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The Rescue of Fannie Mae and Freddie Mac – Module A: The Conservatorships

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The Rescue of Fannie Mae and Freddie Mac – Module A: The Conservatorships[1]

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Abstract

Two government-sponsored enterprises (GSEs), the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac), dominated the secondary mortgage market during the US housing crisis, collectively holding or guaranteeing $5.3 trillion in mortgage assets by late 2007. As the crisis escalated, the two GSEs began to report substantial losses and their survival became uncertain. On September 6, 2008, the GSEs' new regulator, the Federal Housing Finance Agency (FHFA), placed the firms into indefinite conservatorships, one step of a four-part government intervention to stabilize the enterprises. This case study evaluates the purpose and efficacy of the conservatorships and finds that they accomplished their emergency goals of stabilizing the GSEs and allowing them to maintain the secondary mortgage market. However, the FHFA Office of Inspector General concluded that the agency could better accomplish its oversight mission by proactively exerting greater control over its conservator approval process. As of this case study's publication, the conservatorship for both companies is ongoing.

Keywords: GSEs, conservatorship, secondary mortgage market, Fannie Mae, Freddie Mac

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[1] This case study is one of seven 2021 Yale Program on Financial Stability (YPFS) case studies that examine in detail the various elements of the government's rescue of the GSEs:

- "The Rescue of Fannie Mae and Freddie Mac – Module A: The Conservatorships" by Daniel Thompson and Rosalind Z. Wiggins.
- "The Rescue of Fannie Mae and Freddie Mac – Module B: The Senior Preferred Stock Purchase Agreements (SPSPAs)" by Daniel Thompson.
- "The Rescue of Fannie Mae and Freddie Mac – Module C: GSE Credit Facility" by Emily Vergara.
- "The Rescue of Fannie Mae and Freddie