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House of Representatives

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March 1, 2010

The Honorable Edolphus Towns
Chairman
Committee on Oversight and Government Reform
U.S. House of Representatives
Washington, DC 20515

The Honorable Dennis Kucinich
Chairman
Subcommittee on Domestic Policy
U.S. House of Representatives
Washington, DC 20515

Dear Chairman Towns and Chairman Kucinich:

The taxpayer bailout of Fannie Mae and Freddie Mac ("Fannie and Freddie") will almost certainly be the most expensive of the financial crisis. We applaud Chairman Kucinich for his commitment to launch an investigation of the Administration's actions regarding Fannie and Freddie.¹ Treasury Secretary Timothy Geithner's announcement last week that the Administration will not produce a plan to protect taxpayers from mounting losses at these failed companies until 2011 not only constitutes a broken promise to develop a plan this year but also shows that the Administration still does not appreciate the urgency of addressing this critical issue. We are writing to request that a hearing be scheduled as there are a number of serious issues that deserve to be brought to the public's attention.

On December 24, 2009, the Obama Administration extended Fannie and Freddie an unlimited bailout guarantee for the next three years.² The Christmas Eve announcement, perhaps scheduled in an attempt to minimize public scrutiny, is deeply troubling because it threatens to recreate the conditions for economic collapse by encouraging unsustainable public subsidies to the U.S. housing market. It is widely

¹ See Dennis Kucinich, "Kucinich to Investigate Fannie/Freddie Bailout" (December 30, 2009), available at http://kucinich.us/index.php?option=com_content&task=view&id=2869&Itemid=1.

² See Rebecca Christie and Jody Shenn, "U.S. Treasury Ends Cap on Fannie, Freddie Lifeline for 3 Years," *Bloomberg.com* (December 25, 2009), available at <http://www.bloomberg.com/apps/news?pid=20601087&sid=abTVUSp9zbAY>.

recognized that Fannie and Freddie misrepresented trillions of dollars of purchases of high-risk subprime and Alt-A mortgages as low-risk prime loans, contributing greatly to the bubble in housing prices that burst and caused the current financial crisis.³ Other public policies, such as loose monetary policy and mortgage-friendly tax incentives, also contributed to the housing bubble, but the central role of Fannie and Freddie in the financial crisis is no longer in doubt.⁴

To keep Fannie and Freddie out of bankruptcy, the Bush Administration placed the companies into federal “conservatorship” in September 2008, extending them each a \$100 billion line of credit.⁵ The Obama Administration later doubled the potential taxpayer support for Fannie and Freddie to \$200 billion each.⁶ By the end of 2009, the companies had drawn down \$111 billion of this \$400 billion lifeline in order to cover their losses on defaulting home mortgages.⁷ Fannie and Freddie have also issued \$1.6 trillion in corporate debt, which is in effect U.S. taxpayer debt and yet is not reflected in the federal debt.⁸ According to Treasury officials, the Administration does not expect Fannie and Freddie to need more than the \$400 billion previously allotted to them.⁹ The American people have a right to know, therefore, why the Administration believed it was necessary to write Fannie and Freddie a blank check on Christmas Eve at a time of skyrocketing federal deficits and bailout fatigue among the American public.

The Administration also recently reversed its decision to require Fannie and Freddie to shrink their investment portfolios of mortgage assets, setting the stage for these risky investments to grow once again.¹⁰ Managing their mortgage portfolios has long been the companies’ most profitable – and riskiest – activity, contributing directly to their financial collapse. Prior to the Administration’s change of course, Fannie and Freddie were required to reduce their portfolios by ten percent per year in order to reduce the risk to taxpayers. Under the new policy, however, Fannie and Freddie will once again

³ See, e.g., Peter J. Wallison, “The Price for Fannie and Freddie Keeps Going Up,” *The Wall Street Journal* (December 30, 2009), available at <http://online.wsj.com/article/SB10001424052748703278604574624681873427574.html>.

⁴ See, e.g., John B. Taylor, *Getting Off Track: How Government Actions and Interventions Caused, Prolonged, and Worsened the Financial Crisis*, Stanford, CA: Hoover Institution Press (2009) and Vikas Bajaj and David Leonhardt, “Tax Break May Have Helped Cause Housing Bubble,” *The New York Times* (December 19, 2008), available at <http://www.nytimes.com/2008/12/19/business/19tax.html>.

⁵ See N. Eric Weiss, Congressional Research Service, “Fannie Mae’s and Freddie Mac’s Financial Problems” (December 31, 2009).

⁶ *Id.*

⁷ *Id.*

⁸ See “Fannie and Freddie: The Last SIVs,” *The Wall Street Journal* (February 23, 2010), available at <http://online.wsj.com/article/SB10001424052748704259304575043573979877134.html>.

⁹ See Rebecca Christie and Jody Shenn, “U.S. Treasury Ends Cap on Fannie, Freddie Lifeline for 3 Years,” *Bloomberg.com* (December 25, 2009), available at <http://www.bloomberg.com/apps/news?pid=20601103&sid=abTVUSp9zbAY>.

