

The **GSE** REPORT™

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Major Events

House of Representatives passes the Federal Housing Finance Reform Act (H.R. 1427)
by a vote of 313-104

Bush administration support of the H.R. 1427 is uncertain

Fannie Mae and Freddie Mac applaud the passage of H.R. 1427

“Freddie guts Frank”

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H.R. 1427 is “worse than the status quo”

A good idea whose time has come?

The biggest risk in the U.S. financial system: Fannie Mae and Freddie Mac

- On May 22nd, the House of Representatives passed H.R. 1427, the Federal Housing Finance Reform Act of 2007, by a bipartisan vote of 313 to 104 [all nay votes were cast by Republicans]. The legislation will overhaul the regulatory oversight of Fannie Mae, Freddie Mac and the Federal Home Loan Banks, and create a new, independent regulator with powers analogous to current banking regulators, whose primary responsibility will be to ensure the safety and soundness of the GSEs. The bill also creates an off-budget, non-taxpayer financed affordable housing fund, which will dedicate hundreds of millions of dollars for the construction, maintenance and preservation of affordable housing with the first year of the fund to be dedicated to the hurricane stricken areas of the Gulf Coast, and billions of dollars over the next five years for affordable housing nationwide. H.R. 1427 is the product of both bipartisan legislation in the 109th Congress and careful discussions and compromise with the Department of Treasury. The final bill is the result of a series of deliberations and debate of 36 amendments in the House of Representatives.
- House debate centered principally around the bill’s proposed creation of an affordable housing fund from fees garnered from Fannie Mae and Freddie Mac and an amendment which would limit the new regulator’s authority to restrict the GSEs’ mortgage portfolios based solely upon safety and soundness considerations for the Enterprises. The House defeated all but one Republican-introduced amendments related to the GSEs’ affordable housing fund. By a vote of 235-188, the House passed an amendment sponsored by Representative Tom Price (R-GA), which would require owners or renters of facilities built with the support of revenues from the affordable housing fund to prove that they are legal residents of the United States with secure forms of identification. By a vote of 217-205, a second Republican

amendment [sponsored by Representative John Doolittle (R-CA)] was passed, which would prevent the GSEs from buying mortgages in the secondary market that were made to borrowers without valid Social Security numbers.

- The amendment offered by Representatives Melissa Bean (D-IL) and Randy Neugebauer (R-TX) to restrict the GSE regulator's authority to force reductions in the Enterprises' mortgage portfolio passed on a voice vote on May 17. The amendment later passed by a roll-call vote of 383-36 with House Financial Services Committee chairman Barney Frank voting with the minority. After the vote was taken, Frank said that the amendment would ultimately be revisited in conference. "I don't consider it a totally settled issue," said Frank. "We will continue to work on this." Representative Lynn Westmoreland (R-GA), who pushed for the roll call vote on the Bean-Neugebauer amendment, said "That was an amendment that needed to have a vote, so when it went to conference the numbers would be there. A voice vote, that is one thing. When you have a recorded vote, it shows a little strength when you get to conference."
- GSE regulatory reform legislation still faces major obstacles in the Senate, where members are deeply divided on how to regulate the Enterprises, and pressure from the Bush administration for stricter regulatory control over the GSEs. Industry observers say that a legislative framework that provides assurances that Fannie Mae's and Freddie Mac's mortgage portfolios [totaling a combined \$1.4 trillion] do not represent a "systemic risk" will be critical to winning the president's signature on a final bill. In an interview during the week of May 14th, Senator Richard Shelby, ranking member of the Senate Banking Committee, said he would oppose the GSE regulatory reform bill if something like the Bean amendment were included in the legislation. "We're open to debate on everything, but there are things it makes no sense to weaken," said Shelby. "You don't want to create a regulator and give the regulator no power." He added, "I don't think we should rush to judgment on any meaningful piece of legislation. We should examine it in its total package, and we will." In an interview with *Marketplace*, Bert Ely said, "There are a number of aspects of this legislation that important parties for one reason or another don't like. And that's a recipe for paralysis over in the Senate. Among the concerns is an amendment that would water down control over the financial soundness of the mortgage giants. It would put the focus on the risk Fannie and Freddie's actions pose to their own bottom lines — not to the overall U.S. economy. And then there's the political part. Chairman Dodd of the Senate Banking Committee is running for president." Brian Gardner, an analyst with Keefe, Bruyette & Woods, said, "I really get no sense of an interest in compromising, and until that changes, it really is not in Senator Dodd's interest to try to move a bill." Gardner added, "From the markets perspective, on the price of the stocks, a bill will have no effect. If this legislation were to be enacted, it doesn't change the regulatory structure that much and wouldn't have a very big effect on the two companies."
- Representative Barney Frank (D-MA), chairman of the House Committee on Financial Services, said, "We will now have a strong new regulator to restore

confidence in the GSEs. It will keep housing finance affordable and begin the important task of providing needed housing in the Gulf Coast,” Representative Richard Baker (R-LA) said, “This is a great step forward in a long-standing effort to build a stronger wall between the trillion-dollar liabilities of these financial giants and the taxpayers’ pockets. I am particularly proud of the fact that in the first year after enactment this legislation will provide significant resources to post-hurricane Louisiana to help rebuild, recover, and redevelop our communities. While I am disappointed by an amendment weakening the regulator’s authority over the companies’ investment portfolios, my vote for passage of the bill is to keep this important process moving forward, and I will work with the White House, the Treasury, members of the Senate, and Chairman Frank and others in the House to improve the final legislation.”

- On May 23, Chris Dodd issued the following statement regarding passage of H.R. 1427: “I commend Barney Frank and the House for their efforts. Homeownership is the cornerstone of the American dream and we need to do everything possible to make that dream a reality. Clearly, GSE’s can play an important role in advancing that goal. I believe our nation needs a stronger regulatory structure and a deeper commitment to meeting the housing needs of the American people. I am committed to continuing to find common ground to address this important issue in a bipartisan, timely and thoughtful way.” Dodd told reporters that he will continue to work behind the scenes to broker a compromise in the Senate on GSE regulatory reform legislation. “Senator Shelby and I are talking,” Dodd said. “We’re spending a lot of time working already with each other on this to see if we can come to some accommodation on that.” (*Congress Daily*, Bill Swindell, 05/23/07; *National Journal’s CongressDaily*, 05/23/07; *American Banker*, Rob Blackwell, 05/21/07; *Marketplace*, Jeremy Hobson, 05/23/07; *Dow Jones Newswires*, Damian Paletta, 05/22/07; *Washington Post*, Marcy Gordon, 05/23/07; *Wall Street Journal*, Damian Paletta, 05/23/07; *Press Release by Senator Chris Dodd*, 05/22/07; *House Financial Services Committee Press Release*, 05/23/07; *CQ Today*, Michael Crittenden, 05/22/07; *Bureau of National Affairs*, Richard Cowden, 05/23/07)

Bush administration support of the H.R. 1427 is uncertain

- In a May 22 statement, Treasury Under Secretary for Domestic Finance Robert K. Steel said, “The House made progress to reform the oversight of the housing GSEs today. Treasury commends Chairman Frank for working in a bipartisan manner to pass legislation addressing this goal. Regretfully the House significantly weakened the regulator's abilities to examine systemic risk issues. Additionally, we remain troubled by the provisions relating to conforming loan limits, the Federal government's appointment of directors and aspects of the affordable housing fund. Treasury appreciates the efforts of the Financial Services Committee to advance the process of creating a strong GSE regulator but as a result of amendments adopted on the floor, the Department does not believe this bill adequately guards our financial system with the necessary oversight. We look forward to working with the Senate to

address reforms critical to the safety and soundness of the U.S. financial system.”
(*Department of the Treasury Press Release, 05/22/07*)

- In a May 22 statement, OFHEO Director James B. Lockhart, III said, ““We commend Chairman Frank and Members of the U.S. House of Representatives for passing a balanced bill that will strengthen the nation’s housing finance system by enhancing oversight of Fannie Mae, Freddie Mac and the Federal Home Loan Banks. H.R. 1427 gives the new regulator the tools necessary to ensure the safety and soundness of the GSEs so they fulfill their congressionally-established mission, especially affordable housing. It is noteworthy that there was virtually universal agreement by all Members of the need to create a new and stronger regulator for the housing GSEs. We recognize that a few issues remain and we pledge to continue working with the House and the Administration on those issues. We are hopeful that the Senate will act quickly on this important legislation.” (*OFHEO Press Release, 05/22/07*)

Fannie Mae and Freddie Mac applaud passage of H.R. 1427

- In a May 22 statement, Brian Faith, Fannie Mae’s managing director of communications, said, “Today's passage of H.R. 1427 by the full House is an important step in the process of strengthening the safety and soundness oversight of our company and the GSEs. We're pleased the Bean/Neugebauer amendment was passed because it clarifies an important aspect of regulatory discretion over the GSE mortgage portfolios. We congratulate Chairman Frank for securing passage of the legislation with broad support. While there are aspects of the legislation we would hope to see improved as the process unfolds, we remain committed to working constructively with members of Congress and continue to support passage of GSE regulatory reform legislation in this session. Having a credible and effective regulatory regime for the GSEs is important for the GSEs and the marketplace as a whole.” (*Fannie Mae Press Release, 05/22/07*)
- In a published statement, Freddie Mac said, “On May 22, the U.S. House of Representatives passed H.R. 1427, ...a bill that would strengthen the regulation of Freddie Mac, Fannie Mae and the Federal Home Loan Banks. Freddie Mac supports the enactment of legislation, and H.R. 1427 is a major step forward in this process. We applaud Chairman Frank for his leadership in guiding the bill. Improving GSE regulation is in the best interests of Freddie Mac, the housing finance system, and the millions of families we serve. We remain concerned about how certain provisions of this bill could be implemented – especially the possibility of capital requirements not tied to the actual risks of our assets, and business activity regulation that constrains our ability to respond quickly to a changing marketplace. We will continue working with Congress on addressing these concerns in final legislation.” (*Freddie Mac Press Release, 05/22/07*)
- During the first quarter of 2007, the political action committees of Fannie Mae and Freddie Mac gave a total of \$350,200 to lawmakers. (*Washington Post, 05/17/07*)

“Freddie guts Frank”

- In a May 22 editorial, the *Wall Street Journal* wrote, “Barney Frank has received kudos for his ‘statesmanship’ in ushering a compromise on oversight of Fannie Mae and Freddie Mac through his Financial Services Committee. But all that diplomacy was blown away ...by the mortgage giants' allies in the House. Their amendment to Mr. Frank's bill, which passed by voice vote Thursday night, guts the one provision that made it worth the effort. What's left is a regulator who would lack the authority to limit the risk that Fannie and Freddie's \$1.4 trillion mortgage-backed securities portfolios pose to the financial system, plus a \$500 million a year boondoggle that goes by the euphemism ‘affordable housing fund.’”
- “Mr. Frank says he stands by his handshake with Treasury Secretary Hank Paulson, and will work to get the portfolio-limitation power restored via House-Senate negotiations. But Thursday's floor ambush by Democrat Melissa Bean and Republican Randy Neugebauer calls into question whether Mr. Frank has the votes to make good on that promise. With Fannie and especially Freddie back to their arm-twisting ways on the Hill, the answer would appear to be ‘no.’”
- “That leaves the White House and Treasury with some decisions. Administration officials were cautious about the Bean-Neugebauer amendment when first proposed, but Fannie and Freddie's friends are betting the Administration wants a deal enough to accept even a bad one. However, a ‘reform’ that does nothing to reduce the problem of putting so much housing risk into two companies, and which also includes an annual \$500 million donation to ‘housing’ activists such as Acorn is worse than the status quo.”
- “Last year, when reform negotiations faltered, Treasury started grumbling about its power to approve Fannie and Freddie's applications to issue new debt. That threat never went anywhere, but it's still out there, and could be used to rein in Fan and Fred without any change to existing law. Restricting their borrowing to debt that actually furthers their original housing ‘mission’ might just bring the companies around to either substantive reform or, better, full privatization.”
- “The alternative is to hope that Mr. Frank's word will prove better down the road than it did on the House floor last week. This assumes he and other Democratic leaders are sincere, as opposed to pretending to favor reform while letting Fannie and Freddie have their way and pleading ‘nolo contendere.’ Given Congress's history of placating these companies, and their lobbying clout, you don't have to be a cynic to suspect the worst.” (*Wall Street Journal*, 05/22/07)

