



## Testimony

Before Subcommittee on Capital Markets, Securities and  
Government-Sponsored Enterprises, Committee on  
Banking and Financial Services House of Representatives

For Release on Delivery  
Expected at  
1:30 p.m. EDT  
on Tuesday,  
September 12, 2000

# GOVERNMENT- SPONSORED ENTERPRISES

## Creation of a Single Housing GSE Regulator

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**G A O**

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# Government-Sponsored Enterprises: Creation of a Single Housing GSE Regulator

Mr. Chairman and Members of the Subcommittee:

We appreciate the invitation to participate in this roundtable discussion on regulation of the housing government-sponsored enterprises (GSE). In your invitation, you asked us to express our views in writing on the topics raised in H.R. 3703 and other issues related to the housing GSEs. For this purpose, we cite here three previous testimonies that summarize relevant work we have conducted on these issues. Housing Enterprises: Advantages and Disadvantages of Creating a Single Housing GSE Regulator (GAO/T-GGD-97-160, July 24, 1997) discusses the advantages and disadvantages of creating a single housing GSE regulator. Housing Enterprises: The Roles of Fannie Mae and Freddie Mac in the U.S. Housing Finance System (GAO/T-GGD-00-182, July 25, 2000) discusses Fannie Mae, Freddie Mac, and their regulators. Federal Housing Finance Board: Actions Needed to Improve Regulatory Oversight (GAO/T-GGD-98-185, Sept. 24, 1998) summarizes our 1998 review of the Federal Housing Finance Board (FHFB), the safety and soundness and mission regulator of the Federal Home Loan Bank System (FHLBank System).

We continue to support a single housing GSE regulator for Fannie Mae, Freddie Mac, and the FHLBank System. A single regulatory body best fits our criteria of being (1) independent and objective, (2) prominent in government, (3) able to achieve economy and efficiency, and (4) able to provide consistency in regulation. Regulation of mission and safety and soundness would be more effective if combined. One regulator could oversee both compliance with the statutory purposes and the financial health of a GSE, provided that the regulator does not have other responsibilities, such as corporate governance, that could create a conflict of interest in its oversight. We concluded that selecting a “stand-alone” agency with a governing board would better ensure the independence and prominence of the regulator and allow it to act independently of the influence of the housing GSEs, which are large and politically influential. A governing board also has the advantage of allowing different perspectives, providing stability, and bringing prestige to the regulator.

Currently, the Office of Federal Housing Enterprise Oversight (OFHEO) regulates Fannie Mae and Freddie Mac on matters of safety and soundness, while the Department of Housing and Urban Development (HUD) is the mission regulator. In 1992, Congress passed the Federal Housing Enterprises Financial Safety and Soundness Act (act) to minimize the risks that the enterprises pose to U.S. taxpayers while ensuring that they meet the housing needs of all Americans. OFHEO’s primary strategies to fulfilling its mission are to establish risk-based capital

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standards and an examination program. Although OFHEO got off to a slow start in implementing its responsibilities, the risk-based capital standards are to be established by year-end 2000, and the examination program is in place.

The act directed HUD to set housing goals, which require the enterprises to meet specified criteria for the purchase of mortgages serving low- and moderate-income individuals. In 1995, HUD established conservative housing goals for the enterprises. In March of this year, HUD proposed a new rule that would require the enterprises to meet higher housing goals for the period 2000 through 2003. Congress recognized, in passing the Act, that the enterprises face a natural tension between maximizing profitability for their shareholders and fulfilling their housing mission. Therefore, the act also defined HUD's general regulatory authority to ensure that the enterprises' activities are consistent with their housing mission. HUD failed to promptly implement this authority, as evidenced by the fact that HUD has not yet implemented a rule to govern the enterprises' nonmortgage investments, such as long-term corporate bonds.

Our review of FHFB raised several questions about its oversight. Specifically, we found (1) that FHFB did not ensure that its annual examinations met its internal standards for assessing safety and soundness, (2) that its off-site monitoring and supervisory enforcement program needed improvements, and (3) that its mission oversight lacked comprehensive policies and procedures to determine whether the FHLBanks were supporting their public mission. In addition, we found that FHFB's involvement in FHLBank System corporate governance and promoting certain programs could complicate its primary duty as a safety and soundness regulator and raised questions about its objectivity. Since our review, it has addressed some of our concerns relating to its examination program, and in June 2000, FHFB approved a rule governing mission activities. The Gramm-Leach-Bliley Act of 1999 partially removed FHFB from corporate governance of the FHLBank System.

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