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## **Improving the Effectiveness of GSE Oversight: Legislative Proposals in the 108<sup>th</sup> Congress**

**Updated January 6, 2005**

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# Improving the Effectiveness of GSE Oversight: Legislative Proposals in the 108<sup>th</sup> Congress

## Summary

Fannie Mae and Freddie Mac, two of the largest government-sponsored enterprises (GSEs), were created to establish a secondary mortgage market in order to improve the distribution of capital available for home mortgage financing. To help these institutions accomplish this mission, Congress granted them several statutory benefits not available to other private companies. The advantages of GSE status have helped the enterprises to grow rapidly and become the dominant players in the secondary mortgage market.

In 1992, Congress established the Office of Federal Housing Enterprise Oversight (OFHEO), an independent agency within the Department of Housing and Urban Development (HUD), to oversee the financial safety and soundness of the enterprises. OFHEO is authorized to set capital requirements, conduct annual risk-based examinations, and generally enforce compliance with safety and soundness standards.

With the rapid growth in the GSEs, questions have been raised about the effectiveness of the current regulatory regime. Several legislative proposals introduced in the past addressed GSE regulatory reform, but Congress did not take action on them. However, with the recent accounting problems at both Fannie Mae and Freddie Mac, the adequacy of GSE regulation has become a prominent legislative issue once again.

Four bills were considered in the 108<sup>th</sup> Congress that aimed to strengthen the current regulatory framework and improve the effectiveness of GSE supervision: H.R. 2575 (Representative Baker), H.R. 2803 (Representative Royce), S. 1508 (Senators Hagel\Sununu\Dole), and S. 1656 (Senator Corzine). On March 26, 2004, Chairman Shelby of the Senate Banking Committee released a draft bill, which was offered as a substitute for S. 1508 during markup on April 1, 2004, and passed by the committee with several amendments. No further legislative action was taken during the 108<sup>th</sup> Congress. While the proposals took somewhat different approaches to regulatory reform, all appeared to

- abolish OFHEO and reconstitute the GSE regulator within the Department of the Treasury, or as an independent agency;
- increase the budget autonomy of the new office by exempting its assessments from the annual appropriations process; and
- enhance the safety and soundness and enforcement tools available to the new regulator.

This CRS report describes OFHEO's current regulatory framework and provides a detailed analysis of legislative proposals in the 108<sup>th</sup> Congress that aimed to strengthen the safety and soundness regulation of the GSEs. This report is an historical record of consideration of this issue in the 108<sup>th</sup> Congress and will not be updated.

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# Improving the Effectiveness of GSE Oversight: Legislative Proposals in the 108<sup>th</sup> Congress

## Introduction

Government-sponsored enterprises (GSEs) are privately owned, congressionally chartered financial institutions created for specific public policy purposes. They benefit from certain exemptions and privileges, including an implied federal guarantee, intended to enhance their ability to borrow money. The two largest GSEs are Fannie Mae and Freddie Mac (herein referred to as the enterprises or GSEs).<sup>1</sup> These GSEs were created by Congress to establish and maintain a secondary mortgage market, increasing liquidity and improving the distribution of capital available for home mortgage financing.<sup>2</sup> To help these institutions accomplish this mission, Congress has provided them with several benefits not available to other financial institutions.<sup>3</sup> These statutory benefits provide the enterprises with lower funding costs, the ability to operate with less capital, and lower direct costs.<sup>4</sup> The advantages of GSE status have enabled the enterprises to grow rapidly and become dominant players in the secondary mortgage market.

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<sup>1</sup> The other GSEs are the Federal Home Loan Bank System, the Farm Credit System, and Farmer Mac. Sallie Mae, a sixth GSE, is in the process of being fully privatized.

<sup>2</sup> For a detailed description of the development of the U.S. secondary mortgage market, see Office of Federal Housing Enterprise Oversight, *Report to Congress*, June 2003, at [<http://www.ofheo.gov/media/pdf/WEBSITEOFHEOREPTOCONGRESS03.pdf>], visited on Oct. 4, 2004.

<sup>3</sup> These statutory benefits include (1) exemption from state and local taxes, (2) a line of credit with the U.S. Treasury up to \$2.25 billion, (3) eligibility of their debt to serve as collateral for public deposits, (4) eligibility of their securities for Federal Reserve open market purchases, (5) eligibility for their corporate securities to be purchased without limit by federally regulated financial institutions, (6) assignment of mortgage-related securities they have issued or guaranteed to the second-lowest credit risk category at depository institutions, and (7) exemption from the registration requirements of the Securities and Exchange Commission.

<sup>4</sup> For more information on these advantages, see the following reports: U.S. Department of the Treasury, *Government Sponsorship of the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation*, July 11, 1996; U.S. Congressional Budget Office, *Assessing the Public Costs and Benefits of Fannie Mae and Freddie Mac*, May 1996; and U.S. Congressional Budget Office, *Federal Subsidies and the Housing GSEs*, May 2001.

Congress has always been concerned that the safety and soundness of the enterprises be maintained so that they can meet their public policy mission and not pose risks to taxpayers. Prior to 1992, oversight was the responsibility of the Department of Housing and Urban Development (HUD) and the Federal Home Loan Bank Board. In 1992, Congress established the Office of Federal Housing Enterprise Oversight (OFHEO), an independent agency within HUD, to oversee the financial safety and soundness of the enterprises. The office is authorized to set capital requirements, conduct annual risk-based examinations, and generally enforce compliance with safety and soundness standards.

Since the creation of OFHEO, mortgage investments at the GSEs have grown by more than 620% to \$1.4 trillion. The GSEs have become two of the largest private debt issuers in the world. At the end of 2002, the combined debt of the enterprises totaled \$1.5 trillion — an amount equal to almost half of all publicly held federal debt. In addition to enterprise debt, investors now hold over \$1.7 trillion in mortgage-backed securities issued by Fannie Mae and Freddie Mac.<sup>5</sup>

As a result of the rapid growth of these institutions and their implied federal backing, there has been an increasing concern that the enterprises may pose a problem of systemic risk to the nation's financial system.<sup>6</sup> At the same time, questions have been raised about the effectiveness of the current regulatory environment. There have been several legislative proposals introduced in the past to address these issues, but Congress did not take action on them.

Events in the past two years, however, have brought a new urgency to this issue. In 2003, Freddie Mac admitted that it had used improper accounting policies to create the appearance of steady earnings growth and issued a restatement of financial results, revising net income for 2000-2002 upwards by \$5 billion.<sup>7</sup> OFHEO imposed a \$125 million fine and is pursuing civil actions against several former Freddie executives.<sup>8</sup> Following the special examination of Freddie Mac, OFHEO began to

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<sup>5</sup> For more information, see Office of Federal Housing Enterprise Oversight, *FY 2003-2008 Strategic Plan*, Sep. 30, 2003, at [<http://www.ofheo.gov/media/pdf/0308stratplan93003a.pdf>], visited Oct. 4, 2004.

<sup>6</sup> For a comprehensive analysis of these risks, see Office of Federal Housing Enterprise Oversight, *Systemic Risk: Fannie Mae, Freddie Mac, and the Role of OFHEO*, Feb. 2003, at [<http://www.ofheo.gov/media/archive/docs/reports/sysrisk.pdf>], visited Oct. 4, 2004. Furthermore, the IMF has recently stated that the GSE “regulators need to look closely at whether agencies’ capital adequacy is sufficient, especially bearing in mind the questions about internal controls that have emerged in Freddie Mac....it is unclear whether [the GSEs] have taken sufficient account of the risk that the market may not be deep enough to allow them to continuously hedge their growing portfolios in times of stress.” For more information, see IMF, *Global Financial Stability Report: Market Developments and Issues*, Sept. 2003, pp. 16-22, at [<http://www.imf.org/external/pubs/ft/gfsr/2003/02/index.htm>], visited on Oct. 4, 2004.

<sup>7</sup> For more information, see CRS Report RS21567, *Accounting and Management Problems at Freddie Mac*, by Mark Jickling.

<sup>8</sup> For more information, see the Dec. 10, 2003 press release issued by OFHEO at (continued...)

review the accounting policies and practices at Fannie Mae, and recently published its preliminary findings on September 22, 2004.<sup>9</sup> OFHEO charges that Fannie Mae did not follow generally accepted accounting practices in two critical areas: (1) amortization of discounts, premiums, and fees involved in the purchase of home mortgages and (2) accounting for financial derivatives contracts. According to OFHEO, these deviations from standard accounting rules allowed Fannie Mae to reduce volatility in reported earnings, present investors with an artificial picture of steadily growing profits, and, in at least one case, to meet financial performance targets that triggered the payment of bonuses to company executives.<sup>10</sup> On December 15, 2004, the Securities and Exchange Commission (SEC) directed Fannie Mae to restate its accounting results since 2001 after finding inadequacies in Fannie's accounting policies and methodologies. These accounting problems, and the related safety and soundness concerns, have made GSE regulatory reform a prominent legislative issue once again.

Four bills were considered in the 108<sup>th</sup> Congress that aimed to strengthen the current regulatory framework and improve the effectiveness of GSE supervision: H.R. 2575 (Representative Baker), H.R. 2803 (Representative Royce), S. 1508 (Senators Hagel\Sununu\Dole), and S. 1656 (Senator Corzine).

