and responsible subprime credit.”

- At the hearing, industry executives urged the Fed not to limit the availability of credit by over-reacting to problems in the subprime mortgage market and urged the central bank to consider issuing agency guidance rather than bright-line regulatory prohibitions on non-traditional mortgage practices, while consumer advocates argued the agency should have cracked down abusive mortgage practices years ago and argued that providing guidance to only regulated banks creates loopholes that private market entities can exploit. With regard to the use of debt-to-income ratios in making underwriting decisions, Susan Davis, executive vice president for national consumer lending at Wells Fargo Home Mortgage, argued, “This is an area where guidance is more appropriate than bright-line rules. The board should avoid any rulemaking that unnecessarily limits availability of innovative lending products. [The Fed] should allow the market to make necessary corrections, and should not overreact to a current wave of concern.” With regard to requiring mortgage escrows, Martin Eakes, CEO for the Center for Responsible Lending, argued, “Guidance will not work here. Voluntary will not work here. You cannot have it both ways. Guidance is most effective when you are a bank regulator that has supervision over the institution ... If it doesn’t apply to all lenders, then the lenders that do not escrow will win the marketplace because it is deceptive and borrowers will be told we have a payment that is 20 percent lower than the responsible lender next door.” (*Reuters*, 06/13/07; *Associated Press*, 06/15/07; *American Banker*, Steven Sloan, 06/15/07; *Dow Jones Newswires*, Benton Ives-Halperin and Elizabeth Price, 06/14/07; *Bureau of National Affairs*, Richard Cowden, 06/15/07)
- The hearing came a day after House Financial Services Committee Chairman Barney Frank (D-MA) said that the Fed had not done enough to protect consumers. He also expressed doubt about Kroszner’s “consumer-friendly credentials.” [In testimony, Kroszner argued that the Fed can best address problem practices through case-by-case enforcement action and warned that regulatory action runs the risk of unintended consequences.] Frank told Kroszner, “You reinforce my position that the Fed is not the best place for consumer protection.” Frank added, “I just want to put you on notice. If the Fed doesn’t start to use that [HOEPA] authority, then we will give it to somebody who will use it....Use it or lose it.” Senate Banking Committee chairman Chris Dodd continued his criticism of the Fed, accusing the agency of “foot-dragging” and urging the agency to act quickly. Dodd said, “The Federal Reserve has a clear duty ... to extend substantive protections to subprime borrowers, as my colleagues and I have outlined numerous times.” (*American Banker*, Steven Sloan, 06/15/07; *Reuters*, John Poirier, 06/13/07; *American Banker*, Cheyenne Hopkins and Stacy Kaper, 06/14/07; *Bureau of National Affairs*, R. Christian Bruce, 06/14/07)
- In conversations with Federal Reserve chairman Ben Bernanke, Frank said he has found some measure of “theoretical accord” with Bernanke on how problems in the mortgage market might be addressed by legislation. “I was pleasantly surprised at the extent to which we have some general agreement on what to do going forward, including legislation that restricts [loan] originations and has assignee liability as long as it is very carefully and restrictively written,” said Frank. Consumer advocates are

calling for a suitability standard through which lenders could be punished for making loans deemed inappropriate for a given borrower. In turn, bankers argue that such a suitability standard would be impossibly vague from a compliance standpoint. Frank suggested in his conversation with Bernanke, “You don’t say ‘suitable.’ You say what you mean by ‘suitable.’” Legislation could address liability for assignees in a similar manner, said Frank. “You give them some specific things they have to do, and they do them, they’re ok,” he said. While the Fed chief didn’t lend support to any particular approach, Frank cited only a measure of agreement from Bernanke from a conceptual standpoint. (*Bureau of National Affairs*, R. Christian Bruce, 06/14/07)

- In a June 5th speech to the 2007 International Monetary Conference, Chairman Bernanke said that the decline in the real estate market which started last year “appears likely to remain a drag on economic growth for somewhat longer than expected.” He added, residential construction will likely remain “subdued for a time” until builders reduce their inventory of unsold new homes. “We have not seen major spillovers from housing onto other sectors of the economy,” observed Bernanke.
- To address specific problems in the subprime mortgage market, Bernanke said that the central bank is “evaluating what actions may be needed to prevent the recurrence of these problems. ... We have also used, and will continue to use, supervisory guidance to help mitigate problems in nonprime lending. Last year, together with other federal banking regulators, we issued guidance concerning so-called nontraditional mortgages. We have also issued draft supervisory guidance concerning underwriting standards and disclosures for subprime mortgages. The agencies are now reviewing the many responses to the draft proposal.”
- “The patchwork nature of enforcement authority in subprime lending poses a special challenge. For example, rules issued by the Board under HOEPA apply to all lenders but are enforced--depending on the lender--by the Federal Trade Commission, state regulators, or one of the five federal regulators of depository institutions. To achieve uniform and effective enforcement, cooperation and coordination are essential. We are committed to working closely with other federal and state regulators to ensure that the laws that protect consumers are enforced. Together with other regulators and the Congress, we have much to do and many issues to consider. We undertake that effort with utmost seriousness because our collective success will have significant implications for the financial well-being, access to credit, and opportunities for homeownership of many of our fellow citizens.” (*Federal Reserve Press Release*, Remarks by Chairman Ben S. Bernanke, 06/05/07)

FTC study concludes many borrowers fail to understand key terms in mortgage disclosures

- A June 13th Federal Trade Commission staff report concludes that current mortgage disclosures do not “convey key mortgage costs and terms to many consumers” and improved disclosures can be created to help consumers understand their mortgage.

Through a study based on 36 in-depth interviews with recent mortgage customers and testing of prototype disclosure forms with 819 mortgage customers, the study concluded that improved disclosures will not only facilitate customers' understanding but also will enable the customers "to make informed decisions about mortgage products." The study concluded that (1) current mortgage cost disclosures failed to convey key mortgage costs to many customers; (2) prototype disclosures developed for the study significantly increased the customers' recognition of mortgages costs; (3) prime and subprime borrowers failed to understand key mortgage terms used in current disclosures and benefited from improved disclosures; and (4) improved disclosures provided the greatest benefit to more complex loans in which prime and subprime borrowers had the most difficulty in understanding loan terms. The executive summary and full staff report is available at the Commission's website [<http://www.ftc.gov/opa/2007/06/mortgage.shtm>]. (*Bureau of National Affairs*, Cecelia M. Assam, 06/14/07)

Chairman Frank wants loan servicers to be flexible in working with troubled subprime borrowers

- On June 13th, House Financial Committee chairman Barney Frank (D-MA) said he is working with the FASB, the SEC, and Senate Banking Committee chairman Chris Dodd (D-CT) on tax rules to help subprime borrowers obtain more affordable mortgages and making certain that lenders do not suffer adverse accounting ramifications. Frank told reporters that he is negotiating with House Ways and Means Committee chairman Charles Rangle (D-NY) about tax consequences which can be triggered when borrowers' subprime mortgages are restructured into more affordable mortgages, which allows the borrowers to avoid early repayment penalties. While he did not elaborate on his discussions with the SEC or FASB, Frank said he hopes for an outcome that would "take real economic interest into account." (*Bureau of National Affairs*, R. Christian Bruce, 06/14/07)
- The Financial Accounting Standards Board has scheduled a closed-door meeting to discuss the restructurings of troubled subprime mortgages in MBS and their impact on FAS 140. Representatives from the federal banking agencies, the SEC, the IRS, the big four accounting firms and the mortgage industry have been invited to attend the meeting. (*National Mortgage News' MortgageWire*, 06/07/07)

The media template: Fannie and Freddie are cashing in on subprime fallout

- Articles appearing in the *International Herald Tribune* (June 6th), *Associated Press* (June 7th), and *American Banker* (June 8th) all had a common theme: Fannie Mae and Freddie Mac are riding to the rescue of the subprime mortgage market (and enriching their shareholders too). In a *Bloomberg News* article appearing in the *International Herald Tribune*, Jody Shenn and James Tyson wrote, "Fannie Mae and Freddie Mac, once derided as white elephants in the mortgage market, are benefiting from the subprime debacle and trampling just about anything in their way." Some of the articles may have been triggered, in part, by a recent analyst report issued by

Friedman, Billings, Ramsey & Co., which concluded that the subprime market turmoil may help Fannie and Freddie regain some of their former status as mortgage market leaders. FBR analyst Paul Miller wrote, “It is unlikely that Fannie and Freddie will ever regain the power, profitability, and influence that they enjoyed in the U.S. mortgage market in early 2000.” He added that “friendlier political skies” and the lessening likelihood of passage of GSE regulatory reform in 2007 or 2008 led Miller to boost Fannie Mae’s target share price to \$85 and upgrade the GSE to “outperform” from “marketperform.” (*International Herald Tribune/Bloomberg News*, Jody Shenn and James Tyson, 06/06/07; *Associated Press*, Danielle Reed, 06/07/07; *American Banker*, William Launder, 06/08/07)

- In a June 11 speech, OFHEO director James B. Lockhart, III said that Fannie Mae and Freddie Mac currently own \$170 million of subprime mortgage-backed securities. “Both are expanding efforts to avoid foreclosure,” said Lockhart. (*Bloomberg*, James Tyson, 06/14/07)

Well, why not?

- *American Banker* points out this “quotable”: ““The key question is, why can’t you refinance into a 30-year fixed? If you have been a borrower [who’s] been making payments at the starter rate, why can’t you just put them into a fixed rate **at that rate?**” [Emphasis added] — Sheila Bair, chairman of the Federal Deposit Insurance Corp., on modifying adjustable-rate loans...” at the American Securitization Forum in New York on June 6th. Bair also told attendees that regulators will sign off on final guidelines for underwriting and marketing subprime mortgages later this month and called for a national standard to address abusive prepayment penalties and the use of “stated income loans.” (*American Banker*, Kate Berry and Harry Terris, 06/14/07; *Dow Jones Newswires*, Emily Barrett and Anusha Shrivastava, 06/06/07)

CDO boom masked subprime losses, abetted by S&P, Moody’s and Fitch

- On December 12, 2000, Credit Suisse Group sold a \$340.7 million collateralized debt obligation to investors with an investment grade rating on 95% of the securities in the CDO. Investors discovered the hard way –through losses—that the CDO was loaded with junk bonds and subprime mortgage loans. By December 31, 2006, \$125 million of the CDO’s underlying securities defaulted, causing investors to lose more than 35% of their original investment—a far cry from the 10% return promised by Credit Suisse. The uncharted slide of Credit Suisse’s CDO illustrates the critical and little understood role played by rating companies, who serve as de facto regulators in a market with no “official” watchdogs and little, if any, transparency.
- Rating agencies also play an active and integral role in putting together the CDOs, which over the last three years have grown fivefold to \$503 billion (in 2006). According to Charles Calomiris, the Henry Kaufman professor of financial institutions at Columbia University in New York, credit raters participate in every level of packaging a CDO. “It’s important to understand that unlike in the corporate

bond market, in the securitization market, the rating agencies run the show,” said Calomaris. “This is not a passive process of rating corporate debt. This is a financial engineering business.”