Cracking open the honey pot

- In a May 22 editorial, *National Review Online* wrote, “No one disputes that ...Freddie Mac and Fannie Mae need reform. But congressional Democrats look at a reform bill moving through the House as an opportunity to crack open a honey pot for their political allies. Led by House Financial Services Committee chairman Barney Frank, they have written into the bill a provision that would pump money into the coffers of radical liberal activists. The bill ...calls for the creation of an ‘affordable-housing fund’ to be financed by Freddie Mac and Fannie Mae. Those responsible for this provision maintain that the fund is intended to direct money toward housing programs that would benefit the poor. During the first year, a Finance Committee press release says, the money would be largely directed toward areas affected by Hurricane Katrina.”
- “True enough. But there is a convenient catch for the Democrats. The money in the fund — expected to total more than a billion dollars over the next five years — would be siphoned through hard-Left activists like ACORN (the Association of Community Organizations for Reform Now). ACORN is a fringe political group of the ‘stop being so polite’ variety, and it has a history of shady activity. Promoting environmental regulations and government programs is its stock in trade, and it has long advocated such causes as a ‘living wage’— even while quietly asking to be exempt from California laws that would force it to raise wages for its own workers. A 1994 grant from AmeriCorps to the group’s housing division — the same division that would benefit from the housing fund — was cut off after an investigation determined that the group had engaged in political activity using AmeriCorps recruits. Throughout the country, the group has run voter drives that the Heritage Foundation says were ‘aimed at signing up voters most likely to vote against the President.’ The election director of St. Louis all but accused the group of fraud. ACORN ran afoul of the law in Kansas, where four of its employees were indicted for turning in false registration information to election officials. And in Ohio, one former ACORN employee traded crack cocaine for fraudulent registration materials.”
- “A variant on the affordable-housing fund was included in a 2005 version of the reform bill, and many Congressional Republicans had harsh words for it at the time. Sensing that it was little more than a money dump for groups friendly to Democrats, Representative Tom Feeney (R- FL) responded incredulously to the suggestion that it wouldn’t be used for political purposes: ‘Could you imagine if I had proposed an amendment to give \$500 million to the National Rifle Association and said they could not use it to educate school kids on guns?’ Thanks to some tricky maneuvering by Congressman Frank back then, the bill passed in the House, but it stalled in the Senate. There, Senator Richard Shelby (R-AL), then the Banking Committee chairman, proposed a version of the bill with the fund removed.”

- “Unfortunately, the White House announced last week that it would support the bill as currently written, even though it opposes the housing fund for its susceptibility to ‘political influences.’ A recent amendment to the legislation by Rep. Roy Blunt makes disbursement of the funds somewhat more transparent, but this is weak remedy. A better approach would be to do away with the fund entirely.”
- “Senator Shelby has yet to take a position on the fund this time around (and the bill has not reached the Senate), but we hope that he and other Republicans in Congress will refuse to support any measure that includes the fund. It doesn’t take much to realize that doling out cash to radical groups like ACORN is, well, nuts.” (*National Review Online*, 05/22/07)

H.R. 1427 is “worse than the status quo”

- On May 22, Cato@Liberty [the Cato Institute’s blog] wrote, “[The Bean-Neugebauer] amendment to Mr. Frank’s bill, which passed by voice vote..., guts the one provision that made [the bill] worth the effort. What’s left is a regulator who would lack the authority to limit the risk that Fannie and Freddie’s \$1.4 trillion mortgage-backed securities portfolios pose to the financial system, plus a \$500 million a year boondoggle that goes by the euphemism ‘affordable housing fund.’ ...That leaves the White House and Treasury with some decisions. Administration officials were cautious about the Bean-Neugebauer amendment when first proposed, but Fannie and Freddie’s friends are betting the Administration wants a deal enough to accept even a bad one. However, a ‘reform’ that does nothing to reduce the problem of putting so much housing risk into two companies, and which also includes an annual \$500 million donation to ‘housing’ activists such as Acorn is worse than the status quo. (Cato@Liberty, 05/22/07)

A good idea whose time has come?

- In a May 25th editorial in the *American Banker*, AEI resident fellow Alex J. Pollock wrote, “The latest GSE reform bill, HR 1427, has passed the House of Representatives and is presumably headed for consideration by the Senate. Meanwhile, Fannie Mae and Freddie Mac are moving back toward business as usual.”
- “I believe the creation of a combined regulator for Fannie, Freddie, and the Federal Home Loan banks, as the bill provides, is a good idea whose time has come. It makes sense to have a single perspective from which to oversee the trillions of dollars of government-sponsored debt and mortgage-backed securities issued by the three government-sponsored enterprises. But the bill would not cut back on the GSEs’ fundamental government-granted competitive advantages, which deliver implicit subsidies to their shareholders. The special government status of their debt and their lines of credit with the Treasury would be left intact, while the conforming loan universe would be expanded.”

- “In addition, Fannie and Freddie would become the source of a large government affordable housing program. Therefore, one key result of the bill would be to promote the financial market's belief that the GSEs are even more closely tied to the government than before - to reinforce their government-supported status, and to reduce market discipline even further, despite increasing regulation.”
- “Fannie and Freddie did have their accounting scandals. They have had severe embarrassments, replaced their managers, and are out a couple of billion dollars to pay for restating their accounting records. (The scandals appear to be one of the all-time great profit opportunities for accounting firms.) But the global debt markets don't mind. With current financial statements or not, Fannie and Freddie debt and securities continue to sell at narrow spreads and top credit ratings. Even when the GAAP financial statements are finally brought up to date, the market knows that they will be opaque and largely meaningless, anyway, because of FAS 133. However, this won't really matter, because for the fixed-income markets, the real issue is the comforting presence of the government's credit, which the GSE reform bill would make even more comforting.”
- “Another key result of the bill would be increased market share for Fannie and Freddie, because of the increased conforming loan limits for ‘high-cost areas.’ In these areas (however defined), the limit would rise from the current \$417,000 to the median price for a house in the area. The maximum would be 150% of the general conforming limit, so under current circumstances, the maximum would be \$625,500 - moving a good bit of what is now the private ‘jumbo’ loan market into GSE-dominated turf.”
- “Note that this would be a maximum loan amount, so for an 80% loan-to-value mortgage, Fannie and Freddie would be financing a house costing about \$780,000. It is an interesting piece of logic to take the median price and turn it into a loan limit. For an 80% LTV loan, the house being financed at the limit would have a price of 125% of the median. The fundamental idea is that in high-cost areas, Fannie and Freddie should be limited to mortgages for houses costing about 125% of the median or less. They would not be allowed to finance more expensive homes (except in the case of low-LTV mortgages).”
- “This seems a reasonable principle, but why should it apply only to high-cost areas? We could apply it everywhere and define the conforming loan limit as the area median price - with a floor of 50% of the current conforming limit, to match the 150% maximum. Under current circumstances, the minimum would be \$208,500, close to the national median price, so low-cost areas would be protected. This would make symmetrical the asymmetrical provision of HR 1427. It would emphasize that Fannie and Freddie are supposed to be operating more or less from the middle of the market down - everywhere. The ‘middle of the market’ would be defined as houses costing about 125% or less of the area median. This would be a straightforward way to redefine the conforming loan limit so that it matched market conditions in all areas.

- “Though unworkable 70 years ago when the limit was invented for savings and loans, this system would be easy with today's information technology. As the Senate takes up GSE reform once again, it should consider how to counterbalance the effects of making the GSEs' ties to the government even stronger than before.” (*American Banker*, Alex J. Pollock, 05/25/07)

The biggest risk in the U.S. financial system: Fannie Mae and Freddie Mac

- In *Foreign Affairs*, Richard Christopher Whalen wrote, “A financial system is most vulnerable when it is dominated by a small number of large institutions. If one megabank blows up, there will be mountains of unpaid debt to other banks; this could cause the other banks to fail, setting off a chain reaction. In the U.S. financial system, two institutions stand out for the risk associated with their size: Fannie Mae and Freddie Mac, the two semiofficial mortgage financiers. The combined bond portfolio of these players is larger than the outstanding stock of Treasury bills and much larger than any hedge fund.” [Whalen is global risk editor of the magazine, *The International Economy* and co-founder of Institutional Risk Analytics.] (*Foreign Affairs*, Richard Christopher Whalen, May 2007-June 2007)

Fannie Mae and Freddie Mac

Subprime mortgage market news:

Federal Reserve Chairman Bernanke says subprime mortgage crisis will not hurt the national economy

Senator Reed introduces a foreclosure prevention bill

Ohio's Attorney General plans subprime lawsuits against parties "all the way up the line"

Freddie and Fannie likely to serve the "cream of the [subprime] market"

Accounting rules emerge as a complicating factor in the modification of subprime mortgages

Six bank trade groups issue joint statement on subprime mortgage lending

The mortgage bankers' black eye

Should Uncle Sam bail out subprime borrowers?

Federal Reserve Chairman Bernanke says subprime mortgage crisis will not hurt the national economy

- During a May 17 speech at the Federal Reserve of Chicago's 43rd Annual Conference on Bank Structure and Competition, Federal Reserve Chairman Ben Bernanke said that the current crisis in the subprime mortgage sector will have minimal spillover effect on the housing market and the broader economy. He acknowledged public concerns about increasing delinquency and foreclosure rates in the subprime sector and added that he fully expects to see higher rates of delinquencies and foreclosure in 2007 and 2008, as interest rates reset. Curbs on subprime lending will also cause some degree of restraint on home purchases and residential investments for several quarters, he added. "We believe the effect of the troubles in the subprime sector on the broader housing market will likely be limited and we do not expect significant spillovers from the subprime market to the rest of the economy or the financial system," said Bernanke. "The vast majority of mortgages, including even subprime mortgages, continue to perform well. Past gains in house prices have left most homeowners with significant amounts of home equity, and growth in jobs and incomes should help keep the financial obligations of most households manageable."
- Bernanke took issue with critics in Congress, who argue that the Federal Reserve failed to aggressively regulate the mortgage market. He said that the Fed will continue to work to prevent fraud and abusive lending practices, but would not

intervene in a manner which hampers responsible subprime borrowing. With respect to the Fed's responsibilities under the Home Ownership Equity Protection Act (HOEPA), Bernanke urged caution in using that power. "In my judgment, effective disclosures should be the first line of defense against improper lending," he said. "If consumers are well informed, they are in a much better position to make decisions in their own best interest." Bernanke conceded that additional disclosures may not be enough and suggested that principled supervisory guidance might work best. "Rules are useful if they can be drawn sharply, with bright lines, and address practices that are never, or almost never legitimate," he said. "...[S]upervisory guidance that establishes principles or guidance is, when applicable, the better approach." He added, "In deciding what actions to take, regulators must walk a fine line. We must do what we can to prevent abuses or bad practices, but at the same time we do not want to curtail responsible subprime lending or close off refinancing options that would be beneficial to borrowers."