In addition, the House Financial Services Committee released a manager's amendment in preparation for a markup originally scheduled for October 8, 2003. However, on October 7, 2003, the Department of the Treasury announced its opposition to the manager's amendment, claiming the bill "falls short of real reform."<sup>11</sup> Subsequently, the markup was postponed and the current status of the manager's amendment remains uncertain.

On March 26, 2004, Chairman Shelby of the Senate Banking Committee released a draft GSE reform bill. On April 1, 2004, the draft was offered at committee markup as an amendment in the nature of a substitute for S. 1508, and was passed with several further amendments. No further legislative action was taken on this or any other GSE reform bill before the adjournment of the 108<sup>th</sup> Congress.

While the proposals take somewhat different approaches to regulatory reform, all appear to

- abolish OFHEO and reconstitute the GSE regulator within the Department of the Treasury, or as an independent agency;

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<sup>8</sup> (...continued)

[<http://www.ofheo.gov/News.asp?FormMode=Release&ID=119>], visited on Oct. 4, 2004.

<sup>9</sup> Office of Federal Housing Enterprise Oversight, *Report of Findings to Date: Special Examination of Fannie Mae*, Sept. 17, 2004, available at [<http://www.ofheo.gov/media/pdf/FNMfindingsstodate17sept04.pdf>], visited on Oct. 4, 2004.

<sup>10</sup> For a detailed summary of OFHEO's findings, see CRS Report RS21949, *Accounting Problems at Fannie Mae*, by Mark Jickling.

<sup>11</sup> Robert Blackwell and Jody Shenn, "It's Official: White House Won't Back Oxley GSE Bill," *American Banker*, Oct. 8, 2003.

- increase the budget autonomy of the new office by exempting its assessments from the annual appropriations process; and
- enhance the safety and soundness and enforcement tools available to the new regulator.

Treasury Secretary John Snow appeared before the House Financial Services Committee on September 10, 2003, and then again before the Senate Banking Committee on October 16, 2003, to outline the Administration's recommendations "for the essential, minimum requirements for a credible regulator"<sup>12</sup> for the housing GSEs. In addition to the creation of a new agency to oversee the safety and soundness of all the housing GSEs (Fannie Mae, Freddie Mac, and the Federal Home Loan Banks), the Treasury Secretary outlined several recommendations intended to strengthen the new agency's general regulatory, supervisory and enforcement powers. The President's budget plan for FY2005 reiterates these recommendations, but also specifically proposes that the new agency be placed within the Department of the Treasury, "provided the Department is given adequate oversight authority."<sup>13</sup> Currently, there is no legislative proposal that encompasses all of the Administration's recommendations.

However, in testimony before the Senate Banking Committee, Federal Reserve Board Chairman Alan Greenspan noted that "[w]orld-class regulation, by itself, may not be sufficient and indeed, as suggested by Treasury Secretary Snow, may even worsen the situation if market participants infer from such regulation that the government is all the more likely to back GSE debt."<sup>14</sup> Concerned that this may continue to encourage the enterprises to grow faster than the residential mortgage market, posing a potential a risk to the nation's financial system, the Federal Reserve Board Chairman urged Congress to also consider limiting the GSEs' debt issuance and asset purchases. The Treasury Department, however, has recently claimed that it already has the authority to limit the GSEs' debt issuances and that such action is currently being considered.<sup>15</sup>

This report describes OFHEO's current regulatory framework and provides a detailed analysis of the legislative proposals introduced in the 108<sup>th</sup> Congress that aim

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<sup>12</sup> Prepared testimony of John W. Snow, Secretary of the Treasury, in U.S. Congress, Senate Committee on Banking, Housing and Urban Affairs, *Proposals for Improving the Regulation of the Housing GSEs*, hearings, 108<sup>th</sup> Cong., 1<sup>st</sup> sess., Oct. 16, 2003, p. 2, at [[http://banking.senate.gov/\\_files/ACFB2.pdf](http://banking.senate.gov/_files/ACFB2.pdf)], visited on Oct. 4, 2004.

<sup>13</sup> See the Office of Management and Budget, *Budget of the United States Government, Fiscal Year 2005, Analytical Perspectives*, p. 83, at [<http://www.whitehouse.gov/omb/budget/fy2005/pdf/spec.pdf>], visited on Oct. 4, 2004.

<sup>14</sup> Prepared testimony of Alan Greenspan, Chairman, Board of Governors of the Federal Reserve System, in U.S. Congress, Senate Committee on Banking, Housing and Urban Affairs, *Proposals for Improving the Regulation of the Housing Government Sponsored Enterprises*, hearings, 108<sup>th</sup> Cong., 2<sup>nd</sup> sess., Feb. 24, 2004, p. 9, at [[http://banking.senate.gov/\\_files/ACF1BA.pdf](http://banking.senate.gov/_files/ACF1BA.pdf)], visited on Oct. 4, 2004.

<sup>15</sup> Rob Blackwell, "A Treasury View on GSE Debt, And Unintended Consequences," *American Banker*, May 14, 2004.

to strengthen the safety and soundness regulation of the enterprises. A short summary of the Administration's views on GSE oversight can be found in the final section of this report.

## The Current Regulatory Framework

OFHEO is an independent agency, within HUD, whose primary mission is to oversee the financial safety and soundness of the enterprises. The office was established by Congress with the passage of the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (herein referred to as the Safety and Soundness Act).<sup>16</sup> In order to fulfill its mission, OFHEO is authorized to establish and ensure compliance with capital standards for the enterprises, conduct annual risk-based examinations to assess the management practices and financial condition of the enterprises, and take enforcement actions as specified by the Safety and Soundness Act. Mission regulation — ensuring the enterprises comply with their affordable housing mandates — is within the purview of HUD.

OFHEO is under the management of a director, who is appointed by the President and confirmed by the Senate, for a term of five years. The office is funded through annual assessments collected from the enterprises on a semi-annual basis. Unlike other financial regulators, however, OFHEO's assessments are subject to the annual congressional appropriations process.

### Capital Standards

The Safety and Soundness Act mandated the adoption of three capital level standards for the enterprises: (1) the minimum level, (2) the critical level and (3) the “risk-based” level. The first two levels are considered static standards, where a certain amount of capital is required to be held for every dollar of assets and may vary according to the riskiness of the assets. The third level is a performance standard derived from “stress tests.” These types of capital standards indicate how well the capital on hand functions in keeping a company solvent under a variety of adverse economic conditions. Their worth depends upon how well the stress tests are structured.

**The Minimum Level.** The minimum capital standard requires each enterprise to hold capital equal to the sum of 2.5% of its on-balance sheet assets, plus 0.45% of the unpaid balance of mortgage-backed securities sold off-book, plus 0.45% of other off-balance sheet obligations.

**The Critical Level.** The critical capital standard requires that the enterprises hold capital equal to the sum of 1.25% of on-balance sheet assets, plus 0.25% of the

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<sup>16</sup> P.L. 102-550, Title XIII; 106 Stat. 3941 (1992). For a detailed analysis of the oversight provisions of this law, see CRS Report RL32230, *Regulation of Fannie Mae and Freddie Mac Under the Federal Housing Enterprises Financial Safety and Soundness Act: A Legal Analysis*, by Nathan Brooks.



unpaid balance of mortgage-backed securities, plus 0.25% of other off-book obligations.

**The Risk-Based Level.** The risk-based capital standard requires each enterprise to hold enough capital to cover both credit and interest rate risks, plus an additional 30% for management and operations risk.<sup>17</sup> Credit or default risk is the risk that a borrower will default on the mortgage which the company holds as an asset. Interest rate risk is the risk of loss should rates rise or fall dramatically. This risk arises because funds borrowed by the enterprises may come due and have to be refinanced at new interest rates on a different schedule than the funds received from investments which earn yields set under different market conditions.

The Safety and Soundness Act specified several of the details regarding the risk-based capital standard and directed OFHEO to adopt a financial regulation implementing the standard by December 1, 1994. The final regulations, however, were not issued until September 13, 2001. As specified by statute, the risk-based capital standard involves a 10-year stress period, during which severe credit and interest rate shocks occur simultaneously. The parameters of the stress test are specified in the law. The required level of risk-based capital is determined as the amount that allows the enterprises to remain solvent in every quarter of the 10-year stress period, plus an additional 30% for operations and management risk. However, as a result of innovations in handling financial risk, the risk-based standards have turned out to be less strict than the minimum standards.

Based on these three capital standards, Congress defined four classifications with respect to meeting them: (1) *adequately capitalized*, if both the risk-based and the minimum levels are met; (2) *undercapitalized*, if the minimum level is met, but not the risk-based; (3) *significantly undercapitalized*, if only the critical capital level is met; and (4) *critically undercapitalized*, if none of the levels is met by an enterprise.

## Enforcement Actions

The range of enforcement actions available to OFHEO is largely dependent upon the capital classifications. For the adequately capitalized category, there are no prescribed supervisory actions, but cease-and-desist orders may be issued for conduct which seriously threatens the enterprise's capital base. An enterprise in the undercapitalized classification must have a capital restoration plan approved by the office and may not make any capital distribution that could result in further slippages. If no plan is approved or an approved plan is not complied with, the office is authorized to reclassify the enterprise downward. For the significantly undercapitalized class, a capital restoration plan and any capital distributions must be approved. Additional limits may be imposed on growth, activities may be restricted, new capital may be required, and, should the restoration plan not be approved or followed, the office is authorized to appoint a conservator to take over operations. For a critically undercapitalized enterprise, the office shall appoint a

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<sup>17</sup> Congress arbitrarily set the capital standard for management and operations risk at 30%.

conservator unless there is a finding of adverse impact on financial markets and that such appointment is not in the public interest.