- According to data from Moody’s and Morgan Stanley, subprime mortgages comprised about \$100 billion (or 27%) of the \$375 billion of CDOs sold in the United States in 2006. In certain classes of CDOs, the concentration of subprime mortgages is even higher. According to S&P and Fitch, subprime mortgage securities make up more than 70% of mezzanine asset-backed CDOs. In 2006, Morgan Stanley estimates that investors bought \$59.5 billion of these CDOs. On average, more than 90% of these mezzanine asset-backed CDOs were rated investment grade. Investors have little idea how “toxic” some of these CDOs are, said Joseph Mason, a finance professor at Philadelphia’s Drexel University. “We compose CDOs with a bunch of this stuff,” said Mason. “Now we just jack up the risk, jack up the misunderstanding. We’re throwing our money to the wind. We now know the defaults are in the mortgage pools and it’s only a matter of time before they accumulate to levels that will threaten the CDO market.”
- The three leading credit rating agencies claim that policing the CDOs isn’t their job. Moody’s senior managing director Noel Kirnon, said that their CDO ratings are merely educated opinions. S&P tells investors in their published CDO ratings not to base investment decisions on the agency’s analysis. Similarly, Fitch says that its analyses are just opinions and should not be relied upon when making CDO investment decisions.
- The CDOs have been a financial bonanza for the rating agencies with structured finance being the largest and fastest growing source of credit rating revenue. Given the complexities of CDOs, the agencies charge as much as three times more to rate these instruments than to analyze bonds. For example, Moody’s reported \$1.52 billion in revenue for credit rating in 2006, with structured finance accounting for 44% (or \$667 million) of total revenue and other credit ratings accounting for 32% (or \$485 million). “CDOs are the cash cow for rating agencies,” says Frank Partnoy, a former bond trader, now a University of San Diego law professor. “They’re clearly a gold mine. Structured finance is making a lot of Moody’s shareholders and managers wealthy.”
- CDO ratings may mislead investors because they can obscure the risk of default, particularly when compared with similarly rated bonds. Said Darrell Duffie, a finance professor at Stanford Graduate School of Business. “You can’t compare these CDO ratings with corporate bond ratings,” said Duffie. “These ratings mean something else -- entirely.” For example, corporate bonds rated Baa, the lowest Moody’s investment rating, had an average 2.2% default rate from 1983 to 2005, according to Moody’s. In contrast, Moody’s found that CDOs with the same Baa grade suffered five-year default rates of 24% from 1993-2005.

- To evaluate the CDOs, S&P, Moody's and Fitch run models called the Monte Carlo simulation, named after the Mediterranean gambling city, to calculate the probability that the CDO's assets will default in hypothetical situations of financial and commercial stress. The simulation effectively "rolls the dice" more than 100,000 times by running the data randomly. The rating companies base their simulations and ratings of each tranche on assumptions about default and recovery rates that may be incorrect, said Arturo Cifuentes, a managing director at R.W. Pressprich & Co. "The danger with Monte Carlo is that it gives you a false sense of security," said Cifuentes. "If the input data that you use is a little bit uncertain, your numbers are going to be trash, but they will look convincing." The credit rating agencies may have miscalculated the potential toxicity of securities backed by subprime loans, Brian McManus, head of CDO research at Wachovia Corp. "With CDOs, they underestimated the volatility of the subprime asset class in determining how much leverage was OK," he added. "The [agency's] models are fine," said Satyajit Das, a former Citigroup Inc. banker. "But they have an input problem. It becomes a number we pluck out of the air. They could be wrong, and the ratings could be misleading. I'm not even sure we understand the networks of links between the subprime tranches."
- Now, investment banks and rating agencies have introduced CDOs squareds, a bundling together of CDOs, and CDOs cubeds [a bundling of CDOs squareds]. Investors shouldn't put much credence in the risk that rating companies assign to CDOs squareds and cubeds, said Duffie. "The complexity of analyzing that is beyond current methodology," he added. Janet Tavakoli, founder of Chicago-based consulting firm Tavakoli Structured Finance Inc. agrees that the rating agency's grades on these products are worthless. "Ratings on these products are based on smoke and mirrors," said Tavakoli.
- Former Citigroup banker Das wonders why few people are examining the dangers for CDO investors. "I think the regulators seem to be fairly sanguine about all of this," said Das. "The thing that I find quite bewildering is the lack of urgency and focus. ...[Now that subprime mortgage faults have started to soar,] the fuse has been lit. Somebody should be trying to find where this wire is running to." (*Bloomberg News*, David Evans and Richard Tomlinson, 05/31/07)
- In a June 7 posting to *Mish's Global Economic Trend Analysis*, Michael Shedlock wrote, "Based on [*Bloomberg's* analysis of the CDO market], it is highly likely that pension plans holding some of the CDO toxic waste are assuming big returns when in fact they are holding worthless paper. There is easily a potential of a waterfall event... Long Term Capital Management blew up ...when models written by Nobel prize winning economists Myron Scholes and Robert Merton failed. Are the Monte Carlo models (or more importantly the assumptions going into the Monte Carlo models) any better? How can anyone even know if the only 'mark to market process' is based on what the model says?! The scariest thing is that we are in a monetary environment that is unprecedented in history. M3 is soaring in nearly every major country on the globe. Asset prices have never been more correlated than now. The

amount of derivatives in play is in the hundreds of trillions of dollars all bet on Monte Carlo Simulation. Wow!” (*Mish’s Global Economic Trend Analysis*, Michael Shedlock, 06/07/07)

- In a June 9th post, Shedlock added, “...It sure seems like a hell of a lot is riding on the Monte Carlo Simulation of CDOs as well as the parameters and assumption that feed into the model. If and when a credit event occurs that ripples through multiple CDO tranches, the guarantors will be about as well capitalized to handle the guarantees... Do I smell a government bailout coming up?” (*Mish’s Global Economic Trend Analysis*, Michael Shedlock, 06/09/07)
- The *International Herald Tribune* reported that the California Public Employees’ Retirement System has invested \$140 million in unrated CDO (toxic) equity tranches, which were sold to the pension fund by Citigroup. According to public data, public pensions have bought more than \$500 million in CDO tranches in the past five years, including the New Mexico State Investment Council (\$225.5 million; NMSIC purchased an additional \$300 million of equity tranches in April), the General Retirement System of Texas (\$38.8 million), the Teachers Retirement System of Texas (\$62.8 million), and the Missouri State Employees Retirement System (\$25 million). “It’s grossly inappropriate [for pension funds] to take this level of risk,” said Chriss Street, treasurer of Orange County, California. “Fund managers wanted the high yield, so Wall Street sold it to them. The beauty of Wall Street is they put lipstick on a pig.” The big risks taken by public pension funds managers to ramp up their investment performance through purchases of CDO equity tranches could result in big losses, said Street. “Very few pension plans could meet their fiduciary duty by buying portfolios of subprime loans, he added. “They spiked up the yield, but that yield means nothing when the defaults start to mount, as we know they will. The funds will take big losses.” (*International Herald Tribune/Bloomberg News*, David Evans, 06/04/07; *Bloomberg News*, David Evans, 06/01/07).

Loan foreclosures haven’t peaked yet

- According to the Mortgage Bankers Association, the percentage of loans entering foreclosure rose 9 basis points from the fourth quarter to 1.28%. Subprime mortgages remained the driving force in rising foreclosures, with subprime ARMs in foreclosure increasing 53 basis points from a year earlier to 3.23%. According to MBA’s chief economist Doug Duncan, foreclosures and delinquencies are also being driving by investor speculation in Arizona, California, Florida and Nevada, as well as high levels of construction relative to the overall populations in Indiana, Michigan and Ohio. “I think it is reasonable to think that we’ll see a peak of delinquency rates this year, but not see a peak in foreclosures until 2008,” said Duncan. “It’s not going to cause a national recession. It’s simply a housing recession. We are likely to see modest increases in delinquencies over the next few quarters.” (*American Banker*, Kate Berry, 06/15/07)

RealtyTrac to change foreclosure data formula—reported numbers likely to “dramatically decrease”

- According to Sam Ali of the *New Jersey Star-Ledger*, foreclosure data source RealtyTrac will soon change its formula for counting foreclosures due to complaints from housing experts that the company double-and triple-counts properties as they move from various stages of foreclosure. RealtyTrac sources told Ali that the company will start publishing the number of unique households affected by foreclosures in addition to its usual recap of new foreclosure filings. The change to the formula is expected to occur as soon as next month, and will likely “dramatically decrease the number of foreclosures in any given state,” according to RealtyTrac.
- RealtyTrac normally “counts every step every step in the drawn-out foreclosure process separately -- notice of default; lis pendens, or the filing of a lawsuit to repossess a home; sheriff's sale; and a final step when ownership reverts to the bank if the property has not been sold at an auction. Now, in addition to supplying information about each stage of foreclosure, RealtyTrac will report the number of unique properties in the foreclosure process, counting them just once.” Rick Sharga, vice president of marketing at RealtyTrac, told Ali that the company decided to adjust its numbers because too many people – including media—were misinterpreting the numbers. Ali quoted Sharga as noting, “We stand by our numbers and always have...But we want to provide a greater level of detail now ... so people don't misinterpret what we are reporting.”
- Housing experts have long questioned RealtyTrac's methodology. “Jeffrey Otteau, president of the Otteau Valuation Group, a leading real estate research firm in New Jersey, believes RealtyTrac's existing methodology is highly misleading. Back in March, for example, RealtyTrac reported 4,780 properties in New Jersey had entered into foreclosure that month. Otteau's own data suggested the actual number of New Jersey homes repossessed by lenders in March was just 270. The reason for the discrepancy? Otteau is counting homes in the final "REO" stage, when the bank has repossessed the property. ‘RealtyTrac's numbers are counting houses each time they pass through one of those four stages, and thus, some homes are getting counted three or four times, which exaggerates the numbers greatly,’ Otteau said. ‘Given that only a small percentage of delinquent loans actually reach the final stage of foreclosure, the reported figures are not what they appear to be.’”
- In addition to Otteau, the Colorado Division of Housing also accused RealtyTrac of inflating numbers. “RealtyTrac reported Colorado had 54,747 foreclosures in 2006, with a foreclosure rate of 1 in 33 households. But after collecting its own data, the state's Division of Housing concluded the foreclosure rate for Colorado was closer to 1 in 58, with a total number of 28,453 filings in 2006... Doug Duncan, the chief economist at the Mortgage Bankers Association, has also criticized RealtyTrac, noting ‘their business model is to market foreclosed properties.’ RealtyTrac, which is privately held, charges subscribers \$49.95 a month for its foreclosure listings.” (*New Jersey Star-Ledger*, Sam Ali, 06/12/07)

