



# ISSUE PAPER

**Subject:** Congressional Proposals for Regulation of Fannie Mae and Freddie Mac

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**Issue:** In the last Congress, both the House and the Senate considered legislation and held hearings on regulation of the housing government-sponsored enterprises, Fannie Mae and Freddie Mac (here, the GSEs).<sup>1</sup> Progress was made toward resolution of many of the difficult issues, but final legislation was not enacted. The need for regulatory reform had been underscored by the accounting problems that emerged several years ago at both GSEs. In response to concerns about the size of the GSEs and the limited capability of their regulator, Members of Congress and the Administration have been trying to create a new, more powerful regulator for them.

**Background:** Fannie Mae and Freddie Mac have grown rapidly in debt, mortgage-backed securities (MBS) outstanding and mortgage loan portfolio size. Currently, the Department of Housing and Urban Development (HUD) has a small staff handling the mission regulation of Fannie Mae and Freddie Mac. While the Office of Federal Housing Enterprise Oversight (OFHEO) regulates the GSEs' safety and soundness, it lacks authorities conferred on other financial regulators.

GSE Regulatory Reform Activity in the 109th Congress ---In July 2005, the Senate Banking Committee passed a GSE reform bill, S. 190, along a party-line vote. In October 2005, the full House passed a GSE reform bill, H.R. 1461, by a bipartisan vote of 331 – 90. Those bills terminated at the end of the 109<sup>th</sup> Congress but, because we believe the current House and Senate leadership will build on the work done on them, their characteristics are important. Both bills would have replaced OFHEO and the Federal Housing Finance Board (FHFB) with a new, independent, regulatory agency responsible for the safety, soundness, and mission regulation of Fannie Mae, Freddie Mac, and the Federal Home Loan Banks (FHLBs). The new agency would have overseen the affordable housing goals for Fannie Mae and Freddie Mac, as well as their new programs. The new agency would have had general regulatory authority, which OFHEO lacks today. Both bills would have given the new regulator some authority to require Fannie Mae and Freddie Mac to adhere to their statutory secondary market role. Further, the agency would have been funded by the GSEs and would not be subject to Congressional appropriations.

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<sup>1</sup> The GSE regulatory reform legislation has and will cover the Federal Home Loan Banks in addition to Fannie Mae and Freddie Mac. Because some of the regulatory reform issues pertinent to Freddie Mac and Fannie Mae do not pertain to the Federal Home Loan Banks, we have separate issues for them. For MBA positions with regard to the Federal Home Loan Banks, see the Issue Paper with that same title.

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GSE Regulatory Reform Activity in the 110<sup>th</sup> Congress -- In March, 2007, Chairman Frank introduced H.R. 1427 to reform GSE regulation. The bill would make extensive changes to the affordable housing goals, improve the product review and approval requirements, confer greater financial regulatory authority on the new regulator and establish an affordable housing fund to be funded by the GSEs. It is anticipated that with revisions the bill may be approved by the House of Representatives. It is unclear when the Senate will act on GSE legislation.

**MBA Position:** MBA's longstanding view is that the GSEs must be regulated effectively. Regulation to assure the financial safety and soundness of the GSEs is critical given their size and importance to the housing finance system and to their investors. Effective mission oversight is equally essential to assure that the GSEs continue to provide liquidity to maintain the vitality and the robust, competitive nature of both the primary and secondary markets. MBA believes that the GSEs' activities should be carefully regulated to ensure that they continue to respond to the needs of the secondary market but do not use their government-sponsored benefits to stray beyond their charter missions and distort the competitive landscape of the primary mortgage market.

MBA believes that the regulator should have strong and flexible authority on par with other financial regulators to require and adjust minimum and risk-based capital and to undertake enforcement where necessary. MBA also believes that all aspects of GSE regulation must be independent and well-funded and must be carried out by an entity with the resources and expertise to evaluate the GSEs' performance, both as financial institutions and as public purpose entities with an essential secondary market housing finance mission.

MBA supports conferring power on the regulator to address the risks that may arise from each of the GSE's portfolios and to assure that the portfolios and their use support the GSEs' secondary market mission. However, MBA opposes creation of statutory limits on the amount or types of investments that Fannie Mae and Freddie Mac may hold in portfolio. Because markets are dynamic, the GSEs need flexibility to adjust their portfolios to changing conditions and marketplace needs.

While MBA does not oppose modifications to the law to require registration of the GSEs' stock and debt, it strongly supports continued exemption of mortgage backed securities (MBS) from the registration requirements. MBS registration could hinder the to-be-announced (TBA) MBS market and increase costs to mortgage borrowers.

MBA opposes the provisions in H.R. 1427 which expand the high-cost areas where the conforming loan limits will be increased because the private market is effectively serving these borrowers at competitive prices. While MBA has reservations concerning some specific provisions of H.R. 1427 and the predecessor bills, MBA believes the structure they would create would represent an improvement over the current regulatory system.

**Status:** MBA is encouraged by key provisions of H.R. 1427 and is working with Congressmen Frank's office to make improvements in the bill. MBA is also encouraging

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introduction of a bill in the Senate and is hopeful of passage of legislation in this Congress.

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