

# Federal Housing Finance Agency

---

# Eliminate the Federal Housing Finance Agency

## RECOMMENDATION

Congress should eliminate the Federal Housing Finance Agency (FHFA) upon the dissolution of the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac).

Until Congress eliminates it, the FHFA should maintain a limited role as regulator of the Federal Home Loan Banks (FHLBs) and the FHLB Office of Finance, as well as conservator and regulator of Fannie Mae and Freddie Mac.

Specifically, the FHFA should cease any policies that expand the scope of the institutions under its purview. These reforms should include the following changes to the operations of Fannie Mae and Freddie Mac during conservatorship:

- Decrease, annually, the loan limits for conforming mortgages that Fannie Mae and Freddie Mac are eligible to acquire;
- Increase the guarantee fees charged by both Fannie Mae and Freddie Mac in their respective mortgage-backed securities portfolios;
- Maintain the covenant of the third amendment to the preferred stock purchase agreements (PSPAs) that deplete the capital reserves for both Fannie Mae and Freddie Mac by January 1, 2018;
- Cease the implementation of the Common Securitization Platform currently under development by Fannie Mae and Freddie Mac;
- Close the Housing Trust Fund and the Capital Magnet Fund that use revenue from both institutions as finance mechanism; and
- Cease the implementation of the Duty to Serve Underserved Markets regulatory regime, which the FHFA submitted as a final rule to the *Federal Register* in December of 2016.

## RATIONALE

In 2008, Congress established the FHFA as the federal agency authorized to regulate the government-sponsored enterprises (GSEs) dealing with housing; specifically, charged with regulating the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporation, the FHLBs, and the Federal Home Loan Bank Office of Finance. Congress created the FHFA as part of the Housing and Economic Recovery Act (HERA) of 2008, replacing the Office of Federal Housing Enterprise Oversight (OFHEO) as regulator of Fannie Mae and Freddie Mac, and the Federal Housing Finance Board as regulator of the FHLBs and the FHLB Office of Finance.<sup>1</sup> In addition to providing the FHFA with regulatory authority over these GSEs, HERA provided the statutory authority for the FHFA to decide whether to place the financially insolvent Fannie Mae and Freddie Mac into a federal conservatorship, or to structure a liquidation of the GSEs under a federal receivership.

Acting on its statutory authority, the FHFA decided after the 2008 passage of HERA to place both Fannie Mae and Freddie Mac into a federal conservatorship, and the two GSEs have remained under this oversight status. Also in 2008, the FHFA coordinated with the U.S. Department of the Treasury a PSPA structure with Fannie Mae and Freddie Mac.<sup>2</sup> The PSPAs have since been amended three separate times, and under the terms of the third amendment, the Treasury retains exclusive rights to dividend payments as the senior preferred shareholder of both Fannie Mae and Freddie Mac. The PSPAs included a forcing mechanism of sorts to structural reform of both Fannie Mae and Freddie Mac in that the capital reserve accounts for both GSEs must net to zero by January 1, 2018. Fannie Mae and Freddie Mac still retain a separate line of credit with the Treasury to cover instances of financial loss, though this covenant of the PSPA will effectively deplete their ability to retain any earnings year to year after January 1, 2018.

HERA carried over statutory authority and created expanded duties for the FHFA as the regulator of Fannie Mae and Freddie Mac. Carryover authority for the FHFA includes, for example, the oversight of housing goals required of both GSEs; HERA also outlined expanded duties for the FHFA, including broader oversight of the management and governance of the GSEs, as well as an expansion of the mandatory obligation of the GSEs to provide affordable housing credit to underserved markets.<sup>3</sup> Beyond these statutory powers outlined of the agency in HERA, the FHFA has also decided to design not only a strategic direction for itself as a regulatory agency, but also to build out parameters for the securitization market.<sup>4</sup> Specifically, the FHFA concretely established in its strategic plan the creation of a common securitization platform (CSP), an undertaking that will, if fully enacted, provide the structure for the dissemination of a standard, uniform mortgage-backed security. The development of the CSP is a critical element of the FHFA's vision for the U.S. mortgage securitization market. The FHFA should cease, however, the development of this securitization platform; the federal government should neither fund nor direct the development of any particular product in the secondary mortgage market.<sup>5</sup>

Federal reforms of all three GSEs are crucial for the creation of a stable and resilient housing-finance system. The GSEs' institutional design is fundamentally flawed, and the public-private nature of their charters

has created enormous, and highly unfortunate, opportunities for federal politicians to advance nebulous housing policies. Moreover, the GSE institutional model has effectively cost taxpayers during normal housing markets, in addition to the substantial costs during episodes of financial failure. Certainly prior to the 2008 FHFA conservatorship and Treasury bailout, the GSEs benefited from funding advantages not conferred to other financial institutions, allowing them to borrow at below market-interest rates to cover their business operations.