Freddie Mac to resume reporting financial results for the first time since 2002

Freddie reports \$211 million loss for the first quarter of 2007

- Freddie Mac announced that it is scheduled to resume reporting its financial statements on a regular basis for the first time since 2002 and will report interim results on a timely basis starting in August. The company also said it plans to file its FY2007 report within 60 days of the end of the year, making it the first “timely” financial report issued by Freddie Mac in more than five years. “It’s real important, because it’s the gateway to regaining our creditability in general with the marketplace,” said Freddie Mac CFO Buddy Pizsel in an interview. He added that the company will begin its registration process with the SEC in mid-2008. (*Wall Street Journal*, Damian Paletta, 06/14/07)
- At the company’s June 8th annual shareholder meeting, Freddie Mac chairman and CEO Richard Syron said that the company has begun its search for his successor, but added that the board of directors will not rush to pick a candidate. “We’re going to do this in an expeditious way, but we’re not going to rush out and do something before really thinking about - and this really is a board choice - you know, what is it that we should be looking for, how is our management and the organization restructured, and how do we get there,” said Syron, who said he would not play an active role in the selection process. “We’re very cautious on this from a governance perspective, and I really have always believed that it doesn’t work out well - CEOs should never choose their successors,” said Syron. “It’s just emotionally, every other way, there is too much potential for conflict. ...The last thing I want to give, because it’s absolutely completely distant from the truth, is any implication that I’m involved in steering this thing.”
- At the meeting, Freddie Mac shareholders elected 13 directors to its board and approved the re-appointment of PricewaterhouseCoopers as the company’s independent auditor for fiscal year 2007. Shareholders also approved the amendment and restatement of the company’s 1995 Directors’ Stock Compensation Plan. At a board meeting following the annual shareholders meeting, Freddie Mac’s directors approved the appointment of members to the board’s committees and approved a number of amendments to the company’s bylaws, effective immediately. The board also declared a quarterly dividend on Freddie Mac’s common stock of \$0.50 per share, payable on June 29th to shareholders of record as of June 18th. The board also approved dividends for the company’s preferred stock in accordance with the terms of each issue. (*Freddie Mac Press Release*, 06/08/07; *Dow Jones Newswires*, Damian Paletta, 06/08/07; *Freddie Mac Press Release*, 06/08/07; *Wall Street Journal*, Damian Paletta, 06/14/07)

Freddie reports \$211 million loss for the first quarter of 2007

- Freddie Mac reported a \$211 million loss, or \$0.46 per diluted common share, in the first quarter of 2007, compared to net income of \$2.0 billion, or \$2.80 per diluted common share, for the same period in 2006. According to Thomson Financial, analysts had anticipated the company to earn on average \$1.01 a share for the quarter. During the quarter, Freddie said its credit-related expenses totaled \$193 million, more than triple the \$60 million expense it booked during the first quarter of 2006. Freddie Mac said that its increased provision for credit losses was related to the deteriorating quality of mortgages originated in 2006 “that have exhibited higher transition rates from delinquency to foreclosure and higher loan loss severities associated with slower home price appreciation and higher unpaid principal balances.” The company also said it expects future loan charge-offs to increase. “While the full impact of the housing downturn has not been felt, our credit position has remained strong relative to our historical levels and the market as a whole,” said Freddie Mac’s chairman and chief executive, Richard F. Syron.
- The company also reported a decline in fair value of net assets attributable to common stockholders [before capital transactions] of approximately \$300 million in the first quarter of 2007, compared to an increase of \$1.0 billion for the same period a year ago. “While significant mark-to-market losses on our portfolio of derivatives, which are used to hedge our interest-rate risk, and on our credit guarantee activities have resulted in a GAAP loss, we remain encouraged with the underlying fundamentals of Freddie Mac’s business,” said Freddie Mac CFO Buddy Pizsel.
- Freddie Mac’s retained portfolio grew at an annualized 6% rate during the first quarter, as increasing spreads and a pullback by competing investors presented “the first real buying opportunity, probably in several years,” said Syron. The availability of an “attractive rate of return” on additions to Freddie’s investment portfolio came about “partially as a result of the uncertainty in the subprime market,” he said. “[Mortgage rates] have increased relative to a cost of debt more recently.” Syron added that the progress Freddie Mac has made in timely reporting “puts us closer to being able to grow our portfolio as market and mission conditions warrant.” During a conference call with investors, the company’s management framed their discussion of portfolio growth as fundamental to Freddie’s mission to provide liquidity and stability to the mortgage market. Patti Cook, Freddie’s EVP for investments and capital markets, told investors, “It’s really interesting to go back and look at the discussion in the marketplace a year ago, where there was plenty of speculation as to whether you needed the GSEs because of all the aggressive buying that was occurring in mortgages, particularly on the part of banks and the infamous ‘Asian investor.’ What you’re seeing now is a pullback from those two constituents for a variety of reasons at a time when fixed-rate origination is actually increasing.” Management noted that the company’s restrained growth in 2006, when investment opportunities were less favorable, now gives Freddie considerable room to maneuver within its regulatory-mandated cap on growth. “It’s really hard to speculate whether this change in environment is going to persist for months, quarters, years,” said Cook. “What I

would say is that we are attentive to both the opportunity and the need for us to engage now.” As of March 31, Freddie Mac could increase its retained portfolio holding by \$9 billion without exceeding its regulatory cap.

- “[Freddie Mac’s regulatory cap] will remain until all significant operational risks have been addressed,” said OFHEO director James B. Lockhart, III in a statement. “They continue to make progress but they still have a long way to go.” (*Freddie Mac Press Release*, 06/14/07; *Washington Post*, David S. Hilzenrath, 06/15/07; *Wall Street Journal*, Damian Paletta, 06/14/07; *American Banker*, Harry Terris, 06/15/07; *Wall Street Journal*, Damian Paletta and James R. Hagerty, 06/15/07; *Associated Press*, Marcy Gordon, 06/14/07; *Bloomberg News*, James Tyson, 06/14/07)
- On *Seeking Alpha*, George Gutowski wrote, “Richard F. Syron, chairman and chief executive officer was particularly proud that Freddie Mac took a leadership role in the sub prime mortgage market, announcing new underwriting standards and products and committing to purchase up to \$20 billion in mortgages to support sub prime borrowers. The new underwriting standards is a big sleeper comment. Given the problems from sub prime, what does that really mean? When Freddie Mac was conceptualized did they want to be in the sub prime markets[?] Freddie, welcome back, but you need to speak more clearly.” (*Seeking Alpha*, George Gutowski, 06/15/07)

Fannie Mae updates its guidance on timing of 2006 10-K

- On June 8th, Fannie Mae announced it expects to file its Annual Report on Form 10-K for the year ended December 31, 2006 with the SEC during the third quarter of 2007. The company plans to hold its annual meeting of shareholders on December 14, 2007—its first since May 2004. Fannie Mae also announced that it plans to become a current filer by the end of February 2008 with the filing of its 2007 Form 10-K with the SEC. “Today’s update reflects a lot of continued momentum in our efforts to catch up and become a current filer,” said President and Chief Executive Officer Daniel H. Mudd. “We’re looking towards the future, the annual meeting, and to hearing from our shareholders on corporate issues.”
- “[This timetable] is way ahead of market and OFHEO expectations,” wrote Jim Vogel, head of agency debt research at FTN Financial, in a note to clients. “Getting caught up with where you were supposed to be all along doesn’t exactly qualify as good news, but it’s way better than falling further behind.” (*Fannie Mae Press Release*, 06/08/07; *Bloomberg News*, James Tyson, 06/09/07)

Fannie Mae and Freddie Mac

New GSE regulator needed to curb “great risk,” says HUD Secretary

- In a question and answer session following a speech at the National Pres Club, HUD Secretary Alphonso Jackson said, “There’s great risk” if Congress fails to pass GSE regulatory reform legislation. Jackson added, “I think it’s important that we get [GSE] legislation out this year to have a strong regulator... What is important is that we have a regulator to make sure that if one of these entities fails, it is [not a repeat of the failure of the thrift industry in the 1980s], and the only way we can do that is by having a strong regulator.” (*Bloomberg News*, James Tyson, 06/04/07)

Fannie and Freddie continue to require significant regulatory supervision

- In a June 11th speech to the Predictive Methods Conference, OFHEO director James B. Lockhart, III told the audience that Fannie Mae and Freddie Mac suffered through years of mismanagement and underinvestment in infrastructure which facilitated earnings manipulation. Neither Fannie Mae nor Freddie Mac “have been regular filers of audited financial statements for four years and it may take another year” before they do so, said Lockhart. While both companies are spending billions on remediation, the GSEs continue to face significant issues pertaining to data integrity, internal controls, accounting and operating systems, and risk management. Lockhart again urged Congress to pass GSE regulator reform legislation, which would give the new regulator expanded “bank regulator-like” powers, mission and new product authority, stronger independence, the ability to strengthen capital requirements, and clear guidance on the regulation of the GSEs’ mortgage portfolios. (*Bloomberg*, James Tyson, 06/11/07; *Addressing the Risks in Housing GSEs*, James B. Lockhart, III, 06/11/07)