## Legislative Proposals

Four bills were introduced in the 108<sup>th</sup> Congress that aimed to strengthen OFHEO's current statutory framework: H.R. 2575, H.R. 2803, S. 1508, and S. 1656. In addition, the House Financial Services Committee released a manager's amendment in preparation for a markup originally scheduled for October 8, 2003, that was subsequently postponed. On March 26, 2004, Chairman Shelby of the Senate Banking Committee released a draft bill, which was amended and approved by the Banking Committee on April 1, 2004, after being adopted as an amendment in the nature of a substitute for S. 1508.

A side-by-side comparison of the major provisions of these bills and drafts can be found in Table 1 at the end of this report.<sup>18</sup> While the approaches to regulatory reform vary somewhat, all the legislative proposals address (1) reconstituting the GSE regulator, (2) funding, (3) mission approval, (4) capital standards and (5) enforcement authority. Each of these issues will be discussed in detail below.

### Reconstituting the GSE Regulator

All the bills propose to abolish OFHEO and replace it either with a new office located within the Department of the Treasury, or, in the case of S. 1508 (as passed by the Banking Committee) bill, with an independent agency to regulate the housing GSEs, including the FHLBs. S. 1508 (as introduced by Senators Hagel, Sununu, and Dole) would establish the Office of Federal Enterprise Supervision (OFES), an agency in Treasury with the same regulatory responsibilities for safety and soundness oversight as OFHEO. S. 1656 and the House Financial Services manager's amendment would do the same, except S. 1656 would name the new entity the Office of Federal Housing Enterprise Supervision (OFHES) and the manager's amendment would name it the Office of Housing Finance Supervision (OHFS). H.R. 2575 proposes to rename the Office of Thrift Supervision (OTS) as the Office of Housing Finance Supervision (OHFS) and transfer the authority to regulate the safety and soundness of the enterprises to this new office. In addition to OFHEO, H.R. 2803 would also abolish the Federal Housing Finance Board (FHFB), the independent regulator responsible for overseeing the Federal Home Loan Banks (FHLBs), and establishes the Office of Housing Finance Oversight (OFHO) in Treasury to succeed the authority of both OFHEO and FHFB.

Historically, changes in the regulatory environment for the enterprises have tended to reflect the evolving role of GSEs in housing policy. With the growing dominance of the enterprises in U.S. mortgage markets and the possible risks they pose to the financial system, there has been a growing consensus about the potential

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<sup>18</sup> S. 1508 as introduced is not included in the side-by-side, as all of its provisions were replaced by Chairman Shelby's draft bill, which was adopted during committee markup as an amendment in the nature of a substitute.

gains from reconstituting the safety and soundness regulator under the auspices of the Treasury. For example, if the office is established within Treasury, it can benefit from Treasury's financial expertise and prominence. This action not only can be seen as creating opportunities for coordination and sharing of expertise with OTS and the Office of the Comptroller of the Currency (OCC), the two other financial regulators under Treasury, but also help reinforce the importance of the regulator's mission for safety and soundness oversight.

Furthermore, it is a fundamental principle of financial regulation that the office be independent and at arm's length from the enterprises. In a 1997 report, GAO noted that a housing GSE regulator needs to have "the independence and prominence that would allow it to act independently of the influence of the housing GSEs, which are large and politically influential institutions. If a GSE had more political clout and prominence than its regulator, it would be that much more difficult for the regulator to implement corrective action."<sup>19</sup> Establishing the safety and soundness regulator in Treasury, allows the office to acquire the immediate level of government prominence that is thought necessary for overseeing the enterprises.

Although the benefits of reconstituting the GSE regulator within Treasury are well recognized, there remains considerable debate over how involved Treasury should be with the regulatory responsibilities of the new office. The Administration has clearly stated that it will only support proposals for reconstituting the GSE regulator within Treasury that require some degree of policy accountability to the Secretary of the Treasury.<sup>20</sup> Although H.R. 2803 would subject the director to the general oversight of the Secretary of the Treasury, H.R. 2575, the House Financial Services manager's amendment, S. 1508 (as introduced by Senators Hagel, Sununu, and Dole), and S. 1656 would all prohibit the Secretary of the Treasury from involvement in the authority of the director of the office.

If an agreement cannot be reached on this issue, other options such as establishing a new stand-alone agency, may be considered, as S. 1508 (as passed by the Banking Committee) proposes. On February 10, 2003, Comptroller General David Walker testified in favor of creating a single stand-alone regulator for all the housing GSEs.<sup>21</sup>

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<sup>19</sup> U.S. Government Accountability Office, *Government-Sponsored Enterprises: Advantages and Disadvantages of Creating a Single Housing GSE Regulator*, GAO/GGD-97-139, July 1997, p. 14.

<sup>20</sup> For more information on the Administration's recommendations for improving GSE oversight, see "The Administration's View" section of this report.

<sup>21</sup> Prepared testimony of David Walker, Comptroller General of the United States in U.S. Congress, Senate Committee on Banking, Housing and Urban Affairs, *Proposals to Improve the Regulatory Regime for Government Sponsored Enterprises*, hearings, 108<sup>th</sup> Congress, 2<sup>nd</sup> sess., Feb. 10, 2004, at [[http://www.banking.senate.gov/\\_files/walker.pdf](http://www.banking.senate.gov/_files/walker.pdf)], visited on Oct. 4, 2004.

## Funding

As previously discussed, OFHEO's assessments are subject to the annual congressional appropriations process. For many years now, OFHEO has argued that this process has hindered its ability to conduct effective long-term planning and precludes flexibility in resource management. For instance, during periods when the government has operated under a continuing resolution, OFHEO has been forced to cut back on its activities. The agency also claims it is unable to respond quickly to important regulatory concerns, such as Freddie Mac's restatement of income, without stretching thin its ability to conduct its primary safety and soundness oversight responsibilities. In testimony before the Senate Committee on Banking, Housing and Urban Affairs on July 17, 2003, the director of OFHEO noted that the "amount of resources needed to address the issues surrounding Freddie Mac's restatement is straining our resources."<sup>22</sup>

In light of these issues, OFHEO has recommended that the agency be permanently funded, and exempt from the appropriations process, like other financial regulators. OFHEO has said that permanent funding would permit the agency to adapt more easily to changes in the enterprises' activity and respond to problems in a timely manner. The office has asked for assessment language similar to that of the Federal Reserve, OTS, OCC and FHFB:

Amounts received by the Director from assessments under this section may be deposited in the manner provided in section 5234 of the Revised Statutes (12 U.S.C. 192) with respect to assessments by the Comptroller of the Currency. The amounts received by the Director from any assessment under this section shall not be construed to be Government or public funds or appropriated money. Notwithstanding any other provision of law, the amounts received by the Director from any assessment under this section shall not be subject to apportionment for the purpose of chapter 15 of title 31 or under any other authority."<sup>23</sup>

All the bills authorize the director of the new entity to collect annual assessments, exempt from the annual congressional appropriations process. However, H.R. 2575, H.R. 2803, S. 1508 (as introduced by Senators Hagel, Sununu, and Dole) and S. 1656 also retain the requirement that assessments be placed in a fund in the Treasury. The Constitution states that "No money shall be drawn from the Treasury, but in consequence of appropriations made by law..."<sup>24</sup> Thus, the bills retain the requirement for appropriations, but create a permanent appropriation. In

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<sup>22</sup> Prepared testimony of the Honorable Armando Falcon, Jr., Director of the Office of Federal Housing Enterprise Oversight, in U.S. Congress, Senate Committee on Banking, Housing and Urban Affairs, *Regulatory Oversight of Government Sponsored Enterprise Accounting Practices*, hearings, 108<sup>th</sup> Cong., 1<sup>st</sup> sess., July 17, 2003, at [<http://www.ofheo.gov/News.asp?FormMode=Release&ID=84>], visited on Oct. 4, 2004. OFHEO has also seen its requested funding cut by Congress in four of the past 10 years: 1997, 1998, 1999, and 2001.

<sup>23</sup> 12 U.S.C. § 1467. This is the assessments language found in the OTS statute.

<sup>24</sup> U.S. Const., Art. I § 9, cl. 7.

these cases, the appropriations committees can still cap or otherwise restrict the use of funds by an agency, which means that the offices established in these four bills are not removed from the appropriations process. The legislative language found in the House Financial Services manager's amendment is similar to what applies to other federal bank regulators and would completely remove the new regulator from the appropriations process. S. 1508 (as passed by the Banking Committee) similarly provides that the assessments collected by the new agency are not to be considered government funds or appropriated monies.

The bills employ different language as to what costs the assessments are authorized to cover. The House Financial Services manager's amendment, both Senate bills, and S. 1508 (as passed by the Banking Committee) state that the annual assessments shall cover "all reasonable costs and expenses of the Office," while H.R. 2803 and H.R. 2575 state that the assessments shall cover the costs of the director "with respect to regulation and supervision." However, it is not clear in the latter case whether, for example, janitorial staff would be covered under this provision. This could potentially expose the regulator to challenges by the enterprises regarding the appropriateness of the assessments.

