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Highlights

Highlights of GAO-04-269T, a testimony before the Committee on Banking, Housing, and Urban Affairs, U.S. Senate

GOVERNMENT-SPONSORED ENTERPRISES

A Framework for Strengthening GSE Governance and Oversight

Why GAO Did This Study

Congress established government sponsored enterprises (GSE)—such as Fannie Mae, Freddie Mac, the FHLBank System, and the Farm Credit System—to facilitate the development of mortgage and agricultural lending in the United States. Although the federal government does not explicitly guarantee the GSEs' approximately $4.4 trillion in financial obligations, the potential exists that the government would provide financial assistance in an emergency as it has done in the past. Recent financial reporting problems at Freddie Mac have raised concerns about the quality of the GSEs' corporate governance and regulatory oversight.

To assist Congress in reviewing the adequacy of GSE oversight, this testimony provides information on GSE corporate governance, regulatory oversight, and mission compliance measures.

What GAO Recommends

GAO recommends several steps that GSEs, regulators, and Congress can take to strengthen GSE oversight. These steps include strengthening GSE corporate governance, creating a single housing GSE regulator, and establishing standards to measure GSE mission compliance.

www.gao.gov/cgi-bin/getrpt?GAO-04-269T.

To view the full product, including the scope and methodology, click on the link above. For more information, contact Thomas J. McCool at (202) 512-8678 or mccoolt@gao.gov.

What GAO Found

GSEs should lead by example in connection with governance, accountability, integrity, and public trust issues. GSEs should strive to achieve model corporate governance structure, provide reasonable transparency of financial and performance activities, and adopt compensation arrangements that focus on both long-term and short-term results. However, GSE corporate governance has not always reflected best practices. For example, currently, the Chief Executive Officers (CEO) of Freddie Mac and Fannie Mae also serve as the chairmen of their respective GSE boards, which is not consistent with model governance standards that call for officers to work for an independent board. GAO notes that as part of its regulatory agreement, Freddie Mac has agreed to separate the position of CEO and the position of chairman within a reasonable period of time. However, Fannie Mae has yet to take this step. With respect to compensation arrangements, Freddie Mac's focus on short-term financial results as performance targets appears to have contributed to the GSE's recent financial reporting problems.

GSE regulators must be capable, credible, strong, and independent. However, the regulatory structure for the housing GSEs—Fannie Mae, Freddie Mac, and the FHLBank System—is fragmented with safety and soundness and mission oversight responsibilities divided among three regulators. A single housing GSE regulator offers many advantages over this fragmented structure including prominence in government, the sharing of technical expertise, and the ability to assess trade-offs between safety and soundness considerations and certain mission compliance activities, such as affordable housing initiatives. Although there are advantages of a single director model for the new housing GSE regulator, GAO believes on balance that a board or a hybrid board and director might make the most sense to oversee the GSEs' safety and soundness and mission oversight. To be effective, the single GSE regulator must also have all the regulatory oversight and enforcement powers necessary to carry out its critical responsibilities.

Because of a lack of clear measures, it is difficult for Congress, accountability organizations, and the public to determine whether the benefits provided by the GSEs' activities are in the public interest and outweigh their financial risks. Available evidence and data indicate that the housing GSEs have made, in some cases, progress in benefiting homebuyers. For example, it is generally agreed that Fannie Mae and Freddie Mac's activities have lowered mortgage interest rates, although there is debate over the degree of these benefits. However, it is not clear that the housing GSEs' large holdings of mortgage-backed securities benefit borrowers. There is also limited information as to the extent to which the FHLBank System's more than $500 billion in outstanding loans to financial institutions have facilitated mortgage lending.