HUD's Regulation of Fannie Mae and Freddie Mac

HUD regulates two housing government-sponsored enterprises, Fannie Mae and Freddie Mac (the GSEs), which were chartered by Congress to create a secondary market for residential mortgage loans. They are considered "government sponsored" because Congress authorized their creation and established their public purposes.

Fannie Mae and Freddie Mac are the largest source of housing finance in the United States. Their Congressional charters require each corporation to achieve public purposes that include providing stability and liquidity in the secondary mortgage market, providing secondary market assistance relating to mortgages for low-and moderate-income families, and promoting access to mortgage credit throughout the Nation, including underserved areas.

In exchange for carrying out these public purposes, the GSEs are accorded various privileges that provide them with some benefits not available to other private corporations. These benefits include an exemption from state and local taxes (except property taxes) and conditional access to a $2.25 billion line of credit from the U.S. Treasury Department.

While the securities that the GSEs guarantee, and the debt instruments they issue, are explicitly not backed by the full faith and credit of the United States, such securities and instruments trade at yields only a few basis points over those of U.S. Treasury securities with comparable terms, based on the belief of many investors that the Federal government would intervene if a GSE were to become insolvent. Consequently, the GSEs are able to fund their operations at lower costs than other private firms with similar financial characteristics.

Even though Fannie Mae and Freddie Mac are Congressionally chartered, they are also private, shareholder-owned corporations that have been regulated by HUD since 1968 and 1989, respectively. Both GSEs fund residential mortgages by purchasing loans directly from lenders, such as mortgage bankers and depository institutions, and holding these loans in portfolio or by issuing mortgage-backed securities (MBS) that are sold to a wide variety of investors in the capital markets.

The Secretary of HUD is the mission regulator for Fannie Mae and Freddie Mac, with oversight authority to ensure that both GSEs comply with the public purposes set forth in their Charters. An independent office of HUD, the Office of Federal Housing Enterprise Oversight (OFHEO), regulates both GSEs for safety and soundness by ensuring that they are adequately capitalized and operating their businesses in a financially sound manner.

<u>The GSE Act</u>

The Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (the GSE Act) established the current regulatory structure for the GSEs. The legislation divided the Federal government's regulatory responsibilities over Fannie Mae and Freddie Mac between the Secretary of HUD and the Director of OFHEO. Under the GSE Act, the Secretary of HUD is charged with general regulatory authority over Fannie Mae and Freddie Mac in all areas other than the GSEs' financial safety and soundness, which is the responsibility of the Director of OFHEO.

Specifically, the Secretary's authority includes setting the level of, and enforcing, three affordable housing goals, monitoring compliance with fair lending requirements, collecting loan-level data from the GSEs on their mortgage purchase activities, creating and making available to the public a data base of non-proprietary GSE loan purchase data, and reviewing and approving new GSE programs with express authority to disapprove any program that the Secretary determines is not authorized under a GSE's charter act purposes or that otherwise is not in the public interest.

Congress Mandated Three Housing Goals for the GSEs

In the GSE Act, Congress mandated that the GSEs devote a percentage of their business to three specific affordable housing goals (the housing goal or housing goals) each year. These housing goals are:

> **Low-and Moderate-Income Housing Goal:** Targets families with incomes at or below the area median income. *("Area median income" is defined as the median income of the metropolitan area, or for properties outside of metropolitan areas, the median income of the county or the statewide nonmetropolitan area, whichever is greater.)*;
>
> **Special Affordable Housing Goal:** Targets very low income families (at or below 60% of area median income), and low-income families in low-income areas (at or below 80% of area median income); and
>
> **Underserved Areas Housing Goal:** Targets families living in low-income census tracts or in low- or middle-income census tracts with high minority populations.

The housing goals are expressed in percentage terms, as the minimum share of *housing units* financed by a GSE's mortgage purchases in a particular year, and include units financed by the GSE's purchase of both single-family and multifamily mortgages. Housing units may count towards more than one housing goal category. In addition, both purchase and refinance mortgages count toward the housing goals.

Beginning in 1993, HUD initiated a number of regulatory actions with respect to the housing goals.   The first of these, an Interim Notice published on October 13, 1993, implemented the housing goal levels for the transition period 1993-1994. In November 1994, HUD extended the interim goals established for 1994 for both GSEs through 1995. Subsequently, HUD published three regulations under the GSE Act. Each regulation set new levels for the housing goals and was dated as follows: December 1, 1995 for the years 1996-2000 (the "1995 Regulation"); October 31, 2000 for the years 2001-2004 (the

"2000 Regulation"); and November 2, 2004 for the years 2005-2008 (the "2004 Regulation").