- On June 14, the Federal Reserve will hold a public hearing to solicit views on the use its HOEPA authority to "curb abuses while preserving access to credit," said Bernanke. "We at the Federal Reserve will do all that we can to prevent fraud and abusive lending and to ensure that lenders employ sound underwriting practices and make effective disclosures to consumers," he said. "At the same time, we must be careful not to inadvertently suppress responsible lending or eliminate refinancing opportunities for subprime borrowers."
- Speaking at the same Chicago Fed conference, Shelia Bair, chairman of the FDIC, said, "We don't see any systemic risk from [the subprime mortgage sector]... This is obviously a crisis for individual families, neighborhoods and some communities." Bair also said that federal regulators will likely finalize guidance on subprime mortgage lending in June or July. [According to a source, the debate over how regulators should treat refinancings and stated-income loans has delayed the release of the regulators' final guidelines.] In a May 17th letter to the federal banking regulators, Senate Banking Committee chairman Christopher Dodd (D-CT) and other members of the panel said, "We urge you to finalize the Subprime Guidance as quickly as possible, retaining all the protections proposed. This is extremely important both to ensure the safety and soundness of the lender, and the financial well-being of the borrower."
- In response to Bernanke's comments, Senate Banking Committee chairman Chris Dodd (D-CT) issued a press release, decrying the Fed's failure to rein in abusive lending practices and took issue with Bernanke's suggestions that the Fed merely has the "authority" to issue rules under HOEPA. The law "requires" the Fed to write rules protecting homeowners from unfair and deceptive lending practices, argued Dodd. The current crisis in the subprime mortgage market is due, in part, to the Federal Reserve's failure to honor its duty, Dodd concluded. "The result has been a record increase in foreclosures across the country, with more increases predicted," he added. "It is past time for action. I welcome the Board's decision to hold a hearing, and urge the Board to move expeditiously to promulgate a rule. As Mr. Bernanke

says, such a rule would create a federal standard for all home loans. This is an outcome to be welcomed, not avoided.” Senator Charles E. Schumer (D-NY) argued that Congress could not afford to wait as defaults and foreclosures keep rising. “The bottom line is that we have a responsibility to act soon, not just wait and see what the market decides while families lose their homes,” said Schumer. (*American Banker*, Steven Sloan, 05/18/07; *New York Times*, Jeremy W. Peters, 05/18/07; *Dow Jones Newswires*, Jesse Thomas, 05/17/07; *Bureau of National Affairs*, Michael Bologna, 05/18/07; *American Banker*, Cheyenne Hopkins, 05/31/07; *American Banker*, Joe Adler, 05/16/07; *Dow Jones Newswires*, Damian Paletta, 05/18/07; *Dow Jones Newswires*, Damian Paletta, 05/31/07)

- On May 29, the Federal Reserve Board announced the topics to be covered at its June 14th hearing on ways the agency can use rulemaking authority to prohibit abusive mortgage lending practices. The topics to be discussed include (1) the appropriateness of prepayment penalties; (2) whether subprime lenders should be required to establish escrow accounts for taxes and insurance; (3) the role of stated income or “low doc” mortgages; and (4) the basing of underwriting decisions on the borrower’s ability to pay. The hearing will also cover questions about the role of state regulators in banning predatory lending practices and whether the Fed should adopt similar policies. Public comments on the subject will be due August 15.
- In a speech at the George Washington University School of Business, Federal Reserve Board Governor Randall Kroszner said that, while stronger rules may be warranted to protect consumers, such rules must not curb innovation or impose costs that outweigh their benefit. “In fulfilling its responsibility to protect consumers, the Federal Reserve will do all that it can to prevent fraudulent and abusive mortgage lending practices,” said Kroszner. “Any new rules should be drawn clearly to avoid creating legal or regulatory uncertainty that could have the unintended consequence of restricting consumers’ access to responsible subprime credit,” he said. (*Bureau of National Affairs*, 05/30/07; *Reuters*, 05/23/07)

Senator Reed introduces foreclosure prevention bill

- On May 14th, Senator Jack Reed (D-RI) introduced The Homeownership Protection and Enhancement Act of 2007 that would appropriate \$615 million to expand homeownership counseling programs to homeowners in an effort to prevent mortgage foreclosures. Specifically, the bill provides an additional \$300 million in funding to HUD-approved agencies which provide foreclosure prevention counseling; \$50 million to state homeownership protection centers which counsel borrowers on payment options once they fall behind on their payments; and \$260 million in grants to the states operating these centers to be used for subsidized loans for families in distress “with reasonable prospects for resuming mortgage payments within a year,” among other things. The bill would prohibit lenders from foreclosing without first conducting reasonable loss-mitigation efforts and would require lenders and originators to submit loan origination and performance data to a federal database

annually. This bill marks the second legislative attempt by Democrats to try to minimize rising foreclosures rates among subprime mortgages.

- On May 16, HUD Secretary Alphonso Jackson criticized the Democrats' legislative proposals to minimize foreclosures of subprime mortgages. "I know there are some who are calling for a subprime rescue... I strongly disagree... that a bailout is the answer," said Jackson at a Washington conference. Senator Chuck Schumer, author of a similar bill proposing \$300 million for community groups that provide foreclosure counseling, fired back within hours. "Funding counselors who can help homeowners avoid foreclosure by refinancing and restructuring and holding mortgage brokers accountable for fraudulent and deceptive practices is not a bailout," said Schumer in a press release. (*Dow Jones Newswires*, Damian Paletta, 05/14/07; *American Banker*, Stacy Kaper, 05/17/07)

Ohio's Attorney General plans subprime lawsuits against parties "all the way up the line"

- Ohio Attorney General Marc Dann said he plans to sue mortgage lenders and brokers, rating agencies, and Wall Street investments banks on behalf of borrowers and the Ohio Public Employees retirement system, which invested in mortgage-backed bonds secured by subprime mortgages. "Ohio consumers and bondholders were all ripped off on the same deal," said Dann. "We're looking at this issue all the way up the line, from bond rating agencies to mortgage brokers to investment banks. There wasn't just one actor in this. There were decisions being made, and bonds marketed to bondholders who were left holding the bag." He said he expects to file lawsuits in the next few weeks [early June] that allege violations of Ohio's Consumer Sales Practices Act, which prohibits "unfair or deceptive practices" in consumer sales. Legislation that went into effect on January 1st, expanded the Act to apply to mortgage brokers and nonbank lenders. "Nobody is paying any consequences for this [subprime mortgage crisis]," said Dann. "Middle-class Ohioans didn't think Wall Street would put them in a situation where they couldn't repay their mortgages." He added that his office is focused on two types of mortgages—those which involved fraud and those in which Ohioan homeowners were put into loans "that were impossible to repay." (*American Banker*, Kate Berry, 05/15/07)
- In response to Dann's threats to sue parties "all the way up the line" (including rating agencies), the major rating agencies said that the opinions they issue on the creditworthiness of subprime mortgage borrowers have nothing to do with investors in the related MBS losing money. "Our role is to evaluate the credit risk associated with the mortgage loans and securities backed by those loans, but our ratings do not comment on the suitability of an investment for investors," said Standard & Poor's spokesman Chris Atkins. Moreover, the ratings aren't recommendations to buy, hold or sell securities, he added. Fran Laserson, a spokeswoman for Moody's Investors Service, said her agency has a "very narrow, discrete and specific" role, in which it provides opinions on the creditworthiness of securities but doesn't make recommendations on them as investments. Fitch Ratings spokesman James Jockle

said, "Fitch believes that it appropriately expressed its opinion on the subprime mortgage transactions it rated."

- Kurt Pfothauer, the Mortgage Bankers Association's senior vice president for government affairs and public policy, said, "No one that I know of who's had a AA or a AAA strip of any of these [Ohio subprime] mortgage pools has taken a loss on those yet. So it's hard to imagine who's gotten bilked." He added, "We think the delinquency from foreclosure rates in Ohio is being driven from economic factors, not by loan products." (*American Banker*, Kate Berry, 05/15/07; *Dow Jones Newswires*, Stan Rosenberg, 05/18/07)

Freddie and Fannie likely to serve the "cream of the [subprime] market"

- At a speech before the Mortgage Bankers Association, OFHEO director James B. Lockhart, III said that Fannie Mae's and Freddie Mac's new programs for subprime borrowers will likely serve "the cream of the market" and his agency is "piggybacking" the federal bank regulators' subprime mortgage guidance to determine how the guidance should apply to the GSEs' bond portfolio holdings. Lockhart said approximately 30% of the two million subprime hybrid loans in private-label securities involve borrowers with debt-to-income ratios below 45% "that's going to be [the GSEs'] prime target... serving the almost-not-subprime market." He added, "They are going to be looking at the upper parts of the subprime market and ...even trying to put [subprime borrowers] in products that are not subprime going forward." (*American Banker*, Harry Terris, 05/23/07)
- A safer way to find "opportunity in the housing bust" is by investing in Fannie Mae and Freddie Mac, says John C. Thompson, co-manager of Thompson Plumb Growth Fund. "We think the market will continue to go their way because they can still fund loans and the subprime market has disappeared," he added. "[The companies' accounting] issues are going away and, within the next 12 months, it should be business as usual for both of them. They should be able to grow their portfolios substantially, given the market dynamics we see." (*Milwaukee Journal Sentinel*, Kathleen Gallagher, 05/27/07)

Accounting rules emerge as a complicating factor in the modification of subprime mortgages

- Accounting issues related to FASB 140, which effectively bar loan servicers from taking actions not specifically sanctioned in the securitization documents without a majority vote from the bondholders, has emerged as a complicating factor for mortgage servicers, who are attempting to work with distressed subprime borrowers. According to trade groups, lenders, and accountants, the rules are at best ambiguous about what preventive steps a loan servicer may take with securitized loan before the loan becomes delinquent. Several experts warn that taking such steps runs the risk of disqualifying securitized loans from off-balance sheet treatment under FAS 140, which governs "qualifying special-purpose entities." Alison Utermohlen, the

Mortgage Bankers Association's senior director of accounting policy, said that lenders are concerned that if they modify loans that are not yet in default, they might end up "blowing Q status" which "[is] potentially a huge issue." Without further guidance from FASB, the lenders could lose their "Q status" and have to recognize "loans they don't own" on their balance sheet, which would create "adverse effects" for financial statement ratios and capital requirements, said Utermohlen.