OFHEO director Lockhart rebuffs Senators’ calls for copies of Fannie Mae report

- OFHEO director James B. Lockhart, III has denied the request by Senators Chuck Hagel (R-NE) and John Sununu (R-RH) to provide them a copy Fannie Mae’s report on the role of their employees in its accounting scandal. In response to the Senators’ May 15th letter, Lockhart responded, “The type of report involved here is not made public as it contains commercial, financial, and private individual information and was received as a part of our examination program.” In his May 24th letter, the director added, “I want to assure you that, should behavior or activities approach the level of a potential crime, we refer the matter to the Justice Department. Also, should the conduct or an activity violate a statute under the purview of another regulator, we would refer the matter to that regulator.” (*American Banker*, Steven Sloan, 06/06/07)

- In a June 14th editorial appearing in the *Idaho Statesman* [Boise, ID], economist Edward Lotterman wrote, “Be cautious in assuming that markets don’t work, particularly when contemplating government financing of private construction. That is one lesson from a financial kerfluffle in my hometown of St. Paul, MN. It happens to be playing out here, but the same thing could happen in dozens of other cities across the nation.”
- “Back in 1974, city government wanted to speed economic development. Elected officials grumbled that banks and other private financing sources were unwilling to finance what seemed to be terrific projects. Free markets clearly were not working the way the City Council wanted them to. So they acted to fix the situation. Emulating New York City, they had created a Port Authority. Seeing how New York’s Port Authority, headed for decades by Robert Moses, had financed all sorts of projects, they sought to do the same.”
- “The Port Authority set up a fund to finance development projects that could not get private financing. The money came from bonds sold by the Port Authority. Repayments of the loans made to developers would pay principal and interest to people who bought the bonds. They were careful to issue ‘revenue bonds’ rather than ‘general obligation bonds.’ The bonds were not backed by ‘the full faith and credit’ of the Port Authority or the city. If mortgage payments from funded developments were not sufficient to make principal and interest payments, the bondholders were out of luck. There was no legal obligation to use tax money to make up the difference.”
- “For a while, everything was great. The fund operated like gangbusters, making loans totaling nearly a half-billion dollars. But soon one funded development after another went belly up. By 1991 the fund was in deep trouble and stopped selling new bonds or financing new projects. It is finally being liquidated with bond holders getting about 60 cents on the dollar.”
- “Why should anyone not from my hometown care? It matters because hundreds of municipalities have set up similar creative financing schemes across the United States. Some are better managed than the one in liquidation, but all are based on the same faulty thinking. The general lesson here is that resources get wasted when government assumes inappropriate functions. Agencies like this are poor at judging risk and don’t face the incentives to do so thoroughly. Although they disclaim government status, their implicit association with government insulates bond purchasers from underlying risk. **More broadly, this problem of unclear status and risk apply to institutions like Ginnie Mae, Freddie Mac and the Farm Credit System that enjoy implicit federal agency status, and ultimately to multilateral institutions like the World Bank.**” [Emphasis added.]

- “While local development agencies may successfully insulate taxpayers from any liability for projects gone bad, political pressure for government to step in always arises. In the late 1980s, the federal government had little legal liability for the debts of the Farm Credit System, but taxpayers eventually funded a bailout of the system and the investors who had bought its securities.”
- “Many economists, including heads of some Federal Reserve District banks, worry that the same risks apply to Fannie, Freddie and Ginnie. Taxpayers are not supposed to be liable for securities issued by these institutions, but if one went belly up, political pressure for a bail-out would be enormous. The basic mistake in all such situations is to assume that if private capital markets are unwilling to finance private projects, it is due to market failure rather than the fact that the projects are not commercially viable.”
- “A second mistake is to ignore the skewed incentives when administrators of such entities do not answer to anyone with a financial stake in their efforts. Instead, they report to city officials whose objectives are political, not financial. Politicians have notoriously short planning horizons — until the next election — and are more interested in dirt being moved and buildings going up than in long-term financial consequences.”
- “A third mistake is to assume that initial success — or at least the absence of failure — assured long-term viability. In St. Paul, 139 projects got money over 17 years. The fact that some early projects met cash-flow requirements for a few years lulled both the authority and bond purchasers to increase their bets.”
- “Despite the bondholders’ claims of bad faith, one need not grieve for them. A messy default like this reminds all investors not to ignore risk, even if veiled by a borrower’s quasi-government status. Specific complaints can be settled in the courts, which have shown little sympathy so far.”
- “The core problem is that valuable resources are wasted in projects whose value to society is less than their cost. Such resources are diverted from other uses where they might do more good for society.” (*Idaho Statesman*, Edward Lotterman, 06/14/07)

Bush administration notes

- On June 5th, the Senate confirmed David G. Nason as the Treasury Department’s assistant secretary for financial institutions. Previously, Nason served as the deputy assistant secretary for financial institutions and the department’s point person on reforming the oversight of Fannie Mae and Freddie Mac. (*Dow Jones Newswires*, Damian Paletta, 06/06/07)

- Kevin MacMillan, one of Treasury’s top liaisons with Capitol Hill on banking issues, is leaving his post to join Bank of America’s general counsel office. MacMillan spent more than a year and a half, providing lawmakers Treasury’s perspective on banking policies and was particularly active on efforts to pass GSE regulatory reform legislation. (*American Banker*, Stacy Kaper, Steven Sloan, and Cheyenne Hopkins, 06/11/07)

Fannie Mae and Freddie Mac join forces with Homes for Working Families

- Fannie Mae’s CEO Daniel Mudd and Freddie Mac’s chairman and CEO Richard F. Syron are among the 17 board members for Homes for Working Families (HWF), a national nonprofit organization dedicated to advancing policy changes that make safe, good-quality homes affordable for America’s working families. HWF’s chairman is Angelo R. Mozilo, chairman and CEO of Countrywide Financial Corporation; its vice chairman is Harry W. Clark, managing partner of Stanwich Group, LLC; and its secretary/treasurer is Alan Wiener, managing director for Wachovia Multifamily Capital. Other board members include Henry G. Cisneros, HUD Secretary in the Clinton administration, Suzanne P. Clark, president of the National Journal Group, Stephen Goldsmith, Daniel Paul Professor of Government at Harvard University, David K. Hill, chairman and CEO of Kimball Hill Homes, Rick A. Lazio, EVP of Global Government Affairs and Public Policy at JPMorgan Chase, Michael W. Perry, chairman and CEO of Indymac Bancorp, Lewis S. Ranieri, chairman of Hyperion Partners, Deborah Ratner Salzberg, president of Forest City Washington, Inc., Robert K. Ross, the president and CEO of The California Endowment, Donna E. Shalala, president of the University of Miami, Warren Simmons, executive director of the Annenberg Institute for School Reform at Brown University, and Mark Walsh, managing director for Lehman Brothers.
- According to the organization’s website, “HWF was founded in late 2005 to combat the growing problem of home-affordability. The non-profit was established after more than two years of systematic, rigorous research and development efforts, including a feasibility study, public opinion research, pilot work in three states and collaboration with several partners from national affordable housing organizations. Research and development efforts underscored the need for a new organization with a singular focus on policy change at the local, state and national levels to confront the shortage of affordable homes for working families.” Beverley Barnes serves as HWF’s Executive Director. Previously, Barnes was senior vice president, communications for Fannie Mae and senior vice president of the Fannie Mae Foundation. In addition to financial support provided by Fannie Mae and Freddie Mac, the organization has also received financial commitments of \$3 million from Countrywide Financial Corp. and \$1.5 million (over a three year period) from Kimball Hill Homes. (www.homesforworkingfamilies.org, *Homes for Working Families Press Release*, 01/29/07; *Homes for Working Families Press Release*, 04/19/07)

Fannie Mae

OFHEO wants former CEO Franklin Raines's subpoenas tossed out

- OFHEO has asked the U.S. District Court in the District to throw out subpoenas by Fannie Mae's former chairman and CEO Franklin Raines, which seek details about the regulator's investigation of the company. The agency alleges that Raines is using the subpoenas to distract its staff and impede OFHEO's \$84 million lawsuit against him. According to the agency's court filing, the subpoenas are an effort "to interfere with administrative" litigation brought by OFHEO "and delay their day of judgment." (*Washington Post*, 06/06/07)

Thank you, Fannie Mae

- In a June 5th column in the *Washington Post*, Jeffrey Birnbaum wrote, "Robert B. Zoellick, Bush's choice as the next president of the World Bank, will have to worry about only global poverty and not his own. When he turns 55 in July 2008, he will start to receive \$91,310 a year from the Fannie Mae pension fund, according to PoliticalMoneyLine.com. Zoellick's most recent financial disclosure report, covering 2005, also shows that he owned between \$1 million and \$5 million in Fannie Mae stock, as well as a Fannie Mae-established 401(k) with between \$100,000 and \$350,000. Not bad for working as an executive vice president at the mortgage giant for just four years in the 1990s." (*Washington Post*, Jeffrey H. Birnbaum, 06/05/07)

Fannie Mae hopes to receive regulatory approval to resume purchase of ADC loans

- According to *National Mortgage News'* June 11th edition of *MortgageWire*, "Fannie Mae is hoping ...[OFHEO] will complete a review of its residential construction loan program soon, enabling the company to get back into the market again. OFHEO suspended Fannie's purchases of acquisition, development, and construction loans last summer, citing concerns about the program's controls and procedures. *MortgageWire* has learned that Fannie Mae has delivered all information that OFHEO requested on May 8, and now the [GSE] is waiting for the regulator's decision. Fannie operated an ADC pilot program under the oversight of [HUD] for 12 years. But when Fannie wanted to expand the ADC program last year, OFHEO intervened." (*National Mortgage News' MortgageWire*, 06/11/07)

Fannie “alumni” news

- Georgetown University has appointed Bill O’Leary to serve as its Chief Marketing Officer and Associate Vice President for Marketing and Communications in the Office of Advancement. Previously, O’Leary was Fannie Mae’s Director of Business Strategies for Community and Multicultural Lending, where he led a team that developed creative strategies for the GSE’s 2000+ lender partners, which included radio, TV, direct mail, online and event marketing. He also led Fannie Mae’s qualitative and quantitative research a wide range of issues, including consumers, real estate professionals, lenders, mortgage brokers, and home counselors. (*Media-newswire.com*, 06/14/07)

Fannie Mae and RCG Longview announce the availability of the enhanced CI Mezz-Mod Rehab product