Also, with the exception of the House Financial Services manager's amendment and S. 1508 (as passed by the Banking Committee), the bills do not address the regulator's funding requirements during a crisis. In general, regulators have found it important to maintain enough working capital to carry out elevated supervision in a crisis, above and beyond normal costs. For example, in the statute for OTS assessments, Congress authorized a working capital fund for emergency circumstances. It permits OTS to collect fees and assessments in excess of actual expenses to help maintain such a fund. As the four introduced bills are currently written, the safety and soundness regulator may find itself without sufficient funding in a time of crisis. The House Financial Services manager's amendment and S. 1508 (as passed by the Banking Committee) authorize the GSE regulator to maintain a working capital fund above and beyond the agency's immediate operating expenses.

## **Mission Approval**

In the current regulatory environment, HUD has the oversight responsibilities for the housing mission of the enterprises, including approval authority for any new program and enforcement of compliance with affordable housing goals. The decision to split the oversight functions of mission approval from safety and soundness represented the legislative compromise worked out over the potential conflicting interests that could arise between these two functions. For instance, if HUD had to take responsibility for protecting taxpayers from the risk of having to make good on GSE losses by requiring higher capital, then HUD could be in the position of simultaneously promoting housing credit and raising its cost. Alternatively, a separate and independent safety and soundness regulator could set up the possibility of the GSEs playing the regulators off against each other. For example, in order to avoid a mission change which might lower profitability — such as raising goals for specific forms or locations of housing credit — the enterprises might claim it to be unsafe and have the change overruled.

Despite the separation of these functions, Congress included a temporary provision in the Safety and Soundness Act that authorized OFHEO to consult with HUD in regard to the safety and soundness of any proposed new programs. This provision expired last year, but OFHEO and HUD continue to maintain open lines of communication in regards to new program approval. Nevertheless, there is a growing consensus that combining mission and safety and soundness regulation would not necessarily create conflict. For example, other financial regulators, such as the Federal Reserve, OTS, OCC, and the FDIC have been able to successfully oversee both mission compliance and the financial condition of banks and thrifts for years. In addition, the FHFB has combined the two with respect to the Federal Home Loan Banks.

H.R. 2803, S. 1508 (as introduced by Senators Hagel, Sununu, and Dole), and S. 1508 (as passed by the Banking Committee) would both transfer prior approval authority of new programs to the director from the HUD Secretary. Under S. 1656, new programs must be approved by the director, in consultation with the HUD Secretary. H.R. 2575 proposes to retain prior approval authority with the HUD Secretary, but expand the authority to all new “activities” rather than just new “programs.” It would also remove the current 45-day time limit that HUD must meet in order to avoid automatic approval of a proposed new program. The House Financial Services manager’s amendment retains prior approval authority with the HUD Secretary, as well as the 45-day time limit, but expands the Secretary’s authority to both new and ongoing programs. The HUD Secretary is also required to consult with the new safety and soundness regulator in regard to these programs. All the bills, however, would retain the HUD Secretary’s authority for affordable housing goals and/or fair housing responsibilities.

## Capital Standards

As previously discussed, Congress has set in statute the minimum capital level requirements for the enterprises, as well as the parameters of OFHEO’s risk-based capital model. OFHEO does not have the authority to enforce capital requirements based on alternative parameter assumptions or an increase in perceived risk due to unsafe or unsound practices. In an appearance before the House Financial Services Committee on February 11, 2003, Federal Reserve Board Chairman Alan Greenspan argued that a regulator must have strong control over capital requirements “because without it regulation, in my judgment, will be deficient.”<sup>25</sup>

H.R. 2575 and S. 1508 (as introduced by Senators Hagel, Sununu, and Dole) would give the director discretion to apply alternative interest rate scenarios to the risk-based capital model, including the assumptions regarding interest rates, home prices, and new business. S. 1508 (as introduced by Senators Hagel, Sununu, and Dole) also requires that the risk-based capital standard be similar to those used by federal banking regulators. Similarly, these bills authorize the director to increase the required minimum and critical capital levels for the enterprises by regulation or order.

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<sup>25</sup> Damian Paletta, “Greenspan: Give Regulator Control Over GSEs’ Capital,” *American Banker*, Feb. 12, 2004.

H.R. 2803 proposes that safety and soundness standards be prescribed by the director pursuant to Section 39 of the Federal Deposit Insurance Act, which provides the director broad powers in setting standards relating to issues, such as internal controls, interest rate exposure, and asset growth. It could also possibly be interpreted as providing the ability to set capital standards. The bill, however, offers no provision to amend the capital standard requirements currently set out in statute. Thus, current law's specific language pertaining to capital may obviate the bill's broader construction, preventing any changes to the current standards.

S. 1656 mandates that the director review the adequacy of current risk-based capital standards and, if necessary, make recommendations to Congress for changes in the statutory levels. The bill would also authorize the director to modify the capital level if the current level were determined to be inadequate to ensure safety and soundness.

The House Financial Services manager's amendment and S. 1508 (as passed by the Banking Committee) would delete the statutory capital levels in current law and authorize the director to establish risk-based capital requirements by regulation or order. The director would file periodic reports with Congress, describing the risk-based capital standard, the minimum and critical capital levels, and the methodology by which levels were set.

## **Enforcement Authority**

All the bills, except H.R. 2803, would authorize the director to reduce the capital classification of an enterprise by one level if the director determines in writing that an enterprise is engaging in conduct that could result in a rapid depletion of core capital or that the value of the property subject to mortgages held or securitized by the enterprise has decreased significantly. After notice and an opportunity for hearing, the director determines whether an enterprise is in an unsafe or unsound condition. These bills authorize the director to issue cease-and-desist orders to address unsafe or unsound conditions or practices with respect to the enterprises and their affiliates.<sup>26</sup> H.R. 2575, the House Financial Services manager's amendment, and S. 1508 (as passed by the Banking Committee) would also authorize the director to appoint a receiver to liquidate or wind up the affairs of a critically undercapitalized enterprise. Under S. 1508, however, the appointment of a receiver would not become effective unless Congress failed to pass a joint resolution of disapproval within 45 days.

In regard to these bills, there are two important issues that are worth noting. First, it is not clear from the legislative language what constitutes "a rapid depletion of core capital." This lack of clarity could prevent the regulator from responding quickly in order to prevent a financial crisis.

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<sup>26</sup> "Enterprise-affiliated parties" are defined in the bills as (1) directors, officers, or employees of a GSE, (2) shareholders, joint venture partners, or consultants, or (3) independent contractors who knowingly or recklessly violate law, breach fiduciary duty, or participate in an unsafe or unsound practice.

Second, the determination that an enterprise is in an unsafe or unsound condition depends on the potential for a depletion of capital. Thus, the enforcement powers hinge on the enterprises becoming undercapitalized. However, there are circumstances upon which an enterprise can be considered adequately capitalized, yet conducting unsafe or unsound practices. In this regard, H.R. 2803 would allow for the same broad enforcement authority as federal bank regulators that does not depend on the capitalization of the enterprises.

## The Administration's View

Treasury Secretary John Snow appeared before the House Financial Services Committee on September 10, 2003, and then again before the Senate Banking Committee on October 16, 2003, to outline the Administration's recommendations for improving GSE oversight. In his October 16<sup>th</sup> testimony, the Treasury Secretary emphasized that these recommendations are not "a wish list of reforms that we would like to see enacted...[but rather]...the minimum elements that are needed in a credible regulatory structure, a structure that can ensure that our housing finance system remains a strong and vibrant source of funding for expanding homeownership opportunities in America."<sup>27</sup> These same recommendations are outlined in the President's budget proposal for FY2005.<sup>28</sup>

First, given that the present GSE structure "is ill-equipped to deal effectively with the current size, complexity, and importance of Fannie Mae, Freddie Mac, and the Federal Home Loan Banks,"<sup>29</sup> the Administration recommends the creation of a new agency to oversee the safety and soundness of all the housing GSEs.

Although Treasury Secretary Snow testified last year that the Administration was not specifically requesting that the new agency be made a bureau of the Treasury Department, he noted that it would support such a proposal as long as "the new agency were established with adequate elements of policy accountability to the Secretary of the Treasury."<sup>30</sup> The President's budget proposal, however, specifically advocates that the new agency be placed within the Department of the Treasury. The Administration views the direct involvement of the Treasury Department in providing policy guidance to the new regulatory agency as essential to reduce the risk of regulatory capture and to ensure that the new regulator's policies are not reinforcing the market misperception of an implied guarantee. According to the Treasury Secretary's testimony last year, the Administration requires, at a minimum, that the new agency clear any new regulations and policy statements to the Congress

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<sup>27</sup> Prepared testimony of John W. Snow, Secretary of the Treasury, in U.S. Congress, Senate Committee on Banking, Housing and Urban Affairs, *Proposals for Improving the Regulation of the Housing GSEs*, hearings, 108<sup>th</sup> Cong., 1<sup>st</sup> sess., Oct. 16, 2003, p. 2, at [[http://www.banking.senate.gov/\\_files/ACFB2.pdf](http://www.banking.senate.gov/_files/ACFB2.pdf)], visited on Oct. 4, 2004.

<sup>28</sup> Office of Management and Budget, *Budget of the United States Government, Fiscal Year 2005, Analytical Perspectives*, pp. 81-85.