- MBA and the American Bankers Association have submitted letter to FASB, asking for additional guidance on this issue. However, FASB is a year away from issuing any amendment to FAS 140, according to a source with the rulemaking body who asked not to be identified. This amendment will consider the creation of a new model for how to report the transfers of financial assets; developing the actual model could take even longer, said the source. "No one has actually questioned whether servicers have the ability to renegotiate loans, but if a negative answer comes down from FASB, then renegotiating loans in a securitization would effectively unwind the accounting treatment," said Charlie Gilman, an accounting policy adviser at the ABA. "Unwinding those securitizations would not be pretty." (*American Banker*, Kate Berry, 05/18/07)

Six bank trade groups issue joint statement on subprime mortgage lending

- On May 21st, The Financial Services Roundtable, the American Bankers Association, the Mortgage Bankers Association, the Consumer Bankers Association, and America's Community Bankers announced the adoption of a set of subprime lending principles. Specifically, the principles said that lenders should offer subprime loans only to borrowers who they "reasonably believe" will be able to repay the loans, and that disclosures should better explain the loan features. Additionally, "regulators, loan services, and investors should work together to make available to homeowners appropriate options to help them sustain homeownership," said the principles, which are similar to, but less specific than the set of guidelines that Senate Banking Committee chairman Chris Dodd persuaded several lenders to adopt in early May. The joint statement emphasized that the groups' member institutions are actively contacting delinquent borrowers to offer assistance in avoiding foreclosure. The Independent Community Bankers of America's president Camden Fine said his group plans to write a "separate but concurring" statement on this issue that better reflects its members' views. Fine also said that ICBA has not decided whether it supports a national standard for predatory lending. "It just depends on what the legislation would look like," he said. (*American Banker*, Stacy Kaper, 05/22/07; *Bureau of National Affairs*, Richard Cowden, 05/22/07; *American Banker*, Stacy Kaper, 05/23/07)
- America's Community Bankers the Consumer Bankers Association, the Financial Services Roundtable, and the Roundtable's Housing Policy Council also urged federal regulators to establish a uniform standard for banks and non-banks that originate mortgage loans for customers with "blemished credit." The groups said, "A

national uniform standard should provide fair and consistent application to both bank and non-bank mortgage lenders.” (*Marketwatch*, Robert Schroeder, 05/21/07)

The mortgage bankers’ black eye

- In a May 22nd speech at a National Press Club luncheon, John Robbins, chairman of the Mortgage Bankers Association, said “...I stand before you today mad as hell. I have to be angry. It would be too depressing to accept that a very few unethical people [mortgage brokers who originated subprime mortgages] can give my profession and me a black eye. But it's worse than that. It's just not our reputations that have been damaged—the very people we take pride in helping—all because of a very few unethical actors.”
- “And here's what their actions obscure: Millions of Americans building financial security today by owning their own homes, 2.8 million families achieved home ownership for the first time in just the last five years. ...What makes the current situation so frustrating is that those of us now tainted by those very unethical actions were the very ones out front. Our historical data led us to predict a loosening of underwriting standards and increase in ARMs. It occurs after every boom. And we clearly said this boom would be no different. For years we have been calling for legislation to create a tough national standard to protect consumers against predatory lending. We were doing so during years of record volumes, long before the increased share of subprime loans—years in which our industry helped keep this economy out of a recession.”
- “Today, when faced with heartbreaking stories of people losing their homes, there's a clamor for action. You know, it's an easy trap to fall into. Regulators can regulate, so let's have more regulation. Legislators can legislate, so let's have more laws. Problem solved. It was Maslow who said that when all you have is a hammer, every problem looks like a nail. But before we start hammering away, I propose the most intimately involved have the chance to make the necessary changes.”
- “...Let's not smash this subtle ingenious [mortgage finance] system as we fix problems in the subprime market. We have plenty of cleaning up to do. And that's the most important thing—help the people in trouble. Truth is, we're pretty good at cleaning up. We've had a lot of practice after what Katrina and Rita did to the Gulf Coast. We prevented widespread foreclosures for more than 18 months by providing forbearance for many homeowners.”
- “So let's begin by looking at what corrections have already occurred and what's left to be done, and that way we can be sure we take the right steps rather than just the expedient ones—that what we do is truly needed today, not something that was needed a year ago but won't do much good now. This requires an actual understanding of the magnitude of the problem. First, let me point out that fully 35 percent of the homeowners in this country have no mortgage. They own their homes free and clear--35 percent. Plenty of stability there. ...Among homeowners, 5.1

percent of them are subprime borrowers with adjustable rate mortgages—5.1 percent. We are seeing a foreclosure rate of 10.8 percent annualized among subprime ARMs. So what percentage of homeowners are we really talking about here? Ten percent of 5.1 percent of all homeowners. And of that half of 1 percent of the whole, fully half of those will find [a] solution that avoids a foreclosure sale. In other words, one quarter of 1 percent will ultimately face foreclosure. As we can clearly see, this is not a macroeconomic event. No seismic financial occurrence is about to overwhelm the U.S. economy.”

- “...I know this is cold comfort to the people who have been hurt. Their pain is real a mountain to climb each morning. They don't care what the statistics are. ...Those figures even at a half a percent still add up to a lot of people. The Center for Responsible Lending released a foreclosure forecast that ...2.2 million ...subprime borrowers who—and let's pay attention here—have lost or will lose their homes to foreclosure. That's been interpreted as new foreclosures—as something about to happen. They reached that 2.2 million figure by disingenuously totaling all the subprime foreclosures since 1998 of which there have been about 1.6 million, and then of recent subprime loans to add another 600,000 in the near term future. So their 2.2 million figure was cumulative over at least an 11 year period, only a small portion of which is a forecast. That's still a lot of people, but out of 75 million homeowners and 50 million mortgage holders, it's not an eyebrow raising number when looked at over that period of years. It's within what we as a society deem as an acceptable risk for the rewards and opportunities of homeownership. One more thing about the their forecast. It assumes that every loan that goes into foreclosure will be foreclosed upon. But 50 percent of foreclosures are worked out, and that's a percentage we need to keep very high. ...Knowing that the system is not in imminent danger, it's clear that our first steps are to help those in trouble. We mean homeowners living in their own homes. We're not for rescuing real estate speculators.”
- “Second, we must find a way to prevent future abuse without eliminating subprime loans. I want you all to remember that 3 million Americans used a subprime loan to purchase a house. It is an extremely important tool for providing home ownership opportunities in this country. ...Chairman Bernanke said, . . . ‘Regulators must walk a fine line. We must do what we can to prevent abuses or bad practices, but at the same time we do not want to curtail responsible subprime lending or close off refinancing options that would be beneficial to borrowers.’ Here's why that makes sense. More than 81 percent of all holders of subprime loans are making their payments on time. So for every dramatic and heartbreaking story, there are so many more equally dramatic and uplifting stories of people who have gained a home—and in many cases not just a home, but a legacy of financial stability to pass on to the next generation thanks to a subprime loan...”
- “...So what steps have already been taken by the market and by the players involved? Underwriting has tightened. While standards loosened in 2005 and 2006—they always do to some degree when volume declines—today the percentage of banks reporting tighter standards is the highest in 15 years. Investors are wary of too many

subprime loans in their portfolios. If lenders can't sell them on the secondary market, they won't originate them. So they're declining as a result of supply and demand. Many of those who most abuse the system are already out of business. Today over 40 companies have closed for being overly aggressive in their underwriting. And though while the market isn't always perfect, it does punish mistakes severely and is much faster to correct than either legislators or regulators.”

- “Now, many people whose loans are about to reset still have subprime credit. They need to get into some other loan. While they may be able to, many of [the] people in this category are not mere victims of unscrupulous lenders. They're smart people who took a calculated risk to get into a home, all along planning to refinance before the big jump in their ARM. In many states, these borrowers were also hit not just by the rise in interest rates, but by the dramatic run ups in property taxes and hazard insurance as well. We can't leave these people twisting in the wind. They were practicing financial planning and attempting to take advantage of the opportunities they saw in the future. They were betting on themselves. To keep their financing options open, we must avoid a credit crunch. Even so, tight credit is having an affect on home sales. The latest projections for this year revised to around a 4 percent drop compared to last year—remembering that last year was a near record year.”
- “Well, that's what the market has done. What have we and others been doing? And what more do we propose to do? Our first priority should be to help those who need help immediately. Searching for solutions, the mortgage industry has met with the GSEs, with FHA, with our largest servicers, consumer groups and civil rights leaders. We do so both separately and as a participant in Senator Dodd's housing summit last month. There, we helped draft the principles that all agreed to, including early contact of borrowers who may be in trouble and a commitment to find the best alternative for those borrowers. We continue to work toward FHA modernization. Proof of its importance was Commissioner Montgomery's announcement that FHA plans to [refinance] over 60,000 subprime loans in 2007.”
- “The industry has the capacity and the tools to prevent many foreclosures if given the chance. It's human nature for borrowers in trouble to avoid calling their servicer and announcing that they don't have enough money to make their payment. It's just not a call anyone wants to make; indeed, it's counterintuitive. Yet it's the smartest thing a borrower facing delinquency can do. Even 80 percent of those already in foreclosure benefit from lost mitigation techniques resulting in about half not losing their homes. I hope this fact is mentioned in any and all coverage of subprime loan delinquency. Nobody wins in a foreclosure. On average, our industry loses \$40,000 to \$50,000 per home when that happens. But the homeowner loses a lot more: their credit rating, their equity and their home.”
- “So working something out is truly best for everyone. For that reason, MBA, on behalf of the entire mortgage industry, has created a series of radio and television public service announcements. ...MBA has partnered with NeighborWorks America, a nonprofit organization created by Congress, to provide financial support technical

assistance, and training for community revitalization efforts. Specially, we will be able to promote their free counseling hotline, 888-995-HOPE, manned by the Homeownership Preservation Foundation... We'll also be establishing foreclosure intervention programs in cities with the highest foreclosure rates and helping to train and certify more foreclosure counselors all through our partnership with NeighborWorks America. And as part of the Mortgage Bankers Association's ongoing financial literacy effort, we have retooled and relaunched our consumer website, The Home Loan Learning Center, offering tools and information to help consumers decide which mortgages are best for them..."

- “Now, what about prevention? To prevent, we need to once again identify the problem: unethical people. They're responsible for this mess. The short term folks, people who get a commission when the deal happens. For them, it's the number of loans that count—good loan, bad loan, who cares? For them, it's all about their commission... They, not people with marginal credit, are the ones who need to be stopped. Frankly, it's too easy to hand a shingle out and call yourself an expert in mortgages. We need licensing of brokers. With a threshold that will weed out those unwilling to be responsible, to be held accountable. Some cross the line into pure fraud and for them, we have laws. But as long as there are scam artists willing to look someone in the eye and say, ‘I'm going to get you something for nothing,’ people will be hurt.”
- “So do we just throw up our hands? Or do we arm the people who can be vigilant, the people there will always be enough of? The consumers—arm them with the facts. Make them savvy before it's too late. Consumers are smart. Armed with good information, they make intelligent choices. ...That's why MBA launched Project Clarity in 2006, an initiative to simplify and demystify the mortgage process. Let's face it, all those documents that are for consumers, that we see their protection at closing, don't protect consumers at all. There are too many to read and they are too hard to understand. We're working on up front documents that clearly state the pros and cons of the variety of loans available today.”
- “Having the chance to ...talk about what our industry has done and is doing, actually has been pretty good therapy for me today. I'm focusing less on the bad actors who caused this and more on the millions of people we've helped and are still helping...And that's why, despite my temporary black eye, I'm proud to be a mortgage banker.” (*Federal News Service, 05/22/07*)

Should Uncle Sam bail out subprime borrowers?

- In a May 4th commentary, *Fox News*' Neil Cavuto said, “So New York Senator Chuck Schumer wants to help out homeowners who got in over their heads. Subbed and now primed for disaster. So Uncle Sam to the rescue. Senator Schumer might not call this a bailout, but it is. Because any time you put taxpayer money on the table to support folks who cannot support themselves — that's a bailout. Now some of those folks were duped, and signed deals they shouldn't have signed. But they did.

And it's not up to the government to un-do what they did. Now some have said, 'Yeah, Neil, but what happens to home values if we don't?'"