- To address the renovation needs of aging multifamily affordable housing stock, RCG Longview, a real estate opportunity manager in New York City, and Fannie Mae announced the availability of the enhanced Community Investments Mezzanine-Moderate Rehabilitation (CI Mezz-Mod Rehab) product, a one-stop financing solution for multifamily properties with moderate to substantial rehabilitation needs with costs of \$5,000 or more per unit. DUS lenders provide a one-stop shop by underwriting and providing a rate lock on both the DUS and mezzanine loans, funded by The Community Investment Mezzanine Fund LP, a partnership between RCG Longview and Fannie Mae.
- “Fannie Mae has enhanced its CI Mezz-Mod Rehab product to be very competitive and offer a financing solution for the nation’s affordable rental housing stock in need of a serious upgrade,” said Richard Lawch, senior vice president of Community Investments at Fannie Mae. “CI Mezz-Mod Rehab provides our DUS lenders with an innovative product for rehabilitation and preservation of affordable housing,” added Phil Weber, senior vice president of Multifamily at Fannie Mae. (*Fannie Mae Press Release*, 06/11/07)

Freddie Mac

Freddie Mac participates in the financing
of the largest private student housing transaction on record

- Campus Apartments, Inc. has acquired a 14-property student housing portfolio from FirstWorthing Residential Company, LP for \$256 million, representing the largest private student housing transaction on record. The acquisition was funded through Campus Apartments' \$1.1 billion joint venture with GIC Real Estate Pte Ltd., the real estate arm of the Government of Singapore Investment Corp. Deutsche Bank Berkshire Mortgage provided \$153 million in financing with Freddie Mac, which is the GSE's largest student housing transaction to date. "We are very pleased to be able to provide the financing package to enable Campus Apartments to acquire this quality portfolio," said Mitchell W. Kiffe, Freddie Mac vice president of Multifamily Production and Sales. "Freddie Mac views the student housing segment of the market to be an attractive expansion opportunity." (*Business Wire*, 06/13/07)

Freddie Mac Alliance chooses Brooks Systems to assist ABA members with compliance

- The Freddie Mac/American Bankers Association Alliance has chosen Brooks Systems to provide compliance technology and consulting services to ABA members. Brooks Systems will help alliance members with compliance with a variety of state anti-predatory and other lending statutes and help minimize a lender's risk. (*PRWEB*, 06/12/07)

Freddie Mac is largest corporate giver in metro-Washington area

- The *Washington Business Journal* and Greater DC Cares named Freddie Mac as the largest corporate giver in the Washington, DC metro area in 2006, based upon the company's contribution of nearly \$26 million to help children and families in the region. (*Freddie Mac Press Release*, 06/13/07)
- On June 9th, Freddie Mac held its Hoops for Homeless Event to help fight homelessness, in which it raised \$900,000 for six local homeless nonprofits to provide services to homeless families in the Washington, DC area. (*PR Newswire*, 06/09/07)
- On June 15th, Freddie Mac and the Freddie Mac Foundation announced their plans to commit a combined \$5 million to New Orleans, specifically to help rehabilitate and rebuild housing as well as provide needed resident services for many low-to moderate-income families to stabilize their lives. The company and Foundation will

make investments in organizations throughout the next year to support on-going, innovative and effective efforts. “Part of our mission is to play a stabilizing role for housing. That’s why we remain committed to helping Gulf Coast residents. We recognize that access to housing for all families is critical to New Orleans future vitality,” explained Ralph F. Boyd, Jr., executive vice president, Freddie Mac, and chairman, Freddie Mac Foundation. “New Orleans has pockets of outstanding affordable housing projects evolving. To propel these forward, we plan to invest in a number of the non-profits that are leading the charge.” (*Freddie Mac Press Release*, 06/15/07)

Federal Home Loan Banks

Federal Housing Finance Board adopts rule clarifying the financial investments of appointed FHLB directors

- The Federal Housing Finance Board’s board of directors adopted a final rule that clarifies the types of financial investments and other relationships that an appointed director may have with a depository institution that is a member of the Federal Home Loan Bank on whose board the director serves. The new rule reflects the agency’s long-standing policy that financial interests in a Bank member resulting from ownership of shares of a diversified mutual fund are permissible holdings for an appointive director. The rule also extends the rationale for permitting mutual fund investments to other types of investment vehicles and accounts that share certain key features of mutual funds that make them unlikely to pose a risk of conflict of interest for an appointive director. Finally, the rule set forth additional criteria to define when owning shares of a holding company of a member, serving as an officer or director of a holding company of a member, or having other types of financial interests in a member, would be permissible for an appointive director. The final rule is effective 30 days after publication in the *Federal Register*. (*Federal Housing Finance Board Press Release*, 06/13/07)

FHLB-Atlanta hires Richard Dorfman to serve as president and CEO

- The FHLB-Atlanta has hired Richard Dorfman, a mortgage consultant and consultant to several FHLBs, as its president and chief executive. Dorfman, who joins the Bank on June 20, will succeed interim CEO William Ott. From 1997 to 2005, Dorman was the managing director of U.S. agencies and mortgages at ABN Amro Holding N.V. (*American Banker*, Steven Sloan, 06/14/07)

FHLB-Cincinnati names Carole Cossé as the Bank's CFO

- The FHLB-Cincinnati's board of directors has promoted Carole Cossé to senior vice president and CFO of the Bank, responsible for the overall management of investments, external debt management, deposit pricing and hedging activities, and managing market risk exposure. Previously, Cossé served as the Bank's senior vice president and treasurer. (*FHLB-Cincinnati Press Release, 06/13/07*)

FHFB appoints new directors to FHLBs' boards

- The Federal Housing Finance Board has appointed John H. Robinson, chairman of Hamilton Ventures, LLC, to serve on the FHLB-Des Moines board of directors for a term ending December 31, 2009. Since 2004, Robinson has been the chairman of Hamilton Ventures, a consulting and investment business located in Kansas City, KS. He is an engineer with international experience as chairman of EPCglobal Ltd in Sheffield, England and executive director of Amey Plc in London, England. Robinson also serves on the board of directors of COMARK Building Systems Inc., Olsson Associates, Alliance Resource Partners LP and Coeur d'Alene Mines Corporation. (*FHLB-Des Moines Press Release, 06/12/07*)
- The Federal Housing Finance Board has appointed Melinda Guzman, John F. Luikart, Robert F. Nielsen, and John T. Wasley to fill open seats on the FHLB-San Francisco's board of directors. Guzman and Nielsen will fill the remainder of a three-year terms that began on January 1, 2006. Guzman is a partner with Goldsberry, Freeman & Guzman, LLP, a Sacramento law firm. Nielsen is president of Shelter Properties, Inc., in Reno, NV.
- Luikart and Wasley will fill the remainder of a three-year term that began on January 1, 2007. Luikart is president of Bethany Advisors LLC in San Francisco, CA. Wasley is managing partner of Heidrick & Struggles, a Los Angeles law firm. (*FHLB-San Francisco, 05/25/07*)

Ginnie Mae

Chairman Dodd hopes to pass FHA reform by August recess

- Senate Banking Committee chairman Chris Dodd (D-CT) said he will try to get the Committee to pass the FHA reform bill “in the next month or so,” before the Congressional recess in August. (*National Mortgage News’ MortgageWire*, 06/06/07)

HUD Secretary Jackson urges Congress to pass FHA reform

- In a June 4th speech at the National Press Club, HUD Secretary Alphonso Jackson urged Congress to pass FHA regulatory reform legislation. Jackson said, “I will say to you today here and to the Congress, we need this reform now. President Bush and I have repeatedly urged Congress to act. FHA is the mainstay of American housing enterprise. Over the past 73 years, FHA has helped millions of families become homeowners. Late this month, when we celebrate the 34th million FHA customer, we will help many families stay in their homes. I mentioned earlier that refinancing the FHA could help tens of thousands of families already in the subprime problem. If Congress passes FHA reform this summer, we can help hundreds of thousands, and we could do so without any cost... [The] FHA’s ability to help is limited without statutory change. We have fixed as much of the process that we can internally and reduced red tape to make FHA more user-friendly.... We need to be able to help more first-time homebuyers, low-income Americans -- the groups we’re designed to serve, and we want to serve them safely.”
- “...If Congress allows us to set the premium commensurate with the [risk], which makes a lot of sense, FHA will be able to help thousands of borrowers. Imagine risk-based premium for an insurance company. Who could argue with that? Unfortunately, under today’s restricted premium limit, the maximum loan amount, FHA simply cannot reach the borrowers who need the safety net that FHA can only provide. I asked you again, please work with us to ask Congress to get this legislation out by this summer.”
- When asked by an audience member if the “worst is over” with the subprime loans, Jackson responded, “...80 percent of those loans in the subprime market are going to be fine, it’s the 20 percent. And if we can get the FHA modernization legislation passed quickly, we can probably address about 70-80 percent of those loans. ...we can refinance the loans. But let me make it clear: I don’t think we should be the bail-out agency, where low and moderate income persons have had serious difficulties and been bamboozled. I think it’s our responsibility to help them, and we’re going to do everything our power to make sure they keep their home. See, one of the things that we’ve done, ...as I said, we’ve gone from \$10 million in housing counseling to this

year asking for \$50 million. If we can counsel people very well, let them know what is expected, they can begin to keep their homes, and we've been very successful with the ...2.6, 2.7 million homeowners that we've been counseling under the president's new program."