<sup>29</sup> Prepared testimony of Treasury Secretary John W. Snow, p. 2.

<sup>30</sup> Prepared testimony of Treasury Secretary John W. Snow, p. 3.



through the Treasury Department, and that the Treasury Department have review authority over the new agency's budget.

Second, in order to strengthen the new agency's general regulatory, supervisory and enforcement powers, the Administration also recommends the following:

- funding the agency by assessments on its regulated entities that are not subject to the congressional appropriations process;
- transferring the authority for approving new activities of the housing GSEs from HUD to the new regulator;
- providing the agency the authority to direct, if necessary, the liquidation of an enterprise's assets; and
- giving the agency broad authority to set both minimum and risk-based capital standards.

Finally, on a separate note, the Administration also encourages Congress to consider eliminating the statutory requirement for the President to appoint five members of the enterprises' board of directors. Currently, the GSEs' board of directors shall have eighteen members, five of whom are appointed annually by the President, and the remaining thirteen are elected annually by the common stockholders. The Administration's proposal would require that all eighteen board members be elected by the shareholders for a one-year term.

On April 2, 2004, the Secretaries of the Treasury and HUD released a statement of opposition to S. 1508 as reported by the Senate Banking Committee. The statement referred to an amendment adopted in markup which allows Congress to overrule the GSE regulator's decision to appoint a receiver, and characterized this amendment as significantly weakening "a core power needed for a strong regulator," likely to "reinforce the false impression" that the GSEs have a government guarantee.<sup>31</sup> (Under S. 1508 as reported, Congress has 45 days after the appointment of a receiver to pass a joint resolution of disapproval.)

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<sup>31</sup> U.S. Department of the Treasury, Office of Public Affairs, *Joint Statement of Treasury Secretary John Snow and Housing and Urban Development Secretary Alphonso Jackson*, JS-1294, April 2, 2004, at [<http://www.ustreas.gov/press/releases/js1294.html>], visited on Oct. 4, 2004.

**Table 1. Side-By-Side Comparison of GSE Regulation Proposals**

<b>Provision</b>	<b>S. 1508 (as passed by the Banking Committee)</b>	<b>House Fin. Serv. Manager's Amendment</b>	<b>H.R. 2575</b>	<b>H.R. 2803</b>	<b>S. 1656</b>
Short title	Federal Housing Enterprise Regulatory Reform Act of 2004	Secondary Mortgage Market Enterprises Regulatory Improvement Act	Secondary Mortgage Market Enterprises Regulatory Improvement Act	Housing Finance Regulatory Restructuring Act of 2003	Federal Housing Enterprise Oversight Modernization Act of 2003
New regulatory entity to replace OFHEO	Federal Housing Enterprise Supervisory Agency (FHESA)	Office of Housing Finance Supervision (OHFS)	Office of Housing Finance Supervision (OHFS)	Office of Housing Finance Oversight (OHFO)	Office of Federal Housing Enterprise Supervision (OFHES)
Composition and location of new agency	Independent federal agency, to assume functions of OFHEO and Federal Housing Finance Board (FHFB). (Sec. 101)	An office in the Department of the Treasury. (Sec. 101)	Office of Thrift Supervision (OTS) in the Department of the Treasury to be renamed as OHFS and to assume most of OFHEO's functions. (Sec. 101)	Merges OFHEO and Federal Housing Finance Board (FHFB — currently overseer of the Federal Home Loan banks) into OHFO, a bureau in the Department of the Treasury. (Sec. 101)	An office in the Department of the Treasury, not to be merged or consolidated with any other branch of the Treasury. (Sec. 101)

Provision	S. 1508 (as passed by the Banking Committee)	House Fin. Serv. Manager's Amendment	H.R. 2575	H.R. 2803	S. 1656
Governance of new agency	<p>Director appointed by the President, with advice and consent of the Senate, to a six-year term. Three deputy directors to be appointed by director, to oversee (1) the housing GSEs, (2) the FHLBs, and (3) the housing mission and goals. (Sec. 101)</p> <p>Creates a Federal Housing Enterprise Board, with no executive powers, to advise the director. Board members include secretaries of Treasury, HUD, chairman of the SEC, and the FHESA director. (Sec. 103)</p>	Director appointed by the President, with advice and consent of the Senate, to a five-year term. Deputy director to be appointed by director, with such duties and powers as the director may assign. (Sec. 101)	Director of OTS will become director of OHFS. (Sec. 102)	Director appointed by President, with advice and consent of the Senate, to a five-year term. Two deputy directors: 1) for Safety and Soundness (to exercise OFHEO's and FHFB's authority) and 2) for Housing Enterprise Charter Compliance (to exercise authority currently vested in the Secretary of HUD). (Sec. 101)	Director appointed by the President, with advice and consent of the Senate, to a five-year term. OFHEO director to serve as director of OFHES for at least one year. (Sec. 101)

Provision	S. 1508 (as passed by the Banking Committee)	House Fin. Serv. Manager's Amendment	H.R. 2575	H.R. 2803	S. 1656
Qualifications of director	U.S. citizen with knowledge of financial management or oversight and capital markets, including mortgage securities and housing markets. May not be employed by, or have a financial interest in a GSE, or have served as a GSE director or executive for the past three years. (Sec. 101)	U.S. citizen neither employed by nor having a financial interest in a housing GSE, with a demonstrated understanding of housing finance. (Sec. 101)	No financial interest in a housing GSE (in addition to qualifications for head of OTS). (Sec. 102)	No financial interest in a housing GSE or a Federal Home Loan Bank (FHLB), U.S. citizenship. (Sec. 101)	U.S. citizen neither employed by nor having a financial interest in a housing GSE. (Sec. 101)

Provision	S. 1508 (as passed by the Banking Committee)	House Fin. Serv. Manager's Amendment	H.R. 2575	H.R. 2803	S. 1656
Duties and authorities of director	<p>To oversee prudential operations of GSEs, to ensure that GSEs maintain adequate capital and internal controls, to see that GSEs foster liquid, efficient, and competitive housing markets, to ensure that GSEs comply with the authorizing statutes and that they engage only in activities consistent with those statutes, and to meet at least twice a year with GSEs' external auditors. With respect to the FHLBs, to ensure that they provide funds to community financial institutions to support small businesses and farms and accept as collateral whole interests in such loans.</p> <p>(Sec. 102)</p>	<p>To oversee GSEs and ensure that they operate in a safe and sound manner (including maintenance of adequate capital and internal controls), foster liquid and competitive mortgage markets, comply with applicable laws, rules, and regulations, and carry out their missions only through activities authorized by their charters and consistent with the public interest.</p> <p>(Sec. 102)</p>	<p>To ensure that GSEs operate in a financially safe and sound manner, carry out their missions only through authorized activities, and remain adequately capitalized, and to exercise general supervisory and regulatory authority.</p> <p>(Sec. 103)</p>	<p>To prescribe regulations necessary to carry out the act and functions assigned to the director.</p> <p>(Sec. 101)</p> <p>In addition to any other authority of the director, to prescribe safety and soundness standards pursuant to Section 39 of the Federal Deposit Insurance Act. These standards are to have the same force and effect with regard to GSEs as federal bank regulators' standards have with regard to federally insured depository institutions.</p> <p>(Sec. 102)</p>	<p>To ensure that GSEs operate in a financially safe and sound manner, carry out their missions only through authorized activities, and remain adequately capitalized, and to exercise general supervisory authority.</p> <p>(Sec. 102)</p>

<b>Provision</b>	<b>S. 1508 (as passed by the Banking Committee)</b>	<b>House Fin. Serv. Manager's Amendment</b>	<b>H.R. 2575</b>	<b>H.R. 2803</b>	<b>S. 1656</b>
Authority to delegate	Yes. (Sec. 102)	Yes. (Sec. 102)	Yes. (Sec. 103)	Yes, but director may not let FHLBs take on examination duties.  (Sec. 101)	Yes. (Sec. 102)
Authority to hire examiners and accountants through a streamlined process	Yes: examiners, accountants and economists may be hired directly, in accordance with the excepted service procedures. (Sec. 105)	Yes, for three years following enactment. Director must report to Congress within 90 days on changes in the hiring process, results, etc. (Sec. 104)	Yes, and director must report to Congress within 90 days on changes in the hiring process, results, etc. (Sec. 104)	No provision.	Yes, for three years after enactment. Director must report to Congress annually on changes in the hiring process, results, etc. (Sec. 103)

