



Highlights of [GAO-05-576T](#), a testimony before the Committee on Banking, Housing, and Urban Affairs, U.S. Senate

Why GAO Did This Study

Serious concerns exist regarding the risk management practices and the federal oversight of the housing government-sponsored enterprises (GSE)—Fannie Mae, Freddie Mac, and the Federal Home Loan Bank System (FHLBank System), which had combined obligations of \$4.6 trillion as of year-end 2003. In 2003, Freddie Mac disclosed significant accounting irregularities. In 2004, the Office of Federal Housing Enterprise Oversight (OFHEO) cited Fannie Mae for accounting irregularities and earnings manipulation. Fannie Mae has to restate its financial statements for 2001-2004 and OFHEO has required the GSE to develop a capital restoration plan. Also in 2004, the FHLBanks of Chicago and Seattle entered into written agreements with their regulator, the Federal Housing Finance Board (FHFB), to implement changes to enhance their risk management.

To assist Congress in its housing GSE oversight, this testimony provides information on GSEs' missions and risks, the current regulatory structure, and proposed regulatory reforms.

What GAO Recommends

GAO recommends that Congress establish a single regulator with a board or hybrid board and director governance model. This single regulator should be equipped with adequate authorities to oversee all housing GSE activities.

www.gao.gov/cgi-bin/getrpt?GAO-05-576T.

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.

HOUSING GOVERNMENT-SPONSORED ENTERPRISES

A New Oversight Structure Is Needed

What GAO Found

While the GSEs provide certain public benefits, they also pose potential risks. Fannie Mae and Freddie Mac's primary activity involves purchasing mortgages from lenders and issuing mortgage-backed securities that are either sold to investors or held in the GSEs' retained portfolio. The 12 FHLBanks traditionally made loans to their members and more recently instituted programs to purchase mortgages from their members and hold such mortgages in their portfolios. While not obligated to do so, the federal government could provide financial assistance to the GSEs if one or more experienced financial difficulties that could result in significant costs to taxpayers. Due to the GSEs' large size, the potential also exists that financial problems at one or more of the GSEs could have destabilizing effects on financial markets.

The current housing GSE regulatory structure is fragmented and not well-equipped to oversee their financial soundness or mission achievement. For example, although all the GSEs face increasingly similar risks (particularly potential losses in their mortgage portfolios resulting from fluctuations in interest rates), OFHEO is responsible for Fannie Mae and Freddie Mac's safety and soundness oversight while FHFB is responsible for the safety and soundness and mission oversight of the FHLBanks. OFHEO also lacks key regulatory authorities necessary to fulfill its oversight responsibilities. Moreover, the Department of Housing and Urban Development (HUD), which has housing mission oversight responsibility for Fannie Mae and Freddie Mac, faces a number of challenges in carrying out its responsibilities. In particular, HUD may not have sufficient resources and technical expertise to review sophisticated financial products and issues.

Creating a single housing GSE regulator could better ensure consistency of regulation among the GSEs. With safety and soundness and mission oversight combined, a single regulator would be better positioned to consider potential trade-offs between these sometimes competing objectives. To ensure the independence and prominence of the regulator and allow it to act independently of the influence of the housing GSEs, this new GSE regulator should have a structure that consists of a board or a hybrid board and director model. To be effective, the single regulator must also have all the regulatory oversight and enforcement powers necessary to address unsafe and unsound practices, respond to financial emergencies, monitor corporate governance and compensation practices, assess the extent to which the GSEs' activities benefit home buyers and mortgage markets, and otherwise ensure that the GSEs comply with their public missions.