- When asked about the prospects for passage of FHA legislation passing, Jackson responded, "We hope it passes. We think that it's looking good. I think the subprime loan problem has ...given Congress the impetus to pass this legislation." (*Federal News Service*, Remarks of HUD Secretary Alphonso Jackson at the National Press Club, 06/04/07)
- HUD Secretary Jackson recently told a Wells Fargo housing symposium that there is an "urgent need for Congress to pass legislation that modernizes the FHA to help both promote and protect homeownership." Citing a recent survey results released by Wells Fargo, Jackson noted that nearly 80% [of those polled] support legislation that would promote and protect homeownership in America "by providing a safer, fairer and more affordable mortgage alternative to high-cost subprime loans." Jackson said, "Americans are in support of an FHA that could help even more first-time homebuyers and people with moderate incomes have access to safer mortgages." (*National Mortgage News' MortgageWire*, 06/15/07; *HUD News Release*, 07/04/07)

Trade groups promote the need for FHA reform

- The National Association of Homebuilders and the National Association of Realtors have renewed their calls for Congress to pass FHA reform legislation. As part of the NAHB's recognition of June as National Homeownership Month, the trade group called on Congress to act on FHA reform. "Comprehensive FHA reform would mean greater flexibility in responding to the needs of borrowers, enabling more working families to become homeowners, and providing a viable alternative to the volatile subprime market," said NAHB EVP Jerry Howard. "National Homeownership Month is the perfect opportunity to highlight this area where change can result in thousands more Americans realizing the dream of homeownership."
- Megan H. Booth, senior policy representative for the National Association of Realtors, said, "This is a critical window. There's all this congressional concern about the subprime mess, with horror stories in every district. This is our time to get Congress to say: 'If we can reform this program, we can give people a viable alternative that's not risky like these crazy loans,'" she said. "How many hearings has Congress had this spring on subprime? A gazillion. FHA reform can't be a bailout to subprime problems, but it can be a solution." (*National Association for Home Builders Press Release*, 06/04/07; *Milwaukee Journal Sentinel*, Joanne Cleaver, 06/10/07)

House appropriators include provision to increase FHA loan limits

- House appropriators have attached a provision to HUD's budget bill, raising the FHA single-family loan limit to the conforming loan limit (\$417,000) in high-cost areas and 65% of CLL in low cost areas. In all other areas, the FHA loan limit would be determined by the median house price. The provision also suspends for one year a cap on the number of reverse mortgages that FHA can insure. (*National Mortgage News' MortgageWire*, 06/12/07)

FHA: "All talk and no walk"

- In the June 11th issue of *MortgageLine*, Christopher Cruise, a senior national mortgage trainer for Innovations Mortgage Training Services, offered the following viewpoint on FHA: "The leaders of [FHA], among them Brian Montgomery - the FHA commissioner and assistant HUD secretary - talk the talk when it comes to encouraging mortgage brokers to offer FHA loans, but three recent incidents prove that with the FHA it's all talk and no walk, all show and no go."
- "As anyone with a few years in the mortgage business knows, there has been a precipitous decline in the number of mortgage companies that write loans through the often-cumbersome (although now somewhat-streamlined) FHA program. Not too long ago, so-called govvie loans like FHA and VA, were almost 25% of the mortgage market. Now, they comprise less than 3%. There are many reasons for the decline, not least the incompetence and intransigence of the FHA."
- "Another reason for the decline has been the rise of subprime, but what is not often pointed out when the increase in subprime originations is discussed is that the inability of most mortgage brokers to originate FHA loans, and the difficulty in doing them even when one is inclined to offer them, are among the primary factors that led to that rise."
- "Mortgage brokers, who now originate between 50% and 75% of all residential mortgage loans in this country, are effectively barred from originating FHA loans because of burdensome paperwork, maddening bureaucracy and expensive audit requirements. (I am told as much as \$11,000 annually for an audit.) If your product isn't available at Wal-Mart, K-Mart, Kohl's these days, chances are the average American consumer will never hear about it. The same goes for home loans. Mortgage brokers - and the originators who work for them - are the nation's independent, commissioned mortgage sales force, and they don't have the FHA arrow in their quivers. The product isn't being pushed to the American mortgage consumer because the group that is most in touch with that consumer doesn't have that product on its shelf. No wonder few FHA loans are written nowadays."

- “The FHA, not surprisingly, doesn’t seem to understand this. Mired hopelessly in the past, preferring to deal with banks and mortgage bankers as if this were still 1960, HUD and the FHA have failed to ensure that the largest mortgage sales force in the country has ready access to its products. I wouldn’t be surprised if many FHA bureaucrats had previous careers as high-level executives at K-Mart, W.T. Grant, Ames, Zayres, Montgomery Ward, GM, Chrysler and Ford. They’re clueless, out of touch and arrogant.”
- “As a board member and charter member of the National Association of Responsible Loan Officers, I met with Mr. Montgomery and his staff at his HUD office last year. Although they were polite and accommodating, I quickly came to realize that they just don’t get it. It’s like they think this is 40 years ago and everyone goes to their local bank for a mortgage loan. I left the meeting distressed and puzzled by how little the FHA understands about today’s mortgage product delivery system, and how out of touch with the mortgage brokerage industry they are. I told Mr. Montgomery that the FHA was going to have to do a lot of work to get brokers to offer their product, since, as far as I was concerned, they had overlooked this critical marketing force for most of the past 30 years, and had alienated mortgage brokers. ‘We’ve done quite well without you,’ I told him, ‘and we can continue to do quite well without you. You’ve got a lot of bridge-building to do.’ He took it well, although his staff responded with a stony silence. Apparently truth-telling isn’t welcome in the hallowed HUD halls, certainly not directly to a presidential appointee.”
- “I’m not sure, based on the two incidents that followed, that he and his staff understood, or took to heart, what I said. Let’s call that meeting strike one.”
- “Last year in Philadelphia at the annual convention of the National Association of Mortgage Brokers, where many wholesale lenders had huge and expensive booths staffed by large numbers of enthusiastic and accessible (and probably commission-based) sales staff, the FHA had a small, unadorned table manned by two young, very bored representatives who spent the day talking to one another. A few brochures were scattered on the table, and no attempt was made to engage any passersby. ‘Why did the FHA even bother to send anyone?’ I wondered. It sent a terrible message: ‘We’re here, but we don’t really want to be’” I see this same desultory presentation repeated at the many regional mortgage conferences I attend. This terrible message - that the FHA doesn’t really care - is being communicated to mortgage brokers around the country, at taxpayer expense. Nice. Let’s call that strike two.”
- “Then, in mid-March, Mr. Montgomery spoke briefly - very briefly - and perfunctorily to the annual NAMB Legislative and Regulatory Conference in Washington, droning on in a monotone, stumbling through a speech he had obviously not read before he presented it. A ‘busy travel schedule’ precluded him from taking questions from the brokers. Now mind you, these were the leaders of all of the state broker associations, the very leaders and brokerage owners who would decide if they and their staff would offer FHA loans to borrowers rather than just subprime loans. It was a marvelous marketing opportunity for Mr. Montgomery - one can think of none

better - and he was 'too busy' to engage them? Were FHA a private company, I can assure you the CEO would have made the time. In fact, the CEOs of a number of companies were, indeed, in attendance at the NAMB conference, some even giving hour-long presentations. The FHA blew it, again. Mr. Montgomery's boss, the HUD secretary, was invited to the conference but no-showed. Hey HUD, we get it - you don't care about us! HUD apparently has better things to do than talk to people who originate more than half of the residential mortgage loans in this country. That would be strike three."

- "Until the FHA pays more attention to mortgage brokers - actually cultivates a relationship with them, works to increase the minimum loan amounts and drops its audit requirement in favor of a surety bond - the agency will not be successful in its quest to grab a bigger slice of the mortgage market pie and will continue to lose ground. And, yes, I know that in baseball, its three strikes and you're out. But this isn't baseball - it's the FHA, to which the mortgage industry owes much, so I say to Mr. Montgomery and the FHA, you've got a few more swings left, but not many. Most mortgage brokers don't even consider you a player, but some are willing to let you have a few more cuts at the ball. If, however, the FHA keeps treating mortgage brokers like they're the minor leagues, then the FHA program will eventually get the bean ball. And then FHA will really be out - although I'm not even sure they would care. If they aren't willing to hustle, let's just release them. And if the whole team is that way, let's just shut down the entire league. It's too expensive for the American taxpayer, and isn't doing the American homeowner and homebuyer any good. Let's just say, 'Thanks for the memories, FHA, but we're movin' on!'" (*MortgageLine*, Christopher Cruise, 06/11/07)

Ginnie Mae to securitize first pool of FHA-insured reverse mortgages

- Ginnie Mae is "on track" to securitize its first pool of FHA-insured reverse mortgages know as Home Equity Conversion Mortgages (HECM), which will allow lender/issuers to sell federally mortgage-backed securities to Wall Street dealers for placement in real estate mortgage investment conduits with other mortgage products. "We think it is going to improve pricing for consumers and help originators find an efficient secondary market execution," said Ginnie Mae president Robert Couch. The Ginnie HECM structure will allow reverse mortgage lenders to securitize lump-sum payouts as well as monthly draws in pools as small as \$1 million.
- For a hypothetical \$100,000 HECM loan, the initial \$60,000 lump-sum payment to the borrower would be placed in one MBS, while \$1,000 monthly payments and other advances made by the lender/servicer could be bundled and placed in second and third mortgage-backed securities. "It is a fairly simple structure for investors," said Couch, but somewhat complex on the servicing side with one reverse mortgage [having] participations in multiple securities. "We have one servicer ready for the September rollout and we've got others that may be ready," he added.

- Couch is in line to be the new general counsel for HUD. If confirmed by the Senate, he will relinquish his post at Ginnie Mae. (*National Mortgage News*, Brian Collins, 06/04/07)

Farm Credit System / Farmer Mac

State bank supervisors argue that expanding FCA powers “will create safety and soundness issues by harming FDIC-insured institutions”

- In a letter to leaders of key Congressional committees, the Conference of State Bank Supervisors (CSBS) argued that the Farm Credit System’s plan to expand its lending authority to businesses and suburban housing could have the unintended consequences of “eroding the viability of community banks that serve our nation’s smallest and most vulnerable rural communities.” CSBS president and CEO Neil Milner wrote, “The [FCS] proposals threaten to erode the community banking system, which drives economic development in farm communities across the country. ‘We firmly believe expanding the FCS charter will create safety and soundness issues by harming FDIC-insured institutions.’ Milner also was critical of the FCS plans for expanding its business and home financing authority and says the plan will dilute farmer ownership of the cooperatively owned FCS by dismantling stock ownership rules. “Government-sponsored entities should be created to fill economic gaps, not compete with or undermine private enterprise,” he added. (*National Mortgage News*, 06/04/07)

Will FCA’s history repeat itself?

- In a June 12th editorial, *Peoria Journal Star*’s business editor Alan Guebert wrote, “Some things are more reliable than even death and taxes. Take the Farm Credit System (FCS, the System), for example. Since it’s Farm Bill-writing time again, the giant, government-sanctioned, cooperative ag lender is again asking Congress for favors to boost itself in the farm lending marketplace.”
- “The request, like the System, isn’t new. FCS was born in 1916 and, by the grace of Congress, has evolved into the Federal Land Bank, for long-term lending; the Federal Intermediate Credit Banks, for short-term, or production, lending; and the Bank for Cooperatives, to fund farmer-run cooperatives. Every time Congress gave it more rope, however, FCS snared itself in it. Expanded lending authority in 1971 led to a \$1.26 billion government bailout after ag’s ugly, mid-1980s collapse. (FCS repaid the loans, and \$440 million in interest, by 2005.) The near-crackup cost the System dearly. Farmers fled the lender for commercial banks and FCS’s share of total ag lending sagged from 30 percent in the mid-80s to nearly 20 percent five years later.”

