JEB HENSARLING, TX, CHAIRMAN

United States House of Representatives
Committee on Financial Services
2129 Rayburn House Office Building
Washington, D.C. 20515

MAXINE WATERS, CA, RANKING MEMBER

April 2, 2014

The Honorable Melvin L. Watt
Director
Federal Housing Finance Agency
400 7th Street SW
Washington, DC 20024

Dear Director Watt:

As your former colleagues on the House Financial Services Committee, we urge you to continue the Federal Housing Finance Agency's ("FHFA") suspension of contributions to the Affordable Housing Trust Fund and the Capital Magnet Fund ("Funds"), a policy that has been in place for more than five years.

As you know, the Treasury Department – and therefore taxpayers – currently own $189 billion in outstanding senior preferred shares of the Federal National Mortgage Association ("Fannie Mae") and the Federal Home Loan Mortgage Corporation ("Freddie Mac"), commonly referred to as "Government Sponsored Enterprises" ("GSEs"), from the GSEs' bailout, which began in September 2008. We believe that any money diverted from the GSEs to these Funds is money that would otherwise be used to compensate taxpayers for their investment. Further, given the GSEs' conservatorship status, financing these Funds would violate the letter and spirit of the Housing and Economic Recovery Act ("HERA"), a law you supported while in Congress. Lastly, policymakers are in the midst of considering significant reforms to our housing finance system. Any changes to existing policy regarding trust fund payments would be premature given these ongoing policy discussions.

Since 2008, the U.S. taxpayers have provided $189 billion directly to the GSEs. Beyond the direct financial bailout, Fannie Mae and Freddie Mac continue to rely heavily on both taxpayer support and their status as GSEs in executing their day–to-day business operations.[1] Contrary to what some may claim, Fannie Mae and Freddie Mac have yet to "repay" any of the taxpayer-provided bailout. As the terms of their taxpayer bailout dictates, the cash injection constitutes a draw from the U.S. Treasury, not a loan. Thus, taxpayers are still owed tens of billions of dollars. Further, Fannie Mae and Freddie Mac's cost to the taxpayers far exceeds the

[1] See p. 93 of Fannie Mae 2013 10-Q for quarterly period ending September 30, 2013:
"Our ability to issue long-term debt has been strong primarily due to actions taken by the federal government to support us and the financial markets.... We believe that continued federal government support of our business and the financial markets, as well as our status as a GSE, are essential to maintaining our access to debt funding. Changes or perceived changes in the federal government support of our business and the financial markets or our status as a GSE could materially and adversely affect our liquidity, financial condition and results of operations." Available at: http://www.fanniemae.com/resources/file/ir/pdf/quarterly-annual-results/2013/q32013.pdf

terms of their bailout. Their failed business model was at the epicenter of the financial crisis – a crisis that froze fixed income markets, threw millions of Americans out of work and destroyed trillions of dollars in household wealth. It should be clear that any recent positive cash flow from Fannie Mae and Freddie Mac is directly attributable to extensive and continued taxpayer support and any positive cash flow should go directly to the Treasury.

Further, the authors of HERA foresaw the need to suspend contributions to these funds in the face of financial difficulty at the Enterprises. Specifically, Sec. 1337(b) of HERA states:

> "The Director shall temporarily suspend allocations [to fund the Housing Trust Fund and Capital Magnet Fund] by an enterprise upon a finding by the Director that such allocations (1) are contributing, or would contribute, to the financial instability of the enterprise; (2) are causing, or would cause, the enterprise to be classified as undercapitalized; or (3) are preventing, or would prevent, the enterprise from successfully completing a capital restoration plan."

In your capacity as conservator, you are well aware that the GSEs are financially unstable and severely undercapitalized. Diverting assets to housing trust funds instead of improving and increasing the GSE's capital base, or repaying taxpayers, would only exacerbate their already weakened financial position. And despite recent profitability, risks to the GSEs and the taxpayers remain. According to FHFA's most recent Annual Report to Congress:

> "The Enterprises remain exposed to credit, counterparty, and operational risks. Credit risk management remains a key priority for both Enterprises given their large volume of distressed assets and ongoing stress in certain housing markets. In addition, counterparty risk remains an area of concern, especially given the evolving changes in the mortgage industry and the greater prominence of new types of seller-servicers. Operational risk also remains a focus because of challenges related to legacy systems, recordkeeping and ongoing concerns about human capital and key person dependencies."[2]

Lastly, we believe that altering FHFA's long-standing policy regarding trust fund allocations could undermine ongoing efforts to reform the housing finance system. While several legislative initiatives are pending in Congress to reform the GSEs, so far no consensus has yet emerged on whether (and how) these Funds should be financed going forward.

[2] FHFA Annual Report to Congress (2012). Available at:
http://www.fhfa.gov/webfiles/25320/FHFA2012_AnnualReport-508.pdf

Any deviation from current policy regarding these Funds would be a grave mistake. Such a move would further imperil taxpayers and would violate both the letter and spirit of the law. Therefore, we ask that that FHFA refrain from taking such a step prior to Congressional action on the future of the housing finance system.

Sincerely,

JEB HENSARLING
Chairman
Committee on Financial Services

SCOTT GARRETT
Chairman
Subcommittee on Capital Markets and
Government Sponsored Enterprises

ED ROYCE
Member of Congress