Provision	S. 1508 (as passed by the Banking Committee)	House Fin. Serv. Manager's Amendment	H.R. 2575	H.R. 2803	S. 1656
Source of agency funding	<p>Director to establish and collect annual assessments from GSEs, not to exceed reasonable costs of regulation, including examinations, credit reviews, and enforcement. Amounts collected are not to be construed to be government or public funds or appropriated money. (Sec. 106)</p> <p>Assessments may include an amount in excess of actual expenses, as deemed necessary by the Director, to maintain a working capital fund. Collections in excess of the amount the Director deems necessary to maintain the working capital fund shall be remitted annually to GSEs. (Sec. 106)</p>	<p>Director to establish and collect annual assessments from GSEs, not to exceed reasonable costs of regulation, including examinations, credit reviews, and enforcement. Amounts collected are not to be construed to be government or public funds or appropriated money. (Sec. 106)</p> <p>Assessments may include an amount in excess of actual expenses, as deemed necessary by the Director, to maintain a working capital fund. Collections in excess of the amount the Director deems necessary to maintain the working capital fund shall be remitted annually to GSEs. (Sec. 106)</p>	<p>Agency to determine amount of and collect annual assessments from GSEs, not exceeding reasonable costs of regulation, including examinations and credit reviews. Secretary of HUD to levy similar assessment to cover HUD's GSE-related regulatory functions. Amounts collected to be placed in a fund in Treasury with separate accounts for director and HUD, to be available without fiscal year restrictions. Retains requirement for appropriations, but creates a permanent appropriation. (Sec. 106)</p>	<p>Annual assessments to be collected from GSEs and FHLBs. Secretary of HUD to levy similar assessment. Amounts collected to be placed in the Federal Housing Enterprise Oversight Fund in Treasury, to be available without fiscal year restrictions. Retains requirement for appropriations, but creates a permanent appropriation. (Sec. 101)</p>	<p>Director to establish and collect annual assessments from GSEs, not to exceed reasonable costs of regulation, including examinations and credit reviews. Assessments to be deposited in a fund in the Treasury for the director's use without fiscal year limitation. Creates a permanent appropriation. (Sec. 105)</p>

Provision	S. 1508 (as passed by the Banking Committee)	House Fin. Serv. Manager's Amendment	H.R. 2575	H.R. 2803	S. 1656
Financial operating plan and forecasts	No provision.	The Secretary of HUD will submit plans and forecasts to OMB before each fiscal year regarding HUD's GSE oversight activities. (Sec. 121)	Director to submit plans and forecasts to OMB before each fiscal year, and reports on operations as soon as practicable after the ending of the fiscal year and each quarter thereof. The Secretary of HUD will submit similar plans and reports to the director. (Sec. 106)	Director to submit plans and forecasts to OMB and Treasury before each fiscal year, and reports on operations as soon as practicable after the ending of fiscal years and quarters thereof. The Secretary of HUD will submit similar plans and reports to the director. (Sec. 101)	Director to submit plans and forecasts to OMB before each fiscal year, and reports on operations as soon as practicable after the ending of fiscal years and quarters thereof. (Sec. 105)



Provision	S. 1508 (as passed by the Banking Committee)	House Fin. Serv. Manager's Amendment	H.R. 2575	H.R. 2803	S. 1656
Housing goals	<p>HUD authority transferred to FHESA, except for fair housing responsibilities. (Sec. 125)</p> <p>Director shall establish an annual goal for home purchases by low-income, first-time buyers who are good credit risks but can't cover a down payment or closing costs. (Sec. 127)</p> <p>Provides for improved provision of mortgage credit to low-income families and underserved markets. (Title IV)</p>	<p>HUD Secretary retains authority to establish and enforce housing goals. Establishes a HUD Office of GSE Mission Oversight. (Sec. 121) HUD Secretary to prepare an annual housing report on GSEs and housing goals. (Sec. 123)</p>	<p>HUD Secretary retains authority to enforce housing goals. (Sec. 107)</p>	<p>HUD Secretary retains authority to enforce housing goals. (Sec. 103)</p>	<p>HUD Secretary retains authority to enforce housing goals. (Sec. 102)</p>

<b>Provision</b>	<b>S. 1508 (as passed by the Banking Committee)</b>	<b>House Fin. Serv. Manager's Amendment</b>	<b>H.R. 2575</b>	<b>H.R. 2803</b>	<b>S. 1656</b>
Prior approval authority for new GSE programs and/or activities	Director approval needed for new programs. New programs must not be in conflict with the statutes or with the public interest. (Sec. 122)	Secretary of HUD's prior approval authority retained, but consideration of new and ongoing programs to include consultation with the Director. New and ongoing GSE programs must be consistent with their charters, not unsafe or unsound, and in the public interest. (Sec. 122)	Secretary of HUD's approval authority retained — new activities may be approved only if they are authorized by GSE charters, can be conducted in a safe and sound manner, and are in the public interest. (Sec. 108)	GSE charter compliance authority transferred from Secretary of HUD to Director. (Sec. 103)	New programs must be approved by the Director, in consultation with the Secretary of HUD. New programs shall be approved unless they are found to be inconsistent with safety and soundness or not authorized by GSE charters. (Sec. 102)
Limits on non-mission related assets	No provision.	No provision.	Secretary of HUD shall by regulation limit the amount of such assets a GSE may hold at any time. (Sec. 109)	No provision.	On a quarterly basis, Director shall review and provide written comment to GSEs on the appropriateness and quality of nonmortgage-related assets held in and outside the GSE's liquidity portfolio. (Sec. 107)
Conforming loan limits	No provision.	No provision.	Loan limits to be raised or lowered each year according to a housing cost index maintained by the Director. (Sec. 110)	No provision.	No provision.

<b>Provision</b>	<b>S. 1508 (as passed by the Banking Committee)</b>	<b>House Fin. Serv. Manager's Amendment</b>	<b>H.R. 2575</b>	<b>H.R. 2803</b>	<b>S. 1656</b>
Public disclosure of information	<p>Regulated entities must register at least one class of capital stock with the SEC, and maintain such registration under the Securities Exchange Act of 1934. Enterprises must comply with SEC proxy and insider transaction rules. (Sec. 108)</p> <p>Enterprises must also disclose on a quarterly basis the fair value of shareholders' equity. (Sec. 109)</p>	Director shall require each GSE to obtain and disclose an annual credit rating, and to publicly disclose interest rate and credit risk. (Sec. 110)	Director shall require GSEs to release financial, business, and other information that would be in the public interest. (Sec. 111)	No provision.	GSEs must register their stock with the SEC and make public disclosures regarding interest rate and credit risks and their credit rating. (Sec. 112)
Reviews of GSE creditworthiness	Director shall require each GSE to obtain and disclose an annual credit rating. (Sec 108)	Director shall require each GSE to obtain and disclose an annual credit rating. (Sec 110)	Each GSE must be rated biennially by two SEC-recognized credit rating organizations (Sec. 112)	No provision.	Each GSE must be rated biennially by two SEC-recognized credit rating organizations (Sec. 109)

Provision	S. 1508 (as passed by the Banking Committee)	House Fin. Serv. Manager's Amendment	H.R. 2575	H.R. 2803	S. 1656
Risk-based capital tests	<p>Director shall establish by regulation or order risk-based capital requirements to ensure safe and sound operation and the maintenance of sufficient capital and reserves to support risks that arise. (Sec. 108)</p> <p>FHESA shall report quarterly on the levels of required capital and the methods by which the levels are calculated. (Sec. 161)</p>	<p>Director shall establish by regulation or order risk-based capital requirements to ensure safety and soundness. (Sec. 109)</p> <p>Director shall report to Congress annually on risk-based capital requirements and tests. (Sec. 161)</p>	Director may specify the assumptions about interest rates, home prices, and new business that are to be used by GSEs in calculating capital requirements. (Sec. 113)	No provision.	Director to review the adequacy of risk-based standards and, if needed, recommend that Congress make changes in the statutory standards to better align capital with risk and reflect evolving best practices in large financial institutions. Director may also modify the current risk-based capital level if the level is inadequate to ensure safety and soundness. (Sec. 110)
Requirements to enhance capital strength, disclosure, and market discipline	Regulated entities must register at least 1 class of capital stock with the SEC, and make disclosures under the Securities Exchange Act of 1934. (Sec. 108)	Director shall require GSEs to issue subordinated debt, maintain appropriate levels of liquidity, obtain and disclose an annual credit rating, and make public disclosures regarding interest rate and credit risk. (Sec. 110)	Director shall require GSEs to issue subordinated debt, maintain appropriate levels of liquidity, obtain and disclose an annual credit rating, and make public disclosures regarding interest rate and credit risk. (Sec. 115)	No provision.	GSEs must register their stock with the SEC and make public disclosures regarding interest rate and credit risks and their credit rating. (Sec. 112)

<b>Provision</b>	<b>S. 1508 (as passed by the Banking Committee)</b>	<b>House Fin. Serv. Manager's Amendment</b>	<b>H.R. 2575</b>	<b>H.R. 2803</b>	<b>S. 1656</b>
Minimum and critical capital levels	To be set by the director, and may be raised above minimum levels if director determines that the benefits outweigh adverse effects on the housing mission. (Sec. 108)	No provision.	May be adjusted (but not set below statutory minimums) by director. (Sec. 114)	No provision.	Director authorized to issue regulations to ensure compliance with minimum and critical capital levels. (Sec. 111)
Capital classifications	Director may reclassify a GSE whose conduct could rapidly deplete core capital, or has caused a significant loss to asset values, or which is determined (after notice and opportunity for a hearing) to be in an unsafe or unsound condition. (Sec. 141)	Director may reclassify a GSE whose core capital is rapidly being depleted, or which (after notice and opportunity for a hearing) is determined to be in an unsafe or unsound condition, or engaging in an unsafe or unsound practice. (Sec. 141)	Director may reclassify a GSE whose core capital is rapidly being depleted, which (by the director's written finding, after notice and opportunity for a hearing) is in an unsafe or unsound condition, or engaging in an unsafe or unsound practice. (Sec. 131)	No provision.	Director may reclassify a GSE whose core capital is rapidly being depleted, which (by the director's written finding, after notice and opportunity for a hearing) is in an unsafe or unsound condition, or engaging in an unsafe or unsound practice. (Sec. 131)