Other privileges bestowed on the GSEs, providing financial benefits (costing taxpayers) across market cycles, include exemptions from regulatory and compliance filings, as well as various tax exemptions. Ideally, Congress will enact legislation that shuts down Fannie Mae and Freddie Mac, and enact reforms that eliminate all federal subsidies and mandates that govern the 11 FHLBs, the Office of Finance that issues debt to the FHLBs, and all financial member institutions.<sup>6</sup>

After reforming the housing-finance GSEs, Congress should eliminate the FHFA. The FHFA would have no continuing role as a federal property manager (conservator) once Congress dissolves Fannie Mae and Freddie Mac, in addition to transferring any ongoing regulatory functions of the reformed (private, non-GSE) FHLB system to a separate federal department or agency.

---

## ADDITIONAL READING

- John L. Ligon, "A Pathway to Shutting Down the Federal Housing Finance Enterprises," Heritage Foundation *Background* No. 3171, December 21, 2016.
- Norbert J. Michel and John L. Ligon, "Five Guiding Principles for Housing-Finance Policy: A Free-Market Vision," Heritage Foundation *Issue Brief* No. 4259, August 11, 2014.

---

## ENDNOTES

1. Housing and Economic Recovery Act of 2008, Public Law 110–89 § 1101 and 1204, <https://www.gpo.gov/fdsys/pkg/PLAW-110publ289/html/PLAW-110publ289.htm> (accessed October 11, 2016).
2. Federal Housing Finance Agency, “Senior Preferred Stock Purchase Agreements,” <https://www.fhfa.gov/Conservatorship/Pages/Senior-Preferred-Stock-Purchase-Agreements.aspx> (accessed May 11, 2017).
3. John L. Ligon, “Mortgage Principal Forgiveness Is a Bad Idea,” Heritage Foundation *Issue Brief* No. 4598, August 1, 2016, <http://www.heritage.org/housing/report/mortgage-principal-forgiveness-policy-bad-idea>; Norbert J. Michel, John L. Ligon, and Filip Jolevski, “GSE Reform: FHFA Should Not Pursue Principal Reduction Alternatives,” Heritage Foundation *Issue Brief* No. 4108, December 17, 2013, <http://www.heritage.org/housing/report/gse-reform-fhfa-should-not-pursue-mortgage-principal-reduction-alternatives>; and Norbert J. Michel and John L. Ligon, “GSE Reform: Trust Funds or Slush Funds?” Heritage Foundation *Issue Brief* No. 4080, November 7, 2013, <http://www.heritage.org/housing/report/gse-reform-trust-funds-or-slush-funds>.
4. Federal Housing Finance Agency, “FHFA Sends Congress Strategic Plan for Fannie Mae and Freddie Mac Conservatorships,” February 21, 2012, [https://www.fhfa.gov/AboutUs/Reports/ReportDocuments/20120221\\_StrategicPlanConservatorships\\_508.pdf](https://www.fhfa.gov/AboutUs/Reports/ReportDocuments/20120221_StrategicPlanConservatorships_508.pdf) (accessed May 11, 2017).
5. John L. Ligon and Norbert J. Michel, “Why Is Federal Housing Policy Fixated on 30-Year Fixed-Rate Mortgages?” Heritage *Backgrounder* No. 2917, June 18, 2014, <http://www.heritage.org/housing/report/why-federal-housing-policy-fixated-30-year-fixed-rate-mortgages>, and Norbert J. Michel and John L. Ligon, “Five Guiding Principles for Housing-Finance Policy: A Free-Market Vision,” Heritage Foundation *Issue Brief* No. 4259, August 11, 2014, pp. 2 and 3, <http://www.heritage.org/housing/report/five-guiding-principles-housing-finance-policy-free-market-vision>.
6. Michel and Ligon, “Five Guiding Principles for Housing-Finance Policy,” pp. 1–3.