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Lawmakers looking to take charge of Fannie and Freddie reform

Bill would guard against abrupt privatization or nationalization

By: Teke Wiggin - March 14, 2013

the Senate Banking, Housing and Urban Affairs Committee introduced a bill today that many industry experts say could pave the way for reforming bailed-out mortgage giants Fannie Mae and Freddie Mac.

The "Jumpstart GSE Reform Act," unveiled by Senators Bob Corker, R-Tenn., Mark Warner, D-Va., David Vitter, R-La. and Elizabeth Warren, D-Mass., would erect barriers that would prevent the companies from abruptly exiting government conservatorship or morphing into government "cash cows," as one expert put it.

"We know our housing finance system is not sustainable in its current form, and this legislation will keep us on a path to accomplish real reforms," Warren said in a statement.

The bill would prohibit the Treasury from causing the government to relinquish control of the GSEs ("government sponsored enterprises"). The Treasury currently could cut loose Fannie Mae and Freddie Mac by selling its preferred shares of the GSEs (shares that, by extension, are owned by taxpayers) to private investors.

But the proposed bill would prohibit the Treasury from selling those shares without Congressional approval and GSE reform, putting the future of the GSEs, which back more than half of U.S. mortgages, in the hands of Congress.

In addition, the bill would block the GSEs from potentially drifting towards sustained nationalization, by preventing Congress from hiking the guarantee fees charged by Fannie and Freddie to offset government spending.
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Raising guarantee fees could help bring back the secondary market for mortgages not guaranteed by the government, Fannie and Freddie's regulator, the Federal Housing Finance Agency, said in raising fees last year.

But tapping Fannie and Freddie guarantee fees as a source of government revenue is a slippery slope, said Mark Calabria, director of financial regulation studies at the Cato Institute, because it could make Congress reliant on the GSEs and reluctant to dismantle them.

In 2011, Congress demonstrated that it isn't above milking the GSEs for cash when it mandated that the G-fee for 2012 be raised by 0.1 percent in order to make up for lost revenue from a tax cut. In December 2012, the House took G-fee financing a step further, passing a bill that would extend fee hikes to help pay for immigration reform.

"We shouldn't continue to treat these organizations as cash cows," Calabria said.

The Mortgage Bankers Association (MBA) also has balked at leaning on the GSEs for funding, contending that fees should only be raised to hedge against losses that stem from defaults on mortgages that the GSEs guarantee.

David H. Stevens, president and CEO of the MBA, applauded the bill, saying in a statement that its sponsors should be "commended for introducing this piece of legislation and spearheading a transparent, complete discussion about the future of GSEs and the government's role in the housing markets."

The MBA pointed out, however, that the bill merely lays the groundwork for reform. Winding down Fannie and Freddie, the arteries of the U.S. mortgage finance system, is a task that Congress has shied away from ever since the government placed the companies in conservatorship in 2008.

Dismantling the GSEs could negatively impact consumers, some experts say. The GSEs help keep mortgage rates low by keeping investment capital flowing into mortgage lending. Investors see mortgage-backed securities (MBS) guaranteed by Fannie and Freddie as a safe place to put their money, and are willing to accept yields that are not much higher than bonds issues by the government.

Some say private companies could play the same role, without obligating the government -- and taxpayers -- to come to the rescue. But critics say that without some form of government backstop, the cost of taking out a mortgage would probably go up.