Provision	S. 1508 (as passed by the Banking Committee)	House Fin. Serv. Manager's Amendment	H.R. 2575	H.R. 2803	S. 1656
Supervisory actions applicable to undercapitalized GSEs	Director must monitor GSE's condition, compliance with its capital restoration plan, and the efficacy of the plan. No growth in total assets is permitted for an undercapitalized GSE, unless the director has accepted the GSE's capital restoration plan, an increase in assets is consistent with the plan, and the ratio of tangible equity to assets is increasing. No new activities or acquisitions permitted without the Director's prior approval. Actions that may be taken under current law with regard to significantly undercapitalized GSEs may be taken with regard to undercapitalized GSEs. (Sec. 142)	Director must monitor GSE's condition, compliance with its capital restoration plan, and the efficacy of the plan. No growth in total assets is permitted for an undercapitalized GSE, unless the director has accepted the GSE's capital restoration plan, an increase in assets is consistent with the plan, and the ratio of tangible equity to assets is increasing. No new products may be issued, or acquisitions made, without the Director's prior approval. Actions that may be taken under current law with regard to significantly undercapitalized GSEs may be taken with regard to undercapitalized GSEs. (Sec. 142)	Director must monitor GSE's condition, compliance with its capital restoration plan, and the efficacy of the plan. No growth in total assets is permitted for an undercapitalized GSE, unless the director has accepted the GSE's capital restoration plan, an increase in assets is consistent with the plan, and the ratio of tangible equity to assets is increasing. No new products may be issued, or acquisitions made, without the Director's prior approval. Actions that may be taken under current law with regard to significantly undercapitalized GSEs may be taken with regard to undercapitalized GSEs. (Sec. 132)	No provision.	Director must monitor GSE's condition, compliance with its capital restoration plan, and the efficacy of the plan. No growth in total assets is permitted for an undercapitalized GSE, unless the director has accepted the GSE's capital restoration plan, an increase in assets is consistent with the plan, and the ratio of tangible equity to assets is increasing. No new products may be issued, or acquisitions made, without the Director's prior approval. Actions that may be taken under current law with regard to significantly undercapitalized GSEs may be taken with regard to undercapitalized GSEs. (Sec. 132)

Provision	S. 1508 (as passed by the Banking Committee)	House Fin. Serv. Manager's Amendment	H.R. 2575	H.R. 2803	S. 1656
Supervisory actions applicable to significantly undercapitalized GSEs	Supervisory actions that regulator <i>may</i> take under current law <i>must</i> be taken, including one or more of the following: new election of directors, dismissal of directors and/or executives, and hiring of qualified executive officers. Without written approval of director, executives of a significantly undercapitalized GSE may not receive bonuses or pay raises. (Sec. 143)	Supervisory actions that regulator <i>may</i> take under current law <i>must</i> be taken, including one or more of the following: new election of directors, dismissal of directors and/or executives, and hiring of qualified executive officers. Without written approval of director, executives of a significantly undercapitalized GSE may not receive bonuses or pay raises. (Sec. 143)	Supervisory actions that regulator <i>may</i> take under current law <i>must</i> be taken, including one or more of the following: new election of directors, dismissal of directors and/or executives, and hiring of qualified executive officers. Without written approval of director, executives of a significantly undercapitalized GSE may not receive bonuses or pay raises. (Sec. 133)	No provision.	Supervisory actions that regulator <i>may</i> take under current law <i>must</i> be taken, including one or more of the following: new election of directors, dismissal of directors and/or executives, and hiring of qualified executive officers. Without written approval of director, executives of a significantly undercapitalized GSE may not receive bonuses or pay raises. (Sec. 133)

Provision	S. 1508 (as passed by the Banking Committee)	House Fin. Serv. Manager's Amendment	H.R. 2575	H.R. 2803	S. 1656
Supervisory actions applicable to critically undercapitalized GSEs (liquidation authority)	Director may appoint (or FHESA serve as) a receiver or conservator for several causes related to financial difficulty or violation of law or regulation. Director may also appoint a limited-life enterprise to deal with the affairs of a GSE in default. Congress may overrule the appointment of a receiver by passing a joint resolution of disapproval within 45 days. (Sec. 144)	The director may appoint an enhanced conservator to liquidate a critically undercapitalized GSE and wind up its affairs, in accordance with such regulations as the Director may issue. (Sec. 144)	After written notice to Congress, the director may appoint a receiver to liquidate a critically undercapitalized GSE and wind up its affairs. (Sec. 134)	No provision.	No provision.
Restriction on capital distributions	With certain exceptions, a GSE may not make a capital distribution that would cause it to become undercapitalized. (Sec. 141)	With certain exceptions, a GSE may not make a capital distribution that would cause it to become undercapitalized. (Sec. 141)	With certain exceptions, a GSE may not make a capital distribution that would cause it to become undercapitalized. (Sec. 131)	No provision.	With certain exceptions, a GSE may not make a capital distribution that would cause it to become undercapitalized. (Sec. 131)



Provision	S. 1508 (as passed by the Banking Committee)	House Fin. Serv. Manager's Amendment	H.R. 2575	H.R. 2803	S. 1656
Enforcement authority (cease- and-desist orders)	<p>Director may issue cease-and-desist orders for unsafe or unsound practices, or for an unsatisfactory rating. (Sec. 151)</p> <p>Temporary cease-and-desist orders may be issued if GSE actions are likely to weaken its financial condition prior to the conclusion of a cease-and-desist proceeding. (Sec. 152)</p>	<p>Director may issue cease-and-desist orders for unsafe and unsound practices or violations of law. A less-than-satisfactory examination rating may be deemed an unsafe and unsound practice. Director may not enforce compliance with housing goals. (Sec. 151)</p>	<p>Director may issue cease-and-desist orders for unsafe and unsound practices or violations of law. A less-than-satisfactory examination rating may be deemed an unsafe and unsound practice. (Sec. 151)</p>	<p>Director may issue cease-and-desist orders, including orders to take affirmative actions, to the same extent and under the same procedures and conditions as federal bank regulators with respect to insured depository institutions. (Sec. 101)</p>	<p>Director may issue cease-and-desist orders for unsafe and unsound practices or violations of law. A less-than-satisfactory examination rating may be deemed an unsafe and unsound practice. (Sec. 151)</p>

Provision	S. 1508 (as passed by the Banking Committee)	House Fin. Serv. Manager's Amendment	H.R. 2575	H.R. 2803	S. 1656
Enforcement authority (temporary cease-and-desist proceedings)	Temporary cease-and-desist orders may be issued if GSE actions are likely to weaken its financial condition prior to the conclusion of a cease-and-desist proceeding. (Sec. 152)	If an unsound or unsafe practice appears likely to cause insolvency or significant dissipation of assets or earnings, director may issue temporary cease-and-desist orders, including orders to take affirmative action to remedy the unsafe and unsound practice. Director may seek an injunction in federal court to enforce a cease-and-desist order. (Sec. 152)	If an unsound or unsafe practice appears likely to cause insolvency or significant dissipation of assets or earnings, director may issue temporary cease-and-desist orders, including orders to take affirmative action to remedy the unsafe and unsound practice. Director may seek an injunction in federal court to enforce a cease-and-desist order. (Sec. 152)	Director may issue temporary cease-and-desist orders, including orders to take affirmative action, to the same extent and under the same procedures and conditions as federal bank regulators with respect to insured depository institutions. (Sec. 101)	If an unsound or unsafe practice appears likely to cause insolvency or significant dissipation of assets or earnings, director may issue temporary cease-and-desist orders, including orders to take affirmative action to remedy the unsafe and unsound practice. Director may seek an injunction in federal court to enforce a cease-and-desist order. (Sec. 152)

Provision	S. 1508 (as passed by the Banking Committee)	House Fin. Serv. Manager's Amendment	H.R. 2575	H.R. 2803	S. 1656
Removal and prohibition authority	After written notice and opportunity for a hearing, the director may suspend or remove "enterprise-affiliated parties" (defined below) who have 1) violated a law or a cease-and-desist or other written order, 2) engaged in an unsafe or unsound practice, or 3) breached fiduciary duty, such that 1) the GSE is likely to suffer loss or the enterprise affiliated party gain, and 2) the unsafe or unsound practice demonstrates continuing disregard for the safety and soundness of the GSE. Also provides for industry-wide suspensions under certain circumstances. (Sec. 153)	After written notice and opportunity for a hearing, the director may suspend or remove "enterprise-affiliated parties" (defined below) who have 1) violated a law or a cease-and-desist or other written order, 2) engaged in an unsafe or unsound practice, or 3) breached fiduciary duty, such that 1) the GSE is likely to suffer loss or the party gain, and 2) the unsafe or unsound practice demonstrates continuing disregard for the safety and soundness of the GSE. (Sec. 153)	After written notice and opportunity for a hearing, the director may suspend or remove "enterprise-affiliated parties" (defined below) who have 1) violated a law or a cease-and-desist or other written order, 2) engaged in an unsafe or unsound practice, or 3) breached fiduciary duty, such that 1) the GSE is likely to suffer loss or the party gain, and 2) the unsafe or unsound practice demonstrates continuing disregard for the safety and soundness of the GSE. (Sec. 153)	Director may issue suspension and removal orders to the same extent and under the same procedures and conditions as federal bank regulators with respect to insured depository institutions. (Sec. 101)	After written notice and opportunity for a hearing, the director may suspend or remove "enterprise-affiliated parties" (defined below) who have 1) violated a law or a cease-and-desist or other written order, 2) engaged in an unsafe or unsound practice, or 3) breached fiduciary duty, such that 1) the GSE is likely to suffer loss or the party gain, and 2) the unsafe or unsound practice demonstrates personal dishonesty or continuing disregard for the safety and soundness of the GSE. (Sec. 153)

