**WRITTEN STATEMENT OF**

**DANIEL H. MUDD**

**BEFORE THE**

**COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM**

**U.S. HOUSE OF REPRESENTATIVES**

**DECEMBER 9, 2008**

**Written Statement of**
**Daniel H. Mudd**
**Before the**
**Committee on Oversight and Government Reform**
**U.S. House of Representatives**
**December 9, 2008**

Mr. Chairman, Representative Issa, and Members of the Committee, thank you for the opportunity to appear before you this morning. My name is Daniel Mudd. I joined Fannie Mae in 2000, following a decade at General Electric. I served consecutively as Chief Operating Officer and interim Chief Executive Officer of Fannie Mae. In June of 2005, the Board of Directors, with the approval of our regulator, asked me to stay on as CEO, complete the accounting restatement, work cooperatively with our regulator, remediate a number of control weaknesses, and restore the company's position and standing in the capital markets. The company made significant progress in these areas, restating ten quarters of financial filings, returning to timely and current filings as an SEC registrant, settling matters with the SEC and OFHEO, meeting all housing goals and three of four subgoals in 2005, all subgoals in 2006, and two of four subgoals in 2007, and earning $13.3 billion of net income from 2005 through mid-2007. I also worked with Members of Congress to support legislation, passed and signed into law in July, to create a strong, world-class regulator for the GSEs.

Fannie Mae, as a GSE, is required by law to support the housing finance market under all conditions, good or bad. As this market—the only one Fannie was permitted to operate in—went through an unprecedented depression, the company bore commensurate and unprecedented losses; hence we are here today to examine the causes and prescriptions.

By way of background, I believe the roots of the current crisis go back to the enormous increase in consumer and commercial leverage in the 1990s. Indeed, as we entered that decade, there was a significant lag in the supply of homes, particularly for working class and professional families. This lag drove a run-up in home prices, followed by an increase in supply, both of which drove a notable growth in the rate of US homeownership from 1998 to 2006. While Fannie Mae certainly participated in this expansion, others did as well. Interestingly, Fannie's market share fell from its historical level around 40%, to below 20% as competitors including banks, Wall Street, and mortgage specialists entered the market.

Starting in 2007, with the turmoil in the monoline insurance industry, the failure of subprime mortgage originators, and the first nationwide decline in average US home prices since the Great Depression, the financial sector grappled with what most observers view as the worst conditions ever seen in the modern capital markets. While Fannie Mae had made much progress in strengthening its routines, controls, procedures, and practices before this so-called tsunami hit, the business model itself was not immune to the shocks of 2008. To be sure, no financial institution was—and firms that survived both World Wars and the Great Depression were swept under as market conditions continued to worsen throughout 2008.

I will be pleased to elaborate later, but in short, the GSEs were chartered by Congress to provide liquidity, affordability, and stability to the mortgage market at all times. In fact, in the midst of turmoil, when other companies decided not to invest, the GSEs were specifically required to take up the slack. This had worked through several recessions, in the Russian debt crisis of 1998, in the aftermath of 9/11—but not in 2008. The housing market went into a free fall, and with some predicting a decline of as much as 30% from peak, a business model requiring a company to continue to support the entire market could not flourish.

Through the spring and summer of this year, my colleagues and I worked with government officials, regulators, our customers in the banking system, housing advocates, and others to maintain an excruciating balance between providing liquidity to keep the market functioning and protecting Fannie Mae's regulatory capital. At the time the government declared conservatorship over the company, we were still maintaining capital in accord with the relevant regulatory standards, and we were still—along with Freddie Mac—the principal source of lending to the mortgage market. Based on ongoing examinations and frequent, if not daily meetings, our regulator had declared us in full compliance with our capital requirements throughout the period. We were also balancing our HUD housing goals, our role in the global capital markets, our fiduciary responsibility to our shareholders, and critically, our need to help individual homeowners afford their mortgages, stay in their homes, and avoid unnecessary foreclosures. We sought this balance consistent with a strict interpretation of our Congressional charter.

While I deeply respect the myriad challenges facing the Treasury Department and the regulator, I did not believe that conservatorship was the best solution in the case of Fannie Mae. I made that argument at the time and proposed that more modest government support could be used to encourage private investment capital—basically something more like the program many banks are now eligible for. That approach would have maintained the GSE model; admittedly it would not have been a magic bullet, but this market seems to defy magic bullets whether they are fired by the government or the private sector.

I did not prevail with my viewpoint, and events took their course; the issue now presented is how to fashion a more durable solution for the market, the taxpayers, and homeowners. On that topic, I hope there is an opportunity to engage in a debate on the future structure of the US housing finance markets and to develop consensual solutions accordingly. It should be possible to specify a modernized role for the GSEs.

I think it would be a mistake to back into the future by making decisions or eliminating options in the present. I would advocate moving the GSEs out of No Man's Land. Events have shown how difficult it is to balance financial, capital, market, housing, shareholder, bondholder, homeowner, private, and public interests in a crisis of these proportions. We should examine whether the economy and the markets are better served by fully private or fully public GSEs.

It is possible, in all this, to forget the many positive achievements of the GSEs. We financed tens of millions of homes to American families of low-to-moderate income. We provided a set of standards to the industry that made mortgages fairer, more transparent, and available to a broader swath of society. We developed a color-blind underwriting system that became the industry standard. We assured the banking system that their loans, packaged into Fannie and Freddie securities, would garner a predictable, liquid price, around the globe, 24x7. When asked by Congress and the Administration in the spring of 2008, we stepped up and provided the only source of funding for loans up to 125% of local price medians. And, in years when the company did well, we were proud to support organizations that revitalized communities, helped the homeless, sheltered hurricane refugees, and provided our veterans with homes to return to. I hope the good that was done will not be forgotten as we weigh the lessons of 2008.

Let me end by suggesting that homeownership remains a central dream for many Americans. I believe that once the present crisis resolves itself, the fundamental and solid economics of homeownership will be reasserted. Hopefully, there will be a new framework that will encompass comprehensive and judicious reform of the origination and disclosure structure of the mortgage industry, as well as the secondary market where Fannie Mae's role is executed.

Thank you for your attention.