
MEMORANDUM

TO: VALERIE JARRETT, SENIOR ADVISOR AND ASSISTANT TO THE PRESIDENT FOR INTERGOVERNMENTAL AFFAIRS AND PUBLIC ENGAGEMENT

FROM: CONGRESSMAN SCOTT GARRETT

SUBJECT: FANNIE MAE AND FREDDIE MAC

DATE: THURSDAY, APRIL 22, 2010

I was a bit perplexed by your comments during your interview on Fox News this morning when you highlighted the importance of addressing excessive risk taking in our financial sector but discounted reforming the two biggest risk takers in our economy—Fannie Mae and Freddie Mac. Based on your remarks, it appears to me that you might not be fully informed of the facts surrounding these two entities, their government bailout and their continued excessive risk taking. With leverage ratios reaching more than 100 to 1, Fannie Mae and Freddie Mac’s risk taking far outstripped anything that the private sector was doing. Given the importance of this issue, I wanted to take the opportunity to provide you with some facts on what many respected economists have called the “ground zero” of the financial crisis. Of course, you don’t have to take just my word on this.

“Like a lot of my Democratic colleagues, I was too slow to appreciate the recklessness of Fannie and Freddie...Frankly, I wish my Democratic colleagues would admit, when it comes to Fannie and Freddie, we were wrong.” **Rep. Artur Davis (D-AL)** (*USA Today*, October 14, 2008)

The government needs to look no further than itself to find the root cause of the financial crisis. In attempts to meet a dual public and private mission, Fannie and Freddie endorsed lower and lower underwriting standards which allowed significantly less credit-worthy borrowers to purchase homes. These new standards then paved the way for financial institutions to begin seeking new ways to underwrite and approve loans, degrading the overall creditworthiness of securitized products.

“From the current handwringing, you'd think that the banks came up with the idea of looser underwriting standards on their own, with regulators just asleep on the job. In fact, it was the regulators who relaxed these standards--at the behest of community groups and "progressive" political forces. . . . For years, rising house prices hid the default problems since quick refinances were possible. But now that house prices have stopped rising, we can clearly see the damage done by relaxed loan standards.” **Stan Liebowitz, University of Texas at Dallas** (*New York Post*, February 5, 2008)

During the interview you claim that the Obama Administration and the Democrats are trying to fix the problems that “actually led to the financial meltdown”, yet I don’t see how

you can possibly exclude Fannie Mae and Freddie Mac in your reform considerations. It is very easy to connect the dots on how the affordable housing goals of Fannie Mae and Freddie eventually led to the massive explosion of the subprime market and the housing collapse from which we are still recovering. Yet for some reason, both you and President Obama fail to see this as the underlying problem that needs to be promptly addressed. Instead, the Obama Administration is advancing legislation which is merely a band-aid treating a few of the symptoms of our recent economic crisis while failing to adequately address the underlying cause.

"It doesn't address GSE reform, which arguably is the most costly part of the entire bailout process...If you look at the money we've actually spent on the bailout ... the GSEs are costing us billions. There is no solution to that. That fact is the biggest gap in the reform." **Hal Scott, International Financial Systems, Harvard Law School** (American Banker, April 12, 2010)

The fact that has been obscured by the Administration during this regulatory reform debate is that the largest recipients of government assistance since the economic crisis began are actually not Wall Street banks. The largest recipients of taxpayer dollars during this economic crisis are Fannie Mae and Freddie Mac, which are already expected to cost taxpayers at least \$389 billion, according to the non-partisan Congressional Budget Office (CBO). Rather than stem the tide of support for these entities, the Department of Treasury announced on Christmas Eve in 2009 that they would provide unlimited taxpayer-funded support for Fannie Mae and Freddie Mac through 2012. Unlimited. Today, more than \$8.1 trillion in GSE securities is outstanding, and both Federal Reserve Chairman Ben Bernanke and Treasury Secretary Tim Geithner have stated that the U.S. government has an unwavering commitment to these obligations. Which brings up another point – at the very least, it is inconceivable that the President has not come out in favor of being fully transparent about the costs of the bailout of Fannie and Freddie and putting those true costs on budget. Why is the Obama Administration unwilling to advance reforms to protect American taxpayers from this \$8.1 trillion risk?

"The silence on Fannie and Freddie is deafening. How can they look at themselves in the mirror every morning thinking that they have a regulatory reform bill and they are totally silent on Fannie and Freddie? It just boggles my mind." **Lawrence White, Economics Professor, NYU** (American Banker, April 12, 2010)

As you can see, there is widespread agreement that these two entities were the root cause of the financial meltdown. Despite this, the Obama Administration has not proposed a single reform measure to address this issue in the 15 months since the President took office. Considering then-Senator Obama received the second most campaign contributions from Fannie and Freddie, behind only current Senate Banking Chairman, Chris Dodd, and that Senator Obama was one of the Senate Democrats that blocked GSE Reform legislation from getting to the Senate floor in 2005, I can see why you might be hesitant to discuss them and rightly recognize their role in the collapse of the housing market. Might I suggest that, for the good of the country, President Obama stand up and admit he was wrong in blocking

Fannie and Freddie reform and now put forth a plan to reform them to make up for his past misdeeds.

With taxpayers on the hook for \$8.1 trillion in obligations and quarterly bailouts to Fannie and Freddie, the failure of the Obama Administration to prioritize complete reform of Fannie and Freddie is irresponsible. Your failure to recognize the importance of this matter during your Fox News interview appears to be an explicit acknowledgement that the Obama Administration would rather use the financial crisis to play politics with our nation's economy than offer legitimate solutions.