HUD's 2004 Regulation Increased the Housing Goals Levels for 2005-2008 and Created New Home Purchase Subgoals

HUD's 2004 Regulation implemented the following key changes to the housing goals for the years 2005-2008:

- The housing goal levels were increased significantly over the GSEs' housing goal levels for 2001-2004;

- The housing goal levels rise in nearly equal steps from year-to-year. This staging will allow the GSEs the time needed to adjust their business models to meet the required levels;

- The 2004 Regulation established new Home Purchase Subgoals under each of the housing goals, as discussed in paragraph B below.

(A) *Housing Goal Levels for 2005 – 2008*

The following table summarizes the housing goal levels for the years 2005-2008 and compares the current housing goal levels to those in effect for 2001-2004:

Housing Goal	Goal Levels in 2005 - 2008 *Years*				Goal Levels in
	2005	2006	2007	2008	2001-2004
Low- and Moderate Income	52%	53%	55%	56%	50%
Special Affordable	22%	23%	25%	27%	20%
Underserved Areas	37%	38%	38%	39%	31%*

* HUD's increase of the Underserved Areas housing goal from 31% to 37% incorporates the effects of 2000 census data. The 31% Underserved Area housing goal for 2001-2004 was based on the 1990 census data. However, this same housing goal would equal 36% if it had been based on the 2000 census data. HUD used the 2000 census data to create the housing goal for 2005-2008.

(B) *Home Purchase Subgoals*

HUD's 2004 Regulation also established new Home Purchase Subgoals for the GSEs under each of the housing goals. The Home Purchase Subgoals are expressed as percentages of the total *number of mortgages* purchased by the GSEs that finance the purchase (not refinance) of single-family, owner-occupied properties located in metropolitan areas.

HUD established Home Purchase Subgoals to encourage the GSEs to facilitate greater financing and homeownership opportunities for families and neighborhoods targeted by the housing goals. The focus of the subgoals on home purchases will also help increase the GSEs' support of first-time homebuyers.

Like the housing goal levels for 2005-2008, the Home Purchase Subgoals will rise in nearly equal steps from year-to-year. The following table summarizes the Home Purchase Subgoal levels for 2005-2008:

Housing Goal Categories	**2004 Regulation Subgoal Levels** *Years*				**Previous Levels**
	2005	**2006**	**2007**	**2008**	
Low- and Moderate Income	**45%**	**46%**	**47%**	**47%**	N/A
Special Affordable	**17%**	**17%**	**18%**	**18%**	N/A
Underserved Areas	**32%**	**33%**	**33%**	**34%**	N/A

HUD's 2004 Regulation imposes no requirement for the total number of home purchase mortgages that a GSE must buy. Rather, the rule provides that, however many home purchase loans in metropolitan areas the GSEs buy, a certain percentage must be in each goal category. For example, if a GSE buys one million home purchase mortgages in metropolitan areas in 2005, then 450,000 of these mortgages would need to be for low- and moderate-income families.

(C) *The Special Affordable Multifamily Subgoal*

In the 1995 Regulation, HUD established a dollar-based multifamily subgoal under the Special Affordable housing goal. The multifamily subgoal sets a minimum dollar volume of qualifying multifamily mortgage purchases that each GSE must meet annually. In the 2004 Regulation, HUD retained this subgoal but raised the minimum requirement for years 2005 – 2008 as follows:

Special Affordable Multifamily Subgoal	**New Subgoal Levels 2005-2008**	**Previous Subgoal Levels 2001-2004**
Fannie Mae	**$5.49 billion**	$2.85 billion
Freddie Mac	**$3.92 billion**	$2.11 billion

The GSEs Affordable Housing Performance Under the GSE Act

Each year HUD prepares and makes available a public use database that includes loan-level information on each GSE's mortgage purchases during the year. HUD also publishes reports and various analyses on Fannie Mae's and Freddie Mac's performance in serving the affordable housing marketplace.

Appendix A to HUD’s new housing goals rule includes a comprehensive analysis of the GSEs’ performance under the housing goals through 2003. See pages 63683-63729 in Part 3 and pages 63730-63735 in Part 4, available on this website.