¹⁰ See U.S. Department of the Treasury, “Treasury Issues Update on Status of Support for Housing Programs” (December 24, 2009), available at <http://www.treas.gov/press/releases/2009122415345924543.htm>.

be able to grow their portfolios by as much as \$275 billion.¹¹ The Administration's rationale for permitting a risky investment strategy by Fannie and Freddie deserves congressional scrutiny.

The Administration's announcement of lucrative, cash-heavy compensation packages for Fannie and Freddie executives also raises questions about the Administration's plans for the companies' future. The Obama Administration approved \$6 million all-cash pay packages for the CEOs of Fannie and Freddie, with other executives receiving packages of at least \$2 million in cash.¹² These pay packages are significantly higher than the salaries of employees at federal agencies, such as the Department of Housing and Urban Development. Now that Fannie and Freddie are wards of the government, it seems appropriate to ask whether taxpayers are getting good value for their money when executives who are effectively public employees receive such lucrative salaries courtesy of the taxpayers. Furthermore, the Administration's pay czar, Kenneth Feinberg, signed off on the Fannie and Freddie executive compensation packages, yet the cash-heavy plans he approved appear to run counter to what Mr. Feinberg himself recommended in testimony before our Committee.¹³ The Committee ought to demand answers to these questions from the Administration.

Finally, the above questions all point to the most troubling overarching issue: the Administration's continued failure to deliver a plan to unwind its ever-growing commitment to Fannie and Freddie. The Administration promised to deliver such a plan in the President's FY2011 Budget.¹⁴ As late as January 21, 2010, Secretary Geithner promised to propose "a set of detailed reforms beginning this year."¹⁵ However, when the President's Budget was released on February 1, 2010, it made only a vague commitment to "monitor the situation" at Fannie and Freddie.¹⁶ Then, in testimony before the House Budget Committee last week, Secretary Geithner reversed course

¹¹ See Edward Pinto, e-mail to Committee staff (December 26, 2009).

¹² See Chris Isidore, "Big paydays for Fannie and Freddie bosses," *CNNMoney.com* (December 24, 2009), available at http://money.cnn.com/2009/12/24/news/companies/fannie_freddie_pay/index.htm?postversion=2009122416.

¹³ See Kenneth R. Feinberg, testimony before the Committee on Oversight and Government Reform (October 28, 2009).

¹⁴ See note 5, *supra*.

¹⁵ See Timothy Geithner, interview, *PBS Newshour* (January 21, 2010), available at http://www.pbs.org/newshour/bb/business/jan-june10/banks_01-21.html#.

¹⁶ See Nick Timiraos and James R. Hagerty, "No Exit in Sight for U.S. as Fannie, Freddie Flail," *The Wall Street Journal* (February 9, 2010), available at <http://online.wsj.com/article/SB10001424052748704362004575001042824028862.html>. See also Dawn Kopecki, "Fannie, Freddie Kept Off Budget, Dividends Counted," *Bloomberg.com* (February 1, 2010), available at <http://www.bloomberg.com/apps/news?pid=20601110&sid=a3f3k1DeSM4U>.

completely, announcing that the Administration would delay addressing Fannie and Freddie until 2011, conveniently after the mid-term congressional elections.¹⁷

The Administration's ongoing refusal to develop a plan to stanch taxpayers' losses at Fannie and Freddie is unacceptable. According to the Congressional Budget Office, Fannie and Freddie added \$291 billion to the federal deficit last year alone and are expected to add another \$99 billion over the next decade.¹⁸ The real losses for taxpayers may well be much higher, however, given the Administration's determination to use Fannie and Freddie as tools of its troubled housing policy rather than focusing on minimizing taxpayer losses. In the words of Freddie Mac CEO Charles Haldeman, "We're making decisions...without being guided solely by profitability that no purely private bank ever could."¹⁹ The American people have a right to know what the Administration's goals concerning Fannie and Freddie really are and what plans it has in place to meet those goals. It appears that the Administration is using Fannie and Freddie as a backdoor conduit for appropriating billions of dollars of taxpayer money without the consent of Congress. If that is true, the American people have a right to learn about it in a transparent public forum where those responsible for the policy can be held accountable.

A public hearing is a necessary step in continuing the Committee's oversight of government involvement in the financial sector. The ongoing bailout of Fannie and Freddie and the Administration's lack of an exit strategy have profound implications for the future health of the U.S. economy and the fiscal solvency of the federal government. We look forward to cooperating with you in this important investigation.

Sincerely,



Darrell Issa
Ranking Member
Committee on Oversight
and Government Reform



Jim Jordan
Ranking Member
Subcommittee on
Domestic Policy

¹⁷ See Michael R. Crittenden, "The Plan on Fannie, Freddie to Come Next Year, Geithner Says," *The Wall Street Journal* (February 24, 2010), available at <http://online.wsj.com/article/SB10001424052748704240004575085382423762288.html>.

¹⁸ See Congressional Budget Office, "CBO's Budgetary Treatment of Fannie Mae and Freddie Mac" (January 2010), available at <http://www.cbo.gov/ftpdocs/108xx/doc10878/01-13-FannieFreddie.pdf>.

¹⁹ See Nick Timiraos and James R. Hagerty, "No Exit in Sight for U.S. as Fannie, Freddie Flail," *The Wall Street Journal* (February 9, 2010), available at <http://online.wsj.com/article/SB10001424052748704362004575001042824028862.html>.