- “Congress then rewrote FCS’s charter to both clean the System’s house and remodel it. Mergers were encouraged and the System shrank from more than 800 lending institutions in 1985 to just 95 much larger ones by late 2006. Tighter oversight by the Farm Credit Administration, FCS’s regulator, kept it on the straight and narrow, also. The reforms worked. By late 2005, the System had re-established itself as an ag lending powerhouse. Its market share was back to 30 percent, its lending portfolio grew from \$50 billion in 1985 to \$113 billion and profits quadrupled from \$660 million in 1990 to \$2.5 billion.”
- “Much of the growth, however, came through two government blessings, complain commercial bankers. First, FCS operates under a federal umbrella. Since it is chartered by the government, money raised through bond sales on Wall Street to then re-loan to rural America carries an implied guarantee that Congress will not allow the System to fail. Witness the 1987 bailout. That implication allows FCS to acquire loanable funds cheaper than commercial banks. The cheaper money is passed on to FCS borrowers through lower interest rates. In turn, grouse the bankers, the System cherry-picks their biggest, best customers because, after all, customer loyalty in banking is either a quarter point cheaper interest rate or a toaster.”
- “Second, accounting tricks in the government charter effectively lower FCS members’ tax rate to, incredibly, less than 5 percent, says Mark Scanlon, [with]... the Independent Community Bankers of America. Despite these enormous advantages already, FCS now wants Congress to grant it new lending authority. One key change in the draft 2007 Farm Bill would allow System banks to make housing loans in communities of up to 6,000 population (currently FCS is restricted to towns of 2,500 or less) and not require new housing borrowers to buy FCS stock, a bedrock cooperative principle.”
- “An even bigger change would allow System banks to lend to agribiz connected - even by a seemingly invisible thread - to the renewable fuel industry. In short, complain commercial banks, the draft Farm Bill language would open the barn door for FCS to loan money to any and all commercial enterprises in agriculture, from the local gas station to Tyson Foods, says Scanlon. ‘It would turn the Bank for Cooperatives into the Bank for Corporations,’ he predicts.”
- “The point is well-made: If FSC wants to compete head-to-head with commercial banks, then it should play by commercial bank rules. As such, Farm Bill writers should either keep FCS in its traditional ag lending role or strip it of its marketplace advantages.” (*Peoria Journal Star*, Alan Guebert, 06/12/07)

FCA's board of directors approves ANPR related to capital adequacy of the FCS

- At its June 14th meeting, the Farm Credit Administration (FCA) board of directors has approved an advanced notice of proposed rulemaking (ANPR) related to capital adequacy requirements for the Farm Credit System. Specifically, FCA is considering revisions to its capital rules, including changes that would more closely align its minimum capital requirements with the risks to which FCS institutions are exposed. FCA's objective is to develop a regulatory capital framework for FCS institutions that better reflects these advances and more closely aligns its capital requirements with the relative risks inherent in System institutions. By issuing this ANPR, the Agency is seeking comments that might help it fashion a proposed rule to improve the risk sensitivity of its capital rules, as well as to make other changes. The questions posed in this ANPR reflect some of the recent proposals made by other Federal financial regulators, but they are also tailored to fit the System's unique structure and mission.
- In other business, the board of directors approved its May 30th notational vote in which the board voted to allow CoBank, ACB, to include subordinated debt in permanent capital and total surplus and to exclude it from total liabilities when computing its net collateral ratio. The Board also imposed certain limitations, which were not publicly disclosed. (*USFed News*, 06/14/07)

Postal Service

Postal Regulatory Commission to hold public hearings on postal reform rules

- The Postal Regulatory Commission plans to get public input through public hearings, as the Commission develops new rules for the new rate regulation system set forth in the Postal Accountability and Enhancement Act enacted in 2006. "As part [of its] rulemaking... the PRC invites mail users from a broad cross-section of the mailing community to testify at ...hearings" in Kansas City, MO (June 22), Los Angeles, CA (June 28) and Wilmington, DE (July 9). (*DMNews.com*, Melissa Campanelli, 06/11/07)

What did postal reform really accomplish?

- In a white paper on postal reform published by the National Academy of Public Administration, Murray B. Comarow wrote, "The Postal Accountability and Enhancement Act (PAEA) of December 20, 2006 has been hailed as rescuing the Postal Service from a slide into oblivion, with disastrous economic and social

consequences. Now that the dust has settled, it may be useful to figure out what it does and doesn't do for all who depend upon the mails.”

- “Mailers supported the Act for two main reasons: They expected financial relief from escrow and military payments, and a rate cap for its market dominant products, which comprise ninety percent of its volume. The Act does not give financial relief until 2017, and perhaps not then. In fact, it increases costs by requiring billions to go to a new Retiree Health Benefits Fund. The result is a shortfall of \$600 million this year. The rate cap may work if there are no extraordinary costs, and if labor arbitrators respect the cap. The Act does not require them to do so; if an arbitrator makes a wage award that breaks the cap, there is no appeal.”
- “Some mailers supported this legislation, not for a specific reason, such as the hoped for rate cap, but because they say they distrust the Postal Service. They relish the idea of tough regulation by a PRC entrusted with new and unprecedented powers. These mailers justified their position anecdotally and in private...”
- “The labor unions, most but not all nonprofits, and competitors are pleased, with good reason. Board Chairman Jim Miller and Postmaster General Jack Potter are putting a good face on the situation, but they are truly dismayed, also for good reason: The basic business model, which has been at the root of concerns for the Postal Service’s viability, has not been altered by the Act. It has been made worse by the transfer of powers to the Postal Regulatory Commission.”
- “The Act is not devoid of merit. Its provisions on volume discounts, executive compensation, and standards for appointments as Governors or Commissioners are all to the good. PRC’s glacial and expensive rate-setting process is almost certain to improve... PAEA also gives the Postal Service more flexibility with respect to competitive products such as priority mail and bulk parcel post, which represent 10 percent of postal volume. This flexibility, however, must be exercised in accordance with PRC requirements, and may be more apparent than real, given PRC’s raw power to review any postal action on the basis of any complaint.”
- “But let me return to the core disease that afflicts this institution. The Act ignores a slow-growing, potentially lethal condition: the Postal Service’s outdated business model. Calcified by statutory constraints, this has been well known to Congress and all components of the postal community for years, but Congress will not acknowledge it, much less fix it...” (*National Academy of Public Administration: What Does Postal Reform Do?*, Murray B. Comarow, 06/07/07)

Postal Service strongly opposes S.1457, which would over-ride the agency’s collective bargaining agreements

- In a letter to Senate members, Postmaster General John Potter wrote, “The Postal Service strongly opposes S. 1457, the ‘Mail Delivery and Protection Act.’ This bill

would override current collective bargaining agreements and effectively eliminate an important tool needed by the Postal Service to continually introduce greater efficiencies into its operation. If enacted, with an exception of a very limited use, no new contracts for mail delivery could be initiated. The ability of the Postal Service to effectively manage its vast delivery operations would be largely eliminated, and new opportunities for small businesses to carry contracts for transporting and delivering mail would be eliminated. Currently 99 percent of our contract delivery services are performed by small, minority- or women-owned businesses. This use of private-sector services is not new. The Postal Service has used contractors to transport and deliver mail since 1785, when Congress first authorized the Post Office Department to contract with stagecoach companies.” (*Association of Postal Commerce*, 06/14/07)

The critical question: Which side are you on?

- In his President’s Message in the June issue of *Postal Record*, National Association of Letter Carriers President William Young wrote, “As pleased as I was to hear NAPUS President Dale Goff tell the [House] subcommittee that ‘with contractors, you get what you pay for,’ and as thrilled as I was to hear NAPS President Ted Keating declare that contracting out letter carrier work ‘will be the death of the Postal Service,’ I was flabbergasted by the President of the APWU. He repeatedly— and hypocritically—lobbied the subcommittee not to take legislative action [i.e., passage of H.R. 282, which calls on the USPS to discontinue contracting out mail delivery], calling contracting out a “bargaining issue” best left to the parties and to arbitration. That’s the same disingenuous line being peddled by the USPS on Capitol Hill.
- It’s no secret that I have never enjoyed a good working relationship with the President of the APWU. It seems we inhabit different worlds and see issues from entirely different perspectives. Still, you don’t often see a national union leader cozy up to ideologues to endorse union-busting and outsourcing. But I saw it and so did anybody watching C-SPAN.”
- The good news is that APWU is just as isolated and out of step on contracting out as it was on postal reform. As of mid-May, more than 140 members of Congress had co-sponsored H.R. 282, which calls on the USPS to discontinue contracting out mail delivery. ...The wisdom of ‘Which Side Are You On?’ is as compelling today as it was 75 years ago when it was written about a coal miners’ strike in Harlan County, Kentucky. Those miners overcame the armed vigilantes and the scabs. With your help [e.g. union members], we can certainly overcome the misguided views of L’Enfant Plaza and even its most unlikely allies. (*Postal Record*, William J. Young, 06/14/07)

APWU sues USPS and an advisory committee for “conducting policy making in secret”

- In a June 6th message to members, American Postal Workers Union (APWU) President William Burrus wrote, “The APWU, together with an organization representing a coalition of consumers and nonprofit mailers, has filed a suit challenging secret policy-making by a Postal Service advisory committee. The panel, the Mailers Technical Advisory Committee, is made up of trade associations that represent large business mailers. Co-chaired by major mailer representatives and postal officials, MTAC — acting through ‘work groups’ — commissions studies and makes recommendations to senior USPS management on postal operations, postal rates, and postal regulations....MTAC has refused to admit to its membership the Consumers Alliance for Postal Services (CAPS), which is made up of nonprofit associations, small mailers, and individual consumers that rely on the Postal Service to communicate with their members. CAPS is chaired by William Clay Sr., the former Chairman of the House Post Office and Civil Service Committee.” (*APWU Web News Article 348-07*, William Burrus. 06/06/07; Association for Postal Commerce, 06/07/07)

Postal Regulatory Commission appoints its first inspector general

- Dan G. Blair, chairman of the Postal Regulatory Commission, announced that Jack Callender has been appointed the PRC’s first inspector general [effective June 25th], as required by the Postal Accountability and Enhancement Act of 2006. Previously, Callender served as minority counsel to Ranking Member Tom Davis (R-VA) on the U.S. House of Representatives Committee on Oversight and Government Reform. (*Association for Postal Commerce*, 06/12/07)