- “Turn it around. What happens to the poor guy who is struggling to pay his mortgage if we do? What reward does he get for trying to do the right thing? He pays his bills and gets nothing, his neighbor who does not gets everything? I just think it's very unfair to the 87 percent of subprime mortgage customers who ‘are’ paying their bills, to help subsidize the 13 percent who are not. It's wrong. And it's a slippery slope. What about the guy who can't pay his credit card debt? Bail him out? Or the guy late on his car payments? Bail him out?”
- “It's dangerous, my friends, when a government with good intentions puts good money, your money, after bad money. We live in a society where we're free to choose, and free to screw up too.” (*Fox News*, Neil Cavuto, 05/04/07)

Bush administration notes

- On May 16th, the Senate Banking Committee approved the appointment of David Nasan to be assistant secretary of the Treasury for financial institutions. (*Dow Jones Newswires*, Damian Paletta, 05/16/07)
- President George W. Bush plans to nominate Elizabeth A. Duke and Larry Allan Kane to serve on the Federal Reserve Board of Governors. Duke, 54, is the former chairman of the American Bankers Association and currently serves as chief operating officer of TowneBank, Portsmouth, VA. Kane, 46, is president of global financial services of Capital One Financial of McLean, VA. Bush also plans to nominate Fed Board member Randall S. Kroszner, 44, to a new term when his term expires in January. Kroszner, a former economics professor at the University of Chicago, has emerged as the central bank's point person on many banking issues, following the departure from the board of Susan S. Bies in March and Mark W. Olson in June 2006. (*Washington Post*, Nell Henderson, 05/16/07)

Fannie Mae and Freddie Mac expand their market share of MBS issuance

- According to a recent UBS report, the share of mortgage bonds issued by Fannie Mae and Freddie Mac stood at 49% of total bonds issued in March, up from 44% in 2006. (*Dow Jones Newswire*, Danielle Reed, 05/18/07)
- According to HUD, the Chinese investment in U.S. agency mortgage-backed securities totaled \$107 billion in June 2006, making it the biggest foreign holder of U.S. MBS. Japan ranks second behind China with \$85.3 billion invested in U.S. agency MBS, followed by Taiwan with \$24 billion. (*Dow Jones Newswires*, Damian Paletta, 05/24/07)

FICO formulas revamped

- Fair Isaac Corp, the developers of the FICO formula used by credit bureaus to determine credit scores, is revamping the calculations it uses to be more effective in determining the risk profile of people with thin credit histories. The new formulas will debut in September. Ron Totaro, vice president of Global Scoring Solutions at Fair Isaac, said, “We are always coming up with new versions. We started working on this before the current situation with subprime.” He added that the average borrower will detect little, if any, change in his or her credit score under the new formulation. (*Los Angeles Times*, David Colker, 05/17/07)

SEC eases Sarbanes-Oxley requirements and adopts new rules for credit rating agencies

- On May 23rd, the SEC approved new guidance to help companies comply with Section 404 [which addresses internal controls over financial reporting] of the Sarbanes-Oxley Act. By a vote of 5-0, the Commission voted to encourage companies to take a more risk-based approach, which allows managers to identify the highest risks to their books as opposed to forcing them to test a long list of controls. "Congress never intended that the 404 process should become inflexible, burdensome and wasteful," said SEC chairman Christopher Cox. “[The guidance] is intended to right-size the evaluation and assessment efforts of managements, and it’s intended to do that for companies of all sizes. Investors will benefit from reduced compliance costs. (*American Banker*, 05/24/07; *Reuters*, 05/23/07)
- Also at its May 23rd meeting, the SEC adopted new rules to implement provisions of the Credit Rating Agency Reform Act of 2006. In a vote of 5-0, the Commission adopted rules which (1) require a credit rating agency to apply to the SEC for registration as an NRSRO and, if approved, maintain an annual certification on Form NRSRO; (2) require NRSROs to make and retain certain business records for set periods of time; (3) require NRSROs to furnish the agency certain financial information; (4) require NRSROs to develop and maintain written policies and procedures governing the use of material nonpublic information obtained in connection with performance of credit rating services; (5) require the NRSRO to disclose and manage conflicts of interests that arise in the normal course of engaging in the issuance of credit ratings; and (6) prohibit NRSROs from engaging in certain unfair, coercive, or abusive practices. (*Bureau of National Affairs*, Rachel McTague, 05/24/07; *Reuters*, 05/23/07)

Fannie Mae

Fannie Mae names former FBI director, Louis Freeh, to serve as a director

- Fannie Mae's board of directors has elected Louis J. Freeh to serve as a director and serve on the Board's Compliance and Compensation committees. Freeh, former Director of the FBI from 1993 to 2001 and previously General Counsel, Corporate Secretary and Ethics Officer for MBNA Corporation, becomes the eighth new director elected to the company's Board since 2004. "Louie Freeh will be a terrific addition to our Board as the company moves forward," said the company's chairman Stephen B. Ashley. "Louie's impressive legal background and experience working in the financial services sector and on corporate boards will be important assets for the company and our shareholders." Freeh is currently the president of Freeh Group International, LLC, a practice of former federal judges and former senior FBI leaders who provide legal, governance, investigative, litigation, and risk management services, headquartered in Delaware with offices in Washington, D.C. and New York City. (*Fannie Mae Press Release, 05/23/07*)

Fannie Mae's gross mortgage portfolio slips in April

- In April, Fannie Mae's gross mortgage portfolio fell \$2.2 billion to \$710.6 billion from \$712.8 billion in March. The company's net retained commitments fell to \$11.7 billion in April, from \$14.1 billion in March. Fannie Mae's book of business grew at a compound annualized rate of 8.1% in April, driven by the company's growth in its MBS and other guarantees which rose at an annualized 9.6%. Fannie's duration gap, a measure of the portfolio's sensitivity to interest rates, averaged zero months in April compared to -1 month in March. (*Dow Jones Newswires, Anusha Shrivastava, 05/23/07; Fannie Mae Monthly Summary, 05/23/05*)

Shareholders' derivative lawsuit against Fannie Mae is dismissed

- District Judge Richard J. Leon dismissed a shareholders' derivative lawsuit against Fannie Mae, in which the plaintiffs had hoped to force the company to make changes in its governing policies and recover bonuses and severance packages from members of its former management team. Leon threw out the lawsuit because the shareholders did not first petition Fannie Mae to, as a company, sue its board of directors and executives. "We are pleased that the Court found that the Board of Directors acted responsibly, and was fully able to act independently to protect and make decisions on behalf of the company and was not compromised by any self interest," said Fannie Mae chairman Stephen B. Ashley. The judge's ruling does not affect a pending class action lawsuit against Fannie Mae executives for security violations or OFHEO's administrative proceeding which is pending against members of Fannie Mae's former management team. (*Associated Press, Matt Apuzzo, 05/31/07; Fannie Mae Press*)

Washington, D.C. hopes to revoke Fannie Mae's tax exempt status

- Washington, D.C. mayor Adrian Fenty has called upon Congress to revoke Fannie Mae's tax exempt status, which would provide the District more than \$300 million in tax revenues. "The District wants to be able to tax Fannie Mae, but there are senators that have to be able to pull the plug and make it happen," said Fenty, who has asked the GSE for a payment in lieu of taxes. D.C. Delegate Eleanor Holmes Norton said she "would love to see" Fannie Mae pay local corporate income taxes, but doubts there is enough political will on Capital Hill to revoke the company's tax exempt status. "Every congressional district has Fannie Mae financed housing, and therefore, I do not believe there is much of a chance." (*WTOP Radio* [Washington, DC], 05/31/07)

Freddie Mac

Freddie Mac to be "extraordinarily careful" with growth

- Freddie Mac chairman and CEO Richard Syron said his company will be "extraordinarily careful not to chase growth" at the cost of accepting too much credit risk. When the time comes that OFHEO lifts the company's growth restrictions, Freddie Mac will grow carefully and not risk over-exposure to credit risk, said Syron at a UBS investor conference in New York City. "Lending money is an easy business - it's getting it back that is hard," he added. Syron told the attendees that recent distress in the subprime mortgage market has given Fannie Mae and Freddie Mac an opportunity to demonstrate why their business models are important and beneficial for the housing market. "I think in a broad sense it very much demonstrates the need for the GSEs. It gives us a chance to strut our stuff and show what we're doing," said Syron. "You went back three or four years ago and everyone was saying we should privatize - essentially go away, right?," he added. "Now the debate is on much more constrained terms. What should your capital be? What should your relative rate of growth be? We would prefer that there was no debate. OK? But it is about things that are much less onerous than they were a few years ago."
- Anthony S. Pizsel, Freddie's CFO, said that the company plans to file its first quarter financial statement for 2007 in June. When the company begins releasing timely financial statements later this year, Pizsel said Freddie Mac will begin pushing OFHEO to free up its excess capital. "I don't want to be presumptuous about how the regulator is going to come down on all of this but we are extremely aware that this is

your money," said Syron. The company's current capital level is "too high " he added. "One of the investment theses for this company is that [we become] properly capitalized. We intend to be pretty aggressive on that at the proper time." (*Dow Jones Newswires*, Damian Paletta, 05/14/07; *Reuters*, Patrick Rucker, 05/14/07)

Freddie Mac's retained mortgage portfolio down 8.8% (annualized) in April

- In April, Freddie Mac's retained mortgage portfolio declined by \$5.2 billion to \$709.2 billion for an annualized decline of 8.8%. Year-to-date, the company's mortgage holdings have grown 2.2% (annualized). Adjusted for GAAP, Freddie Mac's mortgage holdings totaled approximately \$708.1 billion on April 30th. In April, Freddie Mac bought \$13.8 billion in mortgage bonds compared to \$21.4 billion in March, while it sold \$5.3 billion in April versus sales of \$4.4 billion in March. The company's mortgage bonds that matured or were paid off totaled \$13.7 billion, compared to \$4.4 billion in March. Freddie Mac's duration gap averaged zero months in April, unchanged from March. (*Dow Jones Newswires*, Cynthia Koons, 05/23/07)

Freddie Mac's annual stockholders meeting will be webcast on June 8th

- Freddie Mac will hold its next annual shareholders meeting on June 8, 2007, beginning at 9:00 a.m. The meeting can be heard live, in a listen-only mode, via webcast at www.FreddieMac.com/investors, or in listen-only mode via telephone. Recordings of the meeting will be available on Freddie Mac's website from mid-day June 8 until midnight on June 22. (*Freddie Mac Press Release*, 06/01/07)

In memoriam: Preston Martin

- In the June 2 online edition of *The Wall Street Journal*, Stephen Miller wrote, "Preston Martin fell short of his ambition to be Federal Reserve Board chairman, but his outspoken views helped shape the nation's financial policy and create the now-booming secondary market for home mortgages. As President Ronald Reagan's first appointment to the Fed and its vice chairman from 1982 to 1986, he led a challenge to then-Chairman Paul Volcker's tight-money policy—intended to prevent a return to the inflationary late '70s but which often ran counter to the Reagan administration's efforts to spur economic growth. Those clashes contributed to Mr. Martin's resignation as vice chairman -- ushering in the Alan Greenspan era as Fed chairman when Mr. Volcker decided not to seek another term as chairman in 1987. ... After leaving the Fed, Mr. Martin spent a few years rescuing failing S&Ls in partnership with Mr. [William] Simon. He then switched focus to fostering affordable urban housing, helping found two nonprofits, Neighborhood Housing Services of America and The Social Compact."

