



Fannie Mae, Freddie Mac Deal Raises Troubling Issues

By Mark Melin

March 13, 2014

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When the US Senate Banking Committee announced plans to replace Fannie Mae / Federal National Mortgage Assctn Fnni Me (OTCBB:FNMA) and Freddie Mac / Federal Home Loan Mortgage Corp (OTCBB:FMCC) with a new government backed program, shares of the stocks dropped dramatically, down nearly 15% on Wednesday and off more than 30% the day previous as rumors had been swirling. While the measure had bipartisan participation from the Obama administration, the bill's passage is uncertain. If it does pass, Congress must then decide on "fair" treatment for investors.

The bill might not get attention before political leaders start to consider elections, according to a [Bloomberg](#) report. Once it does receive attention there is no guarantee that the program will receive a warm reception in Congress. A Democratic Senate aide was quoted in the report saying leadership is currently unenthusiastic about legislation that would eliminate Fannie Mae and Freddie Mac.

"It's possible, but it's certainly not probable," Mark Calabria, a former aide on the Senate banking panel who now directs financial regulation studies at the [Cato Institute](#), was quoted in the report saying. "You're looking at maybe a 10 percent chance of a bill getting to the president's desk."

Toomey seeks "fair" treatment for investors, hits raw topic of validity of government contract

In regards to "fair" treatment for investors, Sen. Patrick Toomey (R-PA) is pushing a contentious issue on the floor of the Senate. Speaking with US Treasury Secretary Jack Lew, Toomey touched on what could be a key issue.

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“When the government stepped in and bailed out Fannie Mae / Federal National Mortgage Assctn Fnni Me (OTCBB:FNMA) and Freddie Mac / Federal Home Loan Mortgage Corp (OTCBB:FMCC), they signed a very specific agreement with the board of directors, which they entered into voluntarily,” Toomey said in [Senate questioning](#) of Lew. “This agreement involves the government providing guarantees and a line of credit and a very specific return. The government would receive a 10% return on the money it extended and options to purchase 79% of Fannie Mae and Freddie Mac.”

The agreement between the board of directors and shareholders was clear, until the government changed the terms without any agreement of the board of directors or representatives of shareholders. “In August of 2012, just as it was becoming apparent that Fannie Mae / Federal National Mortgage Assctn Fnni Me (OTCBB:FNMA) and Freddie Mac / Federal Home Loan Mortgage Corp (OTCBB:FMCC) were going to return to significant profitability, the government came along and negotiated a new deal with itself,” Toomey said, highlighting the unusual situation. “With the treasury secretary on one side and a government appointed regulator on the other side, they wrote a new agreement whereby the government now gets 100% of the profits, when the previous agreement stipulated the government would have ownership of just under 80%.”

Breach of contract?

Then Toomey asked the money question. “Isn’t this a serious breach of the sanctity of contracts and doesn’t this undermine our commitment to the rule of law to have done this?”

Lew avoided the question, but ultimately Toomey wouldn’t let it go.

“We have had a very clear policy on Fannie Mae / Federal National Mortgage Assctn Fnni Me (OTCBB:FNMA) and Freddie Mac / Federal Home Loan Mortgage Corp (OTCBB:FMCC), which is we are winding them down. This is important because we are making progress on a bipartisan basis to work on housing finance reform,” said Lew, not addressing the key issue of the government violating a written agreement.

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“When you look at the agreements that were made for the federal government to step in and become a conservator and subsequent agreements that were made, it serves the public interest,” he said, addressing the written agreement but not answering the core question about the validity of the agreement. “The sooner we get on with the debate about housing finance reform the better.”

Then Lew moved to change the issue. “We sent clear signals of what our policy path was, so no one was not informed of what the goal was. The damage done to our economy because of the failures of Fannie and Freddie were deep and I think the policies in place were right.”

After Lew attempted to change the topic to Ukraine, Toomey asked a follow up question that again wasn't answered. "Whatever signals you sent about policy cannot be more important than a contract that has been signed," Toomey questions, hitting on the core issue once again. "When the American people... can't have confidence in a contract they have with the US government, I think that has a chilling effect on our economy and our ability to attract private capital to housing reform."

After this Toomey's time had expired and Lew avoided answering the key question.

(Here is a link to the video. The interaction starts at 1 hour and 12 minutes into the [testimony](#).)