Resolution adopted by Senate Homeland Security and Governmental Affairs Committee affirming the constitutional protections of sealed domestic mail

- On June 13th, the Senate Homeland Security and Governmental Affairs Committee approved a resolution, coauthored by Senators Susan Collins (R-ME) and Joseph Lieberman (ID-CT), which reaffirms the constitutional protections of sealed domestic mail. The Committee’s approval paves the way for the full Senate to consider the legislation, which is also cosponsored by Senators Tom Carper (D-DE), Norm Coleman (R-MN), Daniel Akaka (D-HI), Russ Feingold (D-WI), and Patrick Leahy (D-VT). (*DMNews.com*, Melissa Campanelli, 06/15/07)

Maximizing right turns on postal mail routes saves gas

- *Sustainable Industries* reports, “Avoiding left turns is helping United Parcel Service Inc. save loads on gasoline. Using electronic processing technology to plan delivery routes around right-hand turns, the company is taking full advantage of a U.S. traffic law that was first implemented in the 1970s as a way to save gas... The combination of tracking technology and a right-turn policy helped USPS save 3 million gallons of fuel and over 28 million miles in 2006, according to ABC News.” (*Sustainable Industries*, Sarah Crespi, 06/11/07)

Pay nominal fee to opt out of junk mail

- *Stopthejunkmail.com*, a Boulder, CO-based company, provides a convenient and cost-effective way for subscribers to opt out of receiving unsolicited postal junk mail. For a nominal fee, the website removes subscriber information from mailing lists and, through a partnership with American Forests Organization, plants a tree in an effort to offset the depletion of forests caused by junk mail. The company’s mission is to help consumers eliminate unwanted postal junk mail for households and small businesses and to protect consumers’ privacy by reducing the number of times their names and addresses are shared without their knowledge. (*StopTheJunkMail.com Press Release*, 06/11/07)
- Speaking of junk mail, *Associated Press* reports, “As a freshman congressman, Daniel Lipinski wanted to ensure constituents knew what he was doing, but he rarely got mentioned in Chicago news stories. So he spent \$230,000 in taxpayers’ money to get his message across. [Representative Rahm Emanuel was a close second, spending \$215,000]. The Illinois Democrat spent more than any other member of the state’s congressional delegation on mailings to constituents during 2005-2006 through the use of ‘franking’ privileges.”(*Associated Press*, Dennis Conrad, 06/09/07)

TVA

Senator Alexander opposes renewable energy amendment

- Tennesseans would face higher utility bills and giant wind mills would disfigure mountaintops from Knoxville to Chattanooga if Congress passes an amendment to the energy bill, requiring utilities to generate 15% of their electricity from renewable sources by 2020, warned Senator Lamar Alexander (R-TN). The amendment, which Senate Energy Committee Chairman Jeff Bingham (D-NM) is expected to offer, is so narrowly defined that the only way states could adhere to the standard would be to build giant wind turbines, which would not be effective in Tennessee or much of the Southeast due to low winds in the region, said Alexander. Utilities that don't meet federal standards would pay penalties to the federal government, which would be passed along to their customers. TVA estimates that the proposal would add \$410 million a year to Tennesseans' utility bills. "Residential homeowners can't afford these taxes, industries will take their jobs to states with cheaper power and tourists will spend their dollars where they can see mountaintops instead of giant wind turbines," said Alexander. The wind turbines are unsightly with a height of more than 400 feet and rotor blade span of 240 feet, he added. Alexander called Bingham's proposal as a "classic example of a Washington, D.C. one-size-fits-all plan that doesn't fit Tennessee or most of the Southeast." He added, "Wind may be fine in North Dakota or Colorado, but not for Tennessee." Alexander said, "We need energy independence in America, but we need energy independence that makes sense." A better choice for clean, reasonably priced electricity in Tennessee would be more conservation and efficiency, nuclear reactors, and clean coal, he added. (*Chattanooga Times Free Press*, Herman Wang, 06/13/07; *Knoxville News-Sentinel*, Michael Collins, 06/13/07)
- According to a new poll released by Chicago-based Invenergy Wind LLC, owners of 15 of the 18 wind turbines on TVA's wind farm near Oliver Springs, TN, a random telephone survey conducted by Telephone Strategies Group interviewed "1,047 likely registered voters on June 5-6. Approximately 74% of the those polled want increased use of wind energy in Tennessee. Moreover, the poll showed that 82.8% of those surveyed believe "wind energy is a viable source of pollution-free electricity in Tennessee" and 78.7% know that their state ranks near the bottom of states producing wind power. "The residents of Tennessee are saying 'yes' to more wind power," said Invenergy's Buffalo Mountain manager Karl Eiermann. [According to Telephone Strategies' website, the polling company provides "voter identification" services, "persuasion" programs, and "get-out-the-vote" campaigns for groups such as the Democratic National Committee, the Tennessee Democratic Party, the Tennessee Senate and House Caucuses, the NAACP, the Sierra Club, etc.] (*Associated Press*, Duncan Mansfield, 06/12/07; www.tsgphones.net)

- On June 14, Senate Democrats ran into staunch Republican resistance to the Bingham Amendment, which would require utilities to produce at least 15% of their energy through wind, solar and other renewable sources by 2020. [Only 2.4% of the country's electricity is produced through renewable sources today.] The Democrats were forced to set aside the renewable fuels proposal, when it became clear that they lacked the 60 votes needed to proceed. In response to the impasse, Democrats said they will propose nearly \$13.7 billion in tax breaks to promote clean energy, biofuels, more fuel efficient vehicles and conservation on June 19th in the Senate Finance Committee. The proposal would extend dozens of tax breaks, such the one for building wind turbines and also would create incentives such as tax credits for technology to capture carbon dioxide - the leading greenhouse gas - from power plants. (*Associated Press*, H. Josef Herbert, 06/14/07)

TVA's new direction

- In a June 5th editorial, the *Northeast Mississippi Daily Journal* wrote, “[TVA] directors [adopted] ...at [their] monthly board meeting ...a major, long-range plan that would steer the seven-state public utility toward greater energy efficiency. ...The board's new policy evolved from a series of public meetings across the seven-state region, with customers telling the authority it must operate more efficiently in the face of at least 2 percent annual growth in electricity demand. Part of the new policy focuses on environmental concerns like cleaner energy and energy production in light of global warming forecasts and climatic changes possibly associated with it.
- “Five elements are central in the plan:
 - Simplifying rates and having them more accurately reflect the cost to serve, with system-wide emphasis on energy efficiency and reductions in peak power demands to prepare for even higher growth. Distributor-owned generation means hypothetically that any of the 158 distributors in the TVA system could own their own power sources.
 - Giving safety greater emphasis and opening communications with all customers would become a higher priority, building confidence.
 - Retiring debt on a schedule linked to useful life of assets and better justification of capital expense would strengthen finances in the long term.
 - TVA would enhance its nuclear capacity. It has re-started a second nuclear generator, last month, at the Browns Ferry Nuclear Plant in northern Alabama. It tentatively plans to bring on line three other reactors at Watts Bar in Tennessee and Bellefonte, also in northern Alabama, by 2019. The new nuclear projects will cost about \$18.5 billion, but TVA says it can accomplish the financing with one single-digit rate increase, probably in 2009.

- Deliver reliable generation and transmission services, including nuclear safety and reducing carbon emissions.”
- “Few envisioned TVA’s expansion into the giant business it has become, but its ability to fulfill its other primary mission of economic development has brought it to the apex of power generation leadership. If the authority succeeds in its goals, our region remains better-empowered to continue growing.” (*Northeast Mississippi Daily Journal*, 06/05/07)

TVA names Preston Swafford as the utility’s fossil power chief

- On June 11, TVA announced the retirement of longtime executive Joe Bynum and appointment of his successor, Preston Swafford, who will serve as the agency’s head of its 11-coal burning plants. Swafford, who joined TVA in 2006, has more than 23 years of utility experience. Previously, he was senior vice president of nuclear support, overseeing nuclear plant operations for Exelon Corp. (*Associated Press*, 06/11/07)

TVA will phase out big, year end bonuses for management

- Big year-end executive bonuses may be phased out at TVA, as the utility moves toward a more corporate-like model of performance-based salaries and compensation. “What we are trying to do is have some realistic pay and then have a realistic bonus system that is tied to performance,” said TVA Chairman Bill Sansom in a recent interview with *The Associated Press*. In 2006, TVA paid \$10.5 million in bonuses last year to 143 executives. Under the plan recently approved by TVA’s board of directors, base salaries for the agency’s management could go up and bonuses go down starting this fall. While the total compensation for executives may not change greatly, public perception will. In August, a more detailed plan will be presented to the TVA board, which will shape the fiscal 2008 budget.
- Although it is a self-supporting federal agency, TVA was prevented by law from offering any employee more than a congressional salary \$140,000 in 2006. To compete against privately-owned utilities for high-priced executive talent, TVA padded its pay packages with goal-oriented bonuses and other incentives. In 2006, TVA’s president and CEO Tom Kilgore, TVA’s top-paid employee, last year received nearly \$1.6 million, which was comprised of a \$140,000 salary, \$511,984 in additional annual compensation, \$627,861 in incentive awards, \$300,000 in deferred compensation and a \$6,300 match to his 401(k). According to a Towers Perrin Energy Services study, Kilgore’s pay “paled” to the \$5.3 million average for the top executive at a comparable \$9 billion corporation, according to a. Recent changes made by Congress to the TVA Act, which expanded the board of directors and created a new full-time chief executive officer, also lifted the congressional pay cap on TVA officers. (*Associated Press*, Duncan Mansfield, 06/05/07)

USEC signs a five-year power contract with TVA

- USEC, Inc. has signed a five-year contract with TVA for electric power for its gaseous diffusion uranium enrichment plant in Paducah, KY. “We’re pleased to lock in a long-term rate agreement with TVA for electric power for the Paducah plant. USEC’s baseload power needs make it TVA’s largest industrial customer,” said John K. Welch, USEC president and CEO. “The new contract helps USEC mitigate and manage the risk of rising power prices. USEC needs the certainty and predictability of a long-term power agreement as it continues to provide a reliable source of enriched uranium fuel to our nation’s nuclear power plants.” (*USEC, Inc. Press Release, 06/07/07*)

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