Provision	S. 1508 (as passed by the Banking Committee)	House Fin. Serv. Manager's Amendment	H.R. 2575	H.R. 2803	S. 1656
Who (besides the GSEs and their officers and employees) is subject to cease-and-desist orders or removal and suspension authority?	“Enterprise-affiliated parties” are defined as 1) directors, officers, or employees of a GSE, 2) shareholders, joint venture partners, or consultants, 3) independent contractors who knowingly or recklessly violate law, breach fiduciary duty, or participate in an unsafe or unsound practice (where such actions are likely to cause significant losses in the GSE, or (4) non-profits that receive their principal funding on an ongoing basis from a GSE. (Sec. 2)	“Enterprise-affiliated parties” are defined as 1) directors, officers, or employees of a GSE, 2) shareholders, joint venture partners, or consultants, or 3) independent contractors who knowingly or recklessly violate law, breach fiduciary duty, or participate in an unsafe or unsound practice. (Sec. 111)	“Enterprise-affiliated parties” are defined as 1) directors, officers, or employees of a GSE, 2) shareholders, joint venture partners, or consultants, or 3) independent contractors who knowingly or recklessly violate law, breach fiduciary duty, or participate in an unsafe or unsound practice. (Sec. 116)	No provision.	“Enterprise-affiliated parties” are defined as 1) directors, officers, or employees of a GSE, 2) shareholders, joint venture partners, or consultants, or 3) independent contractors who knowingly or recklessly violate law, breach fiduciary duty, or participate in an unsafe or unsound practice. (Sec. 114)

<b>Provision</b>	<b>S. 1508 (as passed by the Banking Committee)</b>	<b>House Fin. Serv. Manager's Amendment</b>	<b>H.R. 2575</b>	<b>H.R. 2803</b>	<b>S. 1656</b>
Civil money penalties	Three tiers of fines: 1) \$10,000 per day for violations of orders, etc., 2) \$50,000 per day for a pattern of misconduct or breach of fiduciary duty with financial gain to the individual, and 3) up to a maximum of \$2 million for knowingly engaging in violations, breaches of fiduciary duties, or unsafe or unsound practices that cause substantial losses to a GSE. (Sec. 155)	Three tiers of fines: 1) \$10,000 per day for violations of orders, etc., 2) \$50,000 per day for a pattern of misconduct or breach of fiduciary duty with financial gain to the individual, and 3) up to a maximum of \$2 million for knowingly engaging in violations, breaches of fiduciary duties, or unsafe or unsound practices that cause substantial losses to a GSE. (Sec. 155)	Three tiers of fines: 1) \$10,000 per day for violations of orders, etc., 2) \$50,000 per day for a pattern of misconduct or breach of fiduciary duty with financial gain to the individual, and 3) up to a maximum of \$2 million for knowingly engaging in violations, breaches of fiduciary duties, or unsafe or unsound practices that cause substantial losses to a GSE. (Sec. 155)	Director may impose civil fines to the same extent and under the same procedures and conditions as federal bank regulators with respect to insured depository institutions. (Sec. 101)	Three tiers of fines: 1) \$10,000 per day for violations of orders, etc., 2) \$50,000 per day for a pattern of misconduct or breach of fiduciary duty with financial gain to the individual, and 3) up to a maximum of \$2 million for knowingly engaging in violations, breaches of fiduciary duties, or unsafe or unsound practices that cause substantial losses to a GSE. (Sec. 155)
Criminal penalties	Anyone who participates directly or indirectly in the affairs of a GSE while under suspension or order of removal shall be liable for a fine of up to \$1 million, or five years imprisonment. (Sec. 156)	Anyone who participates directly or indirectly in the affairs of a GSE while under suspension or order of removal shall be liable for a fine of up to \$1 million, or five years imprisonment. (Sec. 156)	Anyone who participates directly or indirectly in the affairs of a GSE while under suspension or order of removal shall be liable for a fine of up to \$1 million, or five years imprisonment. (Sec. 156)	No provision.	Anyone who participates directly or indirectly in the affairs of a GSE while under suspension or order of removal shall be liable for a fine of up to \$1 million, or five years imprisonment. (Sec. 156)

<b>Provision</b>	<b>S. 1508 (as passed by the Banking Committee)</b>	<b>House Fin. Serv. Manager's Amendment</b>	<b>H.R. 2575</b>	<b>H.R. 2803</b>	<b>S. 1656</b>
Federal Financial Institutions Examination Council (FFIEC)	No provision.	No provision.	No provision.	Director to become member of FFIEC. (Sec. 106)	Director to become member of FFIEC. (Sec. 102)
GSE directors	Strikes provision in current law under which 5 members of GSE boards of directors are appointed by the President. (Sec. 172)	Strikes provision in current law by which 5 members of GSE boards of directors are appointed by the President. (Sec. 171)	No provision.	No provision.	No provision.
Federal Home Loan Banks	FHLBs come under the regulation of FHESA, which assumes the duties of the Federal Housing Finance Board (FHFB). (Sec. 203)  Creates a Federal Home Loan Bank Finance Corporation to act as a fiscal agent and issue and service the consolidated debt of the FHLBs. (Replaces the Office of Finance.) (Sec. 204)	No provision.	No provision.	Merges OFHEO and Federal Housing Finance Board (FHFB — currently overseer of the Federal Home Loan Banks) into OHFO, a bureau in the Department of the Treasury. (Sec. 101)	Requires FHLBs to register their stock with the SEC and comply with certain SEC reporting requirements. (Sec. 112) Calls for a study of merging FHFB with OFEHS. (Sec. 113)

Provision	S. 1508 (as passed by the Banking Committee)	House Fin. Serv. Manager's Amendment	H.R. 2575	H.R. 2803	S. 1656
Reports and studies for Congress	<p>1. Director and bank regulators to report on various matters related to holdings of GSE securities by insured depository institutions.</p> <p>2. Director (in consultation with GAO) to report on GSE portfolio operations, risk management, and mission.</p> <p>3. Director to report on the growth of GSE debt , and analyze whether debt levels ought to be limited if the GSE is not operating in a safe and sound manner or fails to maintain a certain debt rating.</p> <p>4. Director to report quarterly on risk-based capital standards and the method by which those standards are determined.</p> <p>5. GAO to report annually on the allocation of FHESA's resources and the level of assessments collected by the agency.</p>	<p>1. Treasury and bank regulators to report on holdings of GSE securities by insured banks, and systemic risk implications.</p> <p>2. Director to report on GSEs' investment portfolios, risk management practices, and related safety and soundness implications.</p> <p>3. Treasury to report on growth of GSE debt and possible effects of limits on GSE debt issuance.</p> <p>4. Director to report annually to Congress on risk-based capital standards for GSEs, including minimum and critical capital levels.</p> <p>(Sec. 161)</p>	<p>1. Treasury and bank regulators to report on holdings of GSE securities by insured banks, and systemic risk implications.</p> <p>2. Director to report on GSEs' investment portfolios, risk management practices, and related safety and soundness implications.</p> <p>3. Treasury to report on growth of GSE debt and possible effects of limits on GSE debt issuance.</p> <p>4. Treasury to report on GSEs line of credit with the Treasury: its purposes and the possible effects of eliminating it.</p> <p>5. Director to report annually on risk-based capital standards and minimum and critical capital levels.</p>	No studies or reports called for.	1. Director shall report biennially to Congress on nonmortgage assets held by GSEs and GSE compliance with the Basel Committee's Sound Practices for Managing Liquidity. (Sec. 107)

<b>Provision</b>	<b>S. 1508 (as passed by the Banking Committee)</b>	<b>House Fin. Serv. Manager's Amendment</b>	<b>H.R. 2575</b>	<b>H.R. 2803</b>	<b>S. 1656</b>
Transition from OFHEO to new agency	Various provisions dealing with abolition of OFHEO and the FHFB, continuation of certain regulations, transfer of property and facilities, employee rights and benefits, etc. (Title III)	Various provisions dealing with abolition of OFHEO, continuation of certain regulations, transfer of property and facilities, employee rights and benefits, etc. (Title II, Secs. 201-204)	Various provisions dealing with abolition of OFHEO, continuation of certain regulations, transfer of property and facilities, employee rights and benefits, etc. (Title II, Secs. 201-204)	Various provisions dealing with abolition of OFHEO, continuation of certain regulations, transfer of property and facilities, employee rights and benefits, etc. (Title II, Secs. 201-204)	Various provisions dealing with abolition of OFHEO, continuation of certain regulations and authorities, transfer of property and facilities, employee rights and benefits, etc. (Title II, Secs. 201-204)
Effective date	One year from the date of enactment. (Sec. 173)	One year post-enactment. (Sec. 173)	One year post-enactment. (Sec. 172)	Six months post-enactment. (Sec. 107)	One year post-enactment. (Sec. 162)