- “Earlier, as then-California Governor Reagan's savings-and-loan regulator, he was an early advocate of adjustable-rate mortgages. That job led to his later appointment as chairman of the Federal Home Loan Bank Board, where Mr. Martin helped spearhead the creation of Freddie Mac, which became one of the largest providers of funding for home mortgages.”
- On May 30, Mr. Martin passed away in San Francisco at the age of 83. (*The Wall Street Journal*, Stephen Miller and James R. Hagerty, 06/02/07)

Freddie Mac streamlines its early rate lock program

- Freddie Mac has made adjustments to its early rate lock program, which will speed up the deal time cycle and reduce the amount of money a developer has to put up in advance. The early rate lock program, which accounts for about 60% of the loans purchased by the company, helps eliminate interest-rate and credit-risk spreads by locking in an interest rate early in the mortgage-approval process. To make this program more competitive, Freddie Mac has introduced a standardized electronic preliminary loan submission template to begin pro-forma underwriting and preparation of the investment brief, which speeds up the company’s response time and allows the lenders to get quotes faster. Freddie Mac also has reduced the good faith deposit from 3% to 2% on “immediate delivery deals,” which are defined as deals allowing six months or less between the time the rate lock is issued and Freddie Mac purchases the loan. Freddie also has shortened the early rate lock application form, used after the quote is submitted to the lender, to reduce the amount of time spent processing the application. These changes are designed to increase Freddie’s competitiveness in a market of increasingly heated competition. “With the new CDO products on the market and a strong CMBS market, the agencies are having to adapt, and the more fine-tuning they do, the better it becomes for the borrower,” said Phil Melton, director responsible for affordable housing permanent debt transactions at Collateral Real Estate Capital. (*Affordable Housing Finance*, Jerry Ascierio, June 2007)

Romance, jealousy, and a mortgage?

- According to a May 21st Freddie Mac press release, “Nuestro Barrio (Our Neighborhood), a Spanish-language TV mini-series about Hispanic life in the United States will be shown in 10 media markets beginning June 1, on the new PBS-created V-me (Veh-Meh) Spanish language network. Nuestro Barrio is at the forefront of a new trend of television programming called ‘edutainment,’ a combination of education and entertainment to produce programming that is both informative and engaging. The 13-episode series, where hot storylines are combined with meaningful messages, subtly educates viewers on important financial issues including money management, credit, homeownership, predatory lending and foreclosure prevention,

which are played out against the traditional novella (soap opera) themes of romance, jealousy, greed and conflict. Freddie Mac ...funded the production of Nuestro Barrio..."

- ““The U.S. housing market is changing, challenging the mortgage industry to develop new and creative ways to reach potential homebuyers,’ said Craig Nickerson, vice president of Freddie Mac. ‘Many Hispanic families do not pursue homeownership due to misinformation, lack of trust of financial institutions and language barriers. Educational telenovelas are a unique way to reach the growing Hispanic marketplace with accurate information and to help close the homeownership gap.’” (PR Newswire, 05/21/07)

Federal Home Loan Banks

New mortgage program at the FHLB-Atlanta may expand to five other FHLBs within 30 days

- The Global Alliance Mortgage Program (GAMP), a new mortgage program being offered to the members of the FHLB-Atlanta, is expected to generate at least \$5 billion in mortgage purchases in the next 12 months and may expand to five other FHLBs within the next month. Eric Hillenbrand, the managing partner and CEO of Hillenbrand Partners which is offering GAMP to the FHLBs, said that he is holding discussions with the other Banks and hopes to offer the program as widely as possible. “The fundamental premise here is that we have 8,200 members that are part of the Home Loan Bank System,” said Hillenbrand. “The community banks have great relationships with their customers. We do not want to get in the middle of that. ... For the community banks, all we want to do is provide liquidity.”
- While the program effectively would cast the FHLBs only as intermediaries between its members with limited securitization capabilities in their partnership with Hillenbrand, many in the industry offer only qualified support and express concerns about the new program’s risk profile and its economic value to the FHLBs. One industry source told *The American Banker*, “The Home Loan bank members who like [the FHLBs’ other programs] will certainly look at this, but they might not see this as being useful to them.” While neither the FHLB-Atlanta nor Hillenbrand would discuss the fee structure of the program, Hillenbrand noted, “We would not have thought about engaging in this program unless we thought we would have highly competitive pricing.” The FHLB-Atlanta has assured its members that the Bank will continue to support the FHLBs’ mortgage programs. William Ott, the Atlanta bank's interim CEO, said, “From my point of view, we're still a member-driven organization, so our goal is to provide members with as much choice as possible.” Observers believe that the FHLB-Atlanta’s approach will placate its members who have relied

upon the FHLBs' mortgage programs and may be reluctant to change. "It will take quite some time to develop a new product that all the banks are comfortable with," said Brian Harris, an analyst with Moody's Investors. "For the foreseeable future, I would expect ... [the other programs] to be operational."

- By participating in GAMP rather than the other FHLBs' loan programs, the FHLB-Atlanta's interest rate risk would be eliminated in the new program, but operational risk could remain, said Harris. "I think it's primarily tied to how the Atlanta bank manages its people and systems and controls," he added. "One of the issues that over time became apparent on MPP and MPF was the need for risk models and risk expertise within the [FHLBs]. Looking back on those programs, that was certainly one of the hidden costs." Ott objected to Harris' concerns about the FHLB-Atlanta's operational risks. "This bank has a very, very strong operational process with the MPP and MPF program and is known to have a strong operational risk profile in this particular area," said Ott. "This product runs right off the same platform and backbone. It will not have any additional risk."
- Observers believe that the FHLBs' new mortgage program could ultimately end the Federal Housing Finance Board's debate over raising the Banks' retained earnings. Since mortgages would never touch the FHLBs' books under GAMP, further discussion over retained earnings could be moot. "If this program were to really take off, it would significantly change the discussion," said Joe Pigg, senior counsel at the American Bankers Association. "If there's less risk involved, then you don't need to be talking about increasing retained earnings." (*American Banker*, Steven Sloan, 05/23/07)

FHLBs announce new directors

- The FHLB-Indianapolis announced that Michael E. Petrie was elected to the board of directors to fill the remainder of a three-year term that commenced on January 1, 2006. The seat became vacant with due to the death of director Ronald G. Seals on March 31, 2007. Petrie serves as chairman and CEO of Greensfork Township State Bank, Spartanburg, IN. From 2004-2005, Petrie served as chairman of the Mortgage Bankers Association. (*FHLB-Indianapolis Press Release*, 05/14/07)
- The Federal Housing Finance Board has appointed six directors to the FHLB-Des Moines board. The Finance Board appointed Johnny A. Danos to fill a three-year term to the board that began on January 1, 2006; Lorna P. Gleason, John Francis Kennedy, Sr., and Paula R. Meyer to a three-year term that began on January 1, 2006; and Labh S. Hira, PhD and John H. Robinson to a three-year term that began on January 1, 2007. Danos is president of the Greater Des Moines Community Foundation and a retired partner of KPMG with more than 30 years of public accounting experience serving commercial retail, insurance, banks and financial institutions in Des Moines, IA. Gleason is senior managing director of GMAC Health Capital, a leading lender in the health care industry in Minneapolis, MN. Previously, she was the general counsel of Residential Funding Corporation, which

was later renamed GMAC ResCap. Kennedy is vice president and CFO for the St. Louis Equity Fund, Inc, St. Louis, MO, which invests in affordable housing developments financed through corporate investments and in cooperation with local, state and federal governments. Meyer retired as president of RiverSource Funds, formerly American Express Funds, in Bloomington, MN. Previously, she served as president of Piper Capital Management. Hira is dean of the College of Business at Iowa State University, Ames IA. Robinson is chairman of Hamilton Ventures, LLC, a consulting and investment company in Kansas City, MO. Previously, he served as chairman of EPCglobal, Ltd. in Sheffield, England and executive director of Amey Plc in London, England. (*FHLB-Des Moines Press Release, 05/16/07*)

- The Federal Housing Finance Board has appointed Patrick A. Bond and Brian A. Hudson to serve on the board of directors for the FHLB-Pittsburgh for the remainder of three year terms that expire on December 31, 2008. Bond is a founding general partner of Mountaineer Capital, LP, a venture capital firm licensed as a Small Business Investment Company which provides investments in new and expanding businesses in West Virginia. Previously, Bond served as president and CEO of Atlantic Financial Federal of West Virginia. Hudson is executive director and CEO of the Pennsylvania Housing Finance Agency. (*FHLB-Pittsburgh Press Release, 05/17/07*)

FHLBs announce dividends

- The FHLB-Boston's board of directors has declared a second quarter dividend rate of 6.75% (annualized) for the second quarter, payable on June 4th. (*PR Newswire, 05/18/07*)
- The FHLB-Dallas has declared a first quarter dividend of 5.25% (annualized), payable on March 30. (*Banking Wire, 05/15/07*)

Countrywide announces major initiative to create more efficient capital structure and lower its cost of funds through the use (in part) of FHLB advances
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- Countrywide Financial has announced a major initiative to move its mortgage operations under its bank, which will “improve our financial leverage, enhance our liquidity and lower our funding costs,” according to the company's CEO Angelo Mozilo. In 2007, Countrywide plans to increase its asset-backed financing from 28% to range of 30% to 35%, deposits from 30% to a range of 35% to 40%, and FHLB advances from 15% to a range of 20% to 25%. (*American Banker, Harry Terris, 05/15/07*)

Ginnie Mae

Congress's "second chance" to save the day
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- In the May 26th issue of the *Washington Post*, Kenneth R. Harney wrote, "With more credit-stressed mortgage borrowers falling behind on their payments, will Congress step in and throw them a lifeline? Will legislators transform the most consumer-friendly home mortgage program for moderate income buyers into a serious alternative for refinances heading for default and foreclosure in high-cost communities? Those questions put the spotlight on major legislation now pending on Capitol Hill – the modernization of the Federal Housing Administration's mortgage insurance programs. The House Financial Services Committee passed an overhaul bill earlier this month, and the full House is expected to take it up in June. Then it's over to the Senate, where similar legislation crashed and burned late last year. But that couldn't happen again, right? This year is different: The subprime mortgage market is in tatters, and thousands of borrowers are facing personal financial crises triggered by '2/28' and '3/27' adjustable-rate loans originated in 2004 and 2005."
- "[Given the "safe harbor" that FHA loans could provide subprime borrowers,] you might assume that FHA reform would be a slam dunk. But almost nothing on Capitol Hill is quite that simple. There are always snags. Here are a few that could affect the FHA bill:"
 - "Even though FHA reform is a broadly bipartisan issue -- the White House favors passage, and the bill's co-authors are two of the most liberal Democrats in the House, Reps. Maxine Waters (Calif.) and Barney Frank (Mass.), chairman of the Financial Services Committee – some Republicans are not fans of deeper federal involvement in the mortgage market. They are predisposed to look for portions of the bill that they can attack or seek to remove, potentially stalling consideration during a tight legislative calendar."
 - "One of the provisions drawing fire is a proposal by Frank that would divert some of the additional revenue generated by an expanded FHA -- the agency has sent billions of dollars in profit during the past decade directly to the Treasury -- and spend it on counseling to help financially troubled or unsophisticated applicants before they become homeowners. Other profits would be diverted to help pay for technological improvements to the FHA program, and still others would be set aside for use in an 'affordable housing fund.' Some critics are worried that money that otherwise would go to the Treasury could end up subsidizing 'affordable' mortgages for high-risk borrowers who really shouldn't own homes -- a charge that Frank denies."
 - "Lurking in the background are proponents of private mortgage insurance, the FHA's competitors in backing loans to home buyers making minimal down payments. Although a spokesman for the Mortgage Insurance Companies of

America insists that group "has no position, we have nothing to say" about FHA reform legislation, lobbyists from some mortgage insurers played pivotal roles last year in sandbagging the FHA bill in the Senate, keeping it bottled up in committee and off the floor calendar."

