



*OFFICE OF FEDERAL HOUSING ENTERPRISE OVERSIGHT*  
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*Office of the Director*

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March 31, 2004

The Honorable Richard C. Shelby  
Chairman  
Committee on Banking, Housing and Urban  
Affairs  
U.S. Senate  
534 Dirksen Senate Office Building  
Washington, DC 20510

Dear Chairman Shelby:

I appreciate your interest in my views on your proposed legislation to establish a new regulator for Fannie Mae, Freddie Mac and the Federal Home Loan Bank System.

The objective of any legislation to strengthen GSE regulation must be to ensure that the regulator has all the powers, authority and resources necessary to do the job. Certainly, those powers should be no less than those granted to other safety and soundness regulators. Your legislation accomplishes that objective and I would like to express my support for your effort.

The new Federal Housing Enterprise Supervisory Agency ("FHESA") would have powers equal to those of other safety and soundness regulators. FHESA would have the ability to exercise its best judgment on the setting of capital standards, without the constraints of arbitrary statutory limitations. Experience from the savings and loan crisis demonstrates that capital can quickly dissipate in adverse conditions and that actions may need to be taken before capital is impaired. Therefore, the regulator must be allowed full discretion to set capital standards and make adjustments, both temporary and permanent, as necessary. The regulator must also have the authority to make adjustments quickly without unnecessary procedural hurdles.

FHSEA would also have the authority to place an enterprise into receivership. While the new regulator should do everything possible to avoid such a necessity, including timely adjustments to capital, explicit receivership provisions may be critical to preventing or lessening systemic problems in an extraordinary circumstance. Creditors deserve to know that a process exists for an orderly liquidation and satisfaction of their claims should an enterprise become insolvent. Receivership also fosters market discipline, which is an important component of safety and soundness regulation. The enterprises' subordinated debt would also become a more effective tool for the exercise of market discipline.

Your legislation also provides strong enforcement powers, permanent funding outside the appropriations process, direct hire authority, independent litigation authority, and full general

and incidental supervisory powers. This fills many of the gaps in OFHEO's current regulatory authorities.

Additionally, the new regulator must be an independent regulatory agency, with a governance structure that allows for decisive leadership and clear accountability. FHESA achieves that with the appointment of a Director to run the agency.

Finally, I continue to support giving the new regulator responsibility for mission regulation. All other safety and soundness regulators have this authority because safety and soundness regulation includes a responsibility to ensure that regulated entities are operating in a manner consistent with their charters. However, in exercising this authority, a GSE regulator must appreciate that the enterprises were chartered by Congress to fulfill an important public mission. If the risk and capital concerns of a new activity or program are properly addressed, then the regulator should consider charter questions with due regard for the public mission and need to innovate. Safety and soundness regulation is not incompatible with an enterprise's mission. At OFHEO, we consider our mission to be in part a housing mission, as through our work we are making an important contribution to furthering home ownership.

Thank you for considering my views, and we are available to provide the committee with any assistance it may request.

Sincerely,



Armando Falcon, Jr.  
Director

cc: The Honorable Paul S. Sarbanes  
Ranking Minority Member  
Committee on Banking, Housing  
and Urban Affairs  
U.S. Senate  
534 Dirksen Senate Office Building  
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