- "There is no reason to expect them to back off this year -- after all, a revived and competitive FHA, equipped with authority to go head to head in the biggest and most profitable markets nationwide, could siphon away business."
- "Bottom line for reform: Slam dunk? No way. But the bill has a shot -- either in its current form or by having essential provisions transplanted into an appropriations bill that can sidestep the landmines in the Senate." [Harney is a *Washington Post* columnist, who writes about rules and regulations that affect homeowners, sellers and buyers.] (*Washington Post*, Kenneth R. Harney, 05/26/07)

Growth of reverse mortgages inevitable

- According to Jim Beavers, the acting director for the Office of Single Family Program Development at FHA, the number of FHA-backed reverse mortgages has doubled from 37,789 in FY2004 to 76,283 in FY2006. Year-to-date, the number of HECMs has soared to 58,861. Given the impending wave of baby boomers, new advancements in product development, and potential legislative initiations, an explosive growth in reverse mortgages are inevitable, say mortgage experts. (*Bureau of National Affairs*, 05/31/07)

Farm Credit System / Farmer Mac

House subcommittee adopts portions of FCS's HORIZON Project into the 2007 Farm Bill

- In the May issue of *Farm Credit Watch*, Bert Ely wrote, "Legislation enacting the HORIZONS Project began to move in Congress last week when a House Agriculture subcommittee voted to include portions of the FCS's HORIZONS wish-list in the 2007 Farm Bill. Although banker opposition led to a legislative trimming of what the FCS has been seeking through HORIZONS, what has been included in the Farm Bill, so far, still represents a significant expansion of the FCS's off-farm lending powers. Together, these provisions take the farm out of FCS by watering down farmer ownership or control of the FCS."
- "The bill's key provision would expand the FCS's lending powers to include businesses 'primarily engaged in processing, preparing for market, handling, purchasing, testing, grading, distributing, or marketing farm or aquatic products; or

primarily engaged in furnishing farm or aquatic business services, or farm or aquatic supplies including inputs such as feed or fertilizer, equipment, and other capital goods to farmers, ranchers, or producers or harvesters of aquatic products.’ That wording excludes few, if any, business activities. Worse, the bill fails to define the term ‘primarily engaged.’ Instead, the FCS regulator, the Farm Credit Administration (FCA), must define that term, almost certainly in a manner highly beneficial to the FCS.”

- “Legislative wording tacked onto the Farm Bill would permit expanded FCS lending ‘only to the extent that the activities are related to renewable energy.’ However, as with ‘primarily engaged,’ the FCA would determine when FCS-financed activities ‘are related to renewable energy.’ Given the convoluted wording of this legislation and the FCA’s strong bias in favor of the FCS, this supposed limitation on broader FCS lending is anything but.”
- “Housing is the other area that would get increased FCS lending authority, with the bill boosting to 6,000, from the present 2,500, the population of towns where the FCS could make housing loans. As with other proposed expansions in its lending powers, the FCS has not demonstrated that there is an insufficient supply of housing finance in towns with populations between 2,500 and 6,000. While this boost is not the increase to a 50,000 population limit the FCS had been seeking, there is no justification for any increase whatsoever.”
- “Two other provisions in the bill, as reported by the subcommittee, would dramatically move the FCS away from its congressional charter as a farmer-owned and controlled lending cooperative. First, the bill would eliminate the already minimal borrower stock-purchase requirement (the lesser of \$1,000 or 2% of the amount borrowed) by giving each FCS institution the authority to set a stock-purchase requirement as low as it wanted, perhaps to just one dollar. This could open the door to FCS financing of point-of-sale purchases. Many FCS borrowers would effectively have no ownership stake in their lender -- that’s hardly a lending cooperative?”
- “Second, CoBank, the exclusive FCS lender to cooperatives, would be empowered to issue voting stock to borrowers who are not cooperatives. Today, a stockholder-owned company can borrow from CoBank if its operations ‘are functionally similar to the activities’ of entities eligible to borrow from CoBank. That corporate borrower could then become a voting CoBank shareholder. Finally, a surprising, last-minute addition to the Farm Bill could negatively impact the FCS Insurance Corporation (FCSIC), which Congress created twenty years ago to protect FCS debt from default. Since these provisions could weaken the FCSIC, the Ag Committees should hold hearings to fully explore the implications of this proposed piece of the Farm Bill.”
- “Ken Auer, who heads the Farm Credit Council ...stated in the *American Banker* last week that ‘commercial banks basically don’t like the idea that they have a farmer-owned competitor out there who has access to GSE funding.’ However, Auer

conveniently omitted the fact that ...HORIZONS seeks to undermine the FCS as a lending cooperative by watering down its present ownership requirements while ...keeping the massive taxpayer subsidies without which the FCS could not compete against its taxpaying competitors. Auer went on to state that 'the bankers ...have lied' about the FCS to members of Congress. In fact, bankers and the FCS's other non-subsidized competitors have been the truth-tellers."

- "Although HORIZONS has been trimmed back somewhat, it has just started to move through the legislative process. Next month or in July, the full House Agriculture Committee will piece together a complete Farm Bill, which will provide another opportunity to knock out the HORIZONS provisions which have survived so far. Importantly, House Financial Services Committee Chairman Barney Frank and Spencer Bachus, the top Republican on that committee, sent a second letter to the Ag Committee leadership expressing grave concern about HORIZONS. If the Ag Committee keeps the HORIZONS provisions in the Farm Bill, Frank and Bachus may ask that their committee review those provisions. Also, the Senate Ag Committee has yet to release its version of the Farm Bill. Hopefully, it will ignore what the FCS is seeking." (*Bert Ely's Farm Credit Watch*, Bert Ely, May 2007)
- Banking lobbyists said they would try to stop any expansion when the farm bill moves to the full agriculture committee in June. "This was not a compromise to which we were a party," said Floyd Stoner, American Bankers Association's lead lobbyist. "We are still concerned about any increase [in the FCS's lending authority]." Ike Jones, a lobbyist with the Independent Community Bankers of America, said that if such a provision were included in the final farm bill, it would be difficult for FCA to ensure that business lending was tied to renewable energy. "It's unenforceable," said Jones. "If I lend money to a trucking company and say, 'You can only use this truck to haul corn to an ethanol plant, but you can't use the truck for any other purpose' ... how is that ever enforced?" Mark Scanlan, the director of the ICBA's office of agriculture and rural policy, noted that all it would take to open the FCS's business-lending powers is one amendment striking the renewable-energy qualifier. "What if it goes to full committee and somebody moves to cross out that little tweak and then it's totally everything they asked for?" he asked.
- Kenneth Auer, the president of Farm Credit Council, said that more than 500 organizations, including several farmers' groups, support the proposed additional lending power because increased competition would benefit farmers. "It's not just an issue of credit availability," argued Auer. "It's what are the rates and terms that people have to pay." (*American Banker*, Stacy Kaper, 05/24/07)

FCS makes over \$9 billion available to beginning farmers in 2006

- According to a newly published report by the FCA, the Farm Credit System made more than 46,000 loans totaling \$5.5 billion to young farmers [representing 17% of all new loans made by FCS] and 57,000 new loans totaling \$9.3 billion to beginning

farmers in 2006 [representing 21.2% of FCS's new loans]. (*Western Farm Press Online*, 05/23/07)

Postal Service

APWU president Burrus warns of the danger
of having Congress determining postal employment conditions

- American Postal Workers Union president William Burrus told his members, "The long-standing APWU position is that mandatory subjects of collective bargaining are best left to the parties for resolution, even when bargaining has not achieved the desired results. I believe the danger of Congress determining conditions of employment for postal employees far outweighs the possibility of short-term success in specific areas. The concept of petitioning Congress to declare that mail delivery can be performed only by career postal employees is much more complicated than it appears at first glance. Collective bargaining was never intended to guarantee specific results. Through our unions we are guaranteed the opportunity to continue to try." (*APWU Burrus Update #14-07*, William Burrus, 05/29/07)
- Meanwhile, the National Association of Letter Carriers president William H. Young praised the bill (S. 1457) introduced by Senator Tom Harkin (D-IA), which would protect city and rural letter carriers from having their work contracted out by the USPS to private carriers. Young said that Harkin's bill would bring to a halt the USPS's efforts to privatize the mail delivery service. "...[I]t is now critical that the other members of the Senate hear one loud voice from our members—by letter, email, personal office visit—to bring about a groundswell of support for S. 1457 that will ensure its swift consideration in the Senate and eventual enactment by the 110th Congress," said Young. Co-sponsors of S. 1457 include Senators Max Baucus (D-MT), Jeff Bingaman (D-NM), Robert Casey (D-PA), John Kerry (D-MA), Jon Tester (D-MT), Byron Dorgan (D-ND), Patrick Leahy (D-VT) and Patty Murray (D-WA). (*NALC Bulletin*, 05/24/07)
- Senators Jeff Bingaman (D-NM) and Pete Domenici (R-NM) expressed their unhappiness with the USPS's plans to use temporary employees to address its El Paso processing and distribution needs. In statements released to KFOX-TV, Domenici said, "Hiring temporary employees is not the impression or understanding that I got. No where in the agreement does it say anything about these employees being temporary. I will make an inquiry into this immediately." Bingaman, added, "I'm very unhappy to learn that the 15 new U.S. Postal Service employees hired to staff the El Paso mail processing facility will be temporary. Mail delivery problems in Las Cruces are in need of a permanent solution and not a quick fix. I will continue to

work with the U.S. Postal Service to ensure this problem is addressed.” (KFOX-TV, 05/24/07)

The future is “in the mail” says Postmaster General Jack Potter

- In a May 30 speech at the National Press Club, Postmaster General Jack Potter discussed his agency’s efforts to become “environmentally friendly,” including the USPS’s recycling efforts, support of alternative energy sources, and its annual investments in energy saving improvements. The Postal Service operates the nation’s largest alternative fuel fleet of more than 37,000 vehicles powered by electricity, compressed natural gas, propane, hydrogen fuel cells, ethanol E-85 and biodiesel, he said. In 2006, the agency increased its fleet’s average miles per gallon by more than six percent. In its 37,000 postal facilities, the Postal Service has invested more than \$150 million annually on energy saving improvements to upgrade existing systems. In addition, the agency purchases more than \$200 million of products with recycled content and it recycled millions of tons of wastepaper, cardboard, plastics, cans, and other materials, which generated \$9 million in revenue. (*Remarks of Postmaster General John E. Potter, 05/30/07*)

Coming to a business near you – vanity zip codes

- The *New York Post* reports that days after the Saks Fifth Avenue convinced the Postal Service to give it a vanity zip code [10022-SHOE] for its shoe department, the cash-strapped agency is exploring the use of vanity zip codes to generate additional income. If the USPS’s test of the Saks zip code is successful, the agency could later roll out a nationwide program, said a USPS spokeswoman. According to the *Post*, the possibilities for vanity zip codes are “endless” and might include St Patrick’s Cathedral’s 10021-PRAY, Trump’s Tower’s 10021-HAIR, Mayor Bloomberg’s private resident’s 10021-RICH, and the *Daily News*’ 10023-LOST. (*New York Post, Peter Lauria, 05/27/07*)

The hardest hit by postal rate increases: Alaska’s remotest villages

- On May 14, the USPS increased its postal rates approximately 13% for Alaska’s one-of-a-kind discount mail program for 139 of Alaska’s remotest villages, which ensures the regular delivery of basic supplies. *Before* the postal hike, a regular-sized box of cereal cost more than \$8 and a gallon of milk cost over \$7 a gallon in these remote areas. “The villages are already having a hard time. A lot of people live on food stamps, and I don’t think they get very far,” said 85-year-old Josephine Roberts, who resident in the Athabascan Indian village of Tanana. The Alaska delivery program costs the USPS nearly \$70 million each year to operate, said the agency’s network operations specialist Steve Deaton. “It’s a program that the Postal Service supports in

recognition of the unique circumstances of Alaska residents,” said Deaton. “We are committed to keeping it going in the state of Alaska.” (*Associated Press*, Jeannette J. Lee, 05/26/07)

NALC: “The Union that Delivers”

- According to the *San Francisco Chronicle*, "The former president of a postal workers union was indicted today by a federal grand jury in San Francisco on charges of embezzling more than \$170,000 and falsifying records to cover his tracks. [According to the indictment,] Graham Paul Vane, 59, of Pacifica stole money from the National Association of Letter Carriers, AFL-CIO, Branch 1280 from January 2002 to March 2006 and spent it on dining, travel, massages, jewelry, wine, pet expenses, personal utility bills, groceries and gas..." (*San Francisco Chronicle*, 05/25/07)

TVA

TVA successfully restarts the Unit 1 reactor at Browns Ferry

- On May 22, TVA restarted its Unit 1 reactor at the Browns Ferry Nuclear Plant, 22 years after it was shut down because of safety concerns. The restart capped the utility's five-year, \$1.8 billion renovation, which some say is roughly the price of a new plant. The 60-month restart effort saved time, compared to a roughly 12-year period needed to construct a new nuclear plant. According to James R. Curtis, a former member of the Nuclear Regulatory Commission and lawyer for Winston & Strawn, retooling an old plant is a simpler task than building a new plant from a regulatory point of view. Browns Ferry spokesman Craig Beasley said there were no reports of problems in the restart of Unit 1. "Right now they're looking at the pressure inside the reactor," said Beasley. "They will keep the power very low for several days, and then increase it to 35 percent." (*InTech*, 05/17/07; *Associated Press*, Jay Reaves, 05/22/07)
- In a May 15th statement, Senator Jeff Sessions said, "Today's announcement by the Nuclear Regulatory Commission is fantastic news for [TVA], its ratepayers, and for our nation's energy security. Nuclear power represents our best source of domestically produced emissions-free energy. It is a cost efficient way to produce electricity, and I believe our nation should transition to producing a larger share of our energy from nuclear generation. The commission's authorization for a restart of Unit One comes after an extensive safety inspection, and represents the closing stages of a monumental project that will provide safe, reliable, and affordable electricity to over 650,000 homes in the Valley." (*Congressional Press Release*, 05/15/07)

- On May 25, the Browns Ferry Unit shut-down following an accidental discharge of 600 gallons of non-radioactive electro-hydraulic control fluid. As a precautionary measure, two employees who came in contact with the fluid were treated and released at a local hospital. TVA has begun the restart process of the Unit, following maintenance to valve and a coolant pump. (*Decatur News*, Eric Fleischauer, 05/30/07)
- In a May 21st editorial, *The Tennessean* [Nashville, TN] cautioned, "...Just because the demand for energy is high and the filth factor of sources such as coal-fired power plants is repulsive, those developments alone do not make nuclear energy superior. The nation must be cautious before it ramps up on nuclear power. A new age in nuclear energy could be based as much on wishful thinking as on sound scientific evidence of foolproof nuclear power plants. In fact, it is intriguing that just as the push for renewed nuclear power is declared cleaner and safer, nuclear plants are ramping up security precautions for disaster preparedness and because of worries about terrorism. It's a mixed message that calls for studious decision-making."
- "...The world is increasingly eager to reduce emissions [from burning fossil fuels, which purport to create climate changes on earth]. The United States is actively searching for affordable alternative fuels. But frustration over alternative approaches should not be the sole compelling reason to turn to nuclear energy."
- "Browns Ferry has undergone a five-year, \$1.8 billion renovation, with an 'operational readiness' inspection by the Nuclear Regulatory Commission. Officials are emphatic that they have taken great care in testing and approving the site. There have been few problems reported with the other two reactors at Browns Ferry. The renewal is part of a process that is expected to see utility companies seek licenses for up to 30 reactors in the next two years, 24 of which could be in the South. The industry sees this as part of a much cleaner and efficient age of nuclear energy. The Department of Energy is offering incentives of risk insurance, loan guarantees and \$3 billion in tax credits. Demand for the power is certainly high."
- "The nation is right to be on the hunt for options in energy production, and it is encouraging to hear some of the confidence expressed regarding the new nuclear push. But given the history and concerns over the safety and security of nuclear power, it is certainly worth wondering if concentrating on cleaning up the more conventional plants might be where the most human energy should be directed." (*The Tennessean*, 05/21/07)

TVA reports net income of \$126 million for three months ended March 31 st

- TVA, the nation's largest utility, reported net income of \$126 million for the three months ended March 31, 2007, based upon total revenues of \$2.27 billion, up \$229 million from the corresponding period in 2006. The utility said that its improved

profitability was attributable to increased power rates over the past 12 months. Power sales were flat for the quarter, and down 2.8% from budgeted levels for the six months ended March 31. As a result, TVA said that its FY2007 profitability would be down \$60 million or 13.9%, from its \$9.3 billion budget. The agency blamed the mild winter, which reduced its power sales, and a lack of rain, which cut electric generation by 28% less than projected, as the major factors behind its lower profitability. “We expect the dry conditions, which we have experienced since December, to continue to affect TVA's hydro generation output and revenue outlook throughout the summer months,” said the utility’s President and CEO Tom Kilgore. According to the agency’s Form 10Q filing, TVA “has identified cost reductions in operating and maintenance activities to be implemented over the remainder of the year.” (*Associated Press*, Duncan Mansfield, 05/16/07)

TVA adopts a strategic plan focused on increasing its energy efficiency and power production capacity

- Following months of deliberation, revision and public input, the TVA board of directors unanimously approved the utility’s strategic plan, calling for increased power generation capacity and more energy efficiency. TVA conducted nine public comment sessions which garnered about 300 comments, roughly half of which dealt with environmental issues, said TVA president and CEO Tom Kilgore. Much of the plan deals with increasing energy efficiency, from the generation and transmission end to the individual consumer. “About two-thirds of the energy involved in making and transmitting electricity gets away into the environment, usually as heat,” said Kilgore said. “We’re looking for more efficiency.”
- The plan anticipates that TVA will create special electric rates based on time of use, new efforts to promote energy efficiency, and “three-way partnerships [between] TVA, distributors and the end-use consumers.” Kilgore said, “[TVA’s objective is to] try to save one year's worth of growth, which is 500 to 700 megawatts, with energy efficiency and conservation. And if we are able to do more than that, that is a good thing. Because we can retire some of our older coal units.” Greater operating efficiency could represent \$10 billion in savings to TVA, said Kilgore, which could result in layoffs—but declined to say how many positions would be eliminated or when such layoffs would occur. The agency’s strategic plan will require one “single-digit” rate increase, he added, which would go into effect “soon, but not this year.”
- Strategically, TVA also needs to become more self-sufficient. .” Kilgore said, “We need to be close to self-sufficient. We cannot keep buying \$1 billion of power a year and think that’s a good idea.” TVA anticipates it will need to build a second nuclear reactor at the Watts Bar station in Tennessee and two reactors at the Bellefonte site in Alabama by 2019 at a cost of about \$18.5 billion. Kilgore believes that TVA can build these facilities without the agency exceeding its \$30 billion borrowing cap set by Congress. The utility also expects to invest \$4.2 billion on its coal-powered plants in order to meet new air quality requirements on carbon emissions that Congress is

likely to mandate in the future. (*Knoxville News-Sentinel*, Andrew Eder, 05/24/07; *Associated Press*, Duncan Mansfield, 05/23/07; *Associated Press*, Duncan Mansfield, 05/31/07; *Associated Press*, 06/01/07; *Commercial Dispatch* [Columbus, MS], Joey Vaughan, 06/03/07)

Columbus Light & Water joins GENCO, a generation/transmission cooperative

- Columbus [MS] Light & Water has agreed to participate in a generation/transmission cooperative called GENCO, in which power distributors and cooperatives will band together to purchase electric generation facilities and sell power to TVA. The participants in GENCO have concluded that over time TVA will not be able to meet the power demand of its coverage area and will have to purchase power from outside sources. To meet future demand, these local utilities want to own electric generation facilities, which will in turn sell power to TVA. Under this structure, the GENCO members will make capital expenditures and issue debt to fund these assets rather than TVA. “The biggest advantage is the distributors would own a portion of generation,” said CL&W General Manager Todd Gale. “We’d have somewhat of a say-so in the TVA area. ... In the long run, distributors and customers are going to pay for it anyway. This way, customers gain an asset.” Currently, GENCO is in its startup phase. Organizers are researching the corporate structure under which the cooperative could work with TVA. (*Commercial Dispatch* [Columbus, MS], Joey Vaughan, 05/18/07)

TVA facilitates an automobile research alliance

- TVA, the National Transportation Research Center, and the Oak Ridge National Laboratory have organized the Automotive Research Alliance (ARA), in which seven universities [Tennessee, Auburn, Clemson, Mississippi State, Alabama, Alabama-Birmingham, and Kentucky] will participate. The ARA, a powerful alliance of federal research, economic development and university interests, will be dedicated to attracting automotive research and development work to the South. The alliance will act as a central clearinghouse for information on research and technology resources in the region and help link industry, researchers and funding organizations interested in automotive issues. The ARA also will help link top graduates of the participating universities with automotive employers. Kirk H. Schulz, vice president for research and economic development at Mississippi State, said “[The] expansion of the worldwide auto industry into the Southeast is an unprecedented opportunity for Southern research institutions ...to create a technologically savvy work force attuned to this industry.” (*Associated Press*, Bill Poovey, 05/16/07; *Automotive News*, Lindsay Chappell, 05/21/07)

- Memphis Light, Gas and Water was in the news last month, when the public learned that the utility had failed collect more than \$16,000 from former City Councilman Edmund Ford for utility services to his mortuary. As MLG&W moves forward to revamp its credit and collection policies to “restore the public trust,” local residents have learned that they were over-billed more than \$25 million for natural gas that they have yet to consume. City council members are demanding that customers be refunded the overcharges. “We’re in quicksand, so you gotta do a refund [by check rather than credit to customers accounts],” argued City Councilman Joe Brown. However, utility officials say that cutting checks to ratepayers is not an option, because the cost of the related refund (\$284,600 for printing, labor and postage) makes a refund cost-prohibitive. “That is not feasible,” said MPGW general auditor Lesa Walton. [Given MLG&W’s problems with billing, perhaps TVA should audit the utility to ensure that its customers are being billed “without discrimination among customers,” as set forth in the two parties’ contract.] (*Commercial Appeal*, Michael Erskine, 05/16/07; *Commercial Appeal*, Michael Erskine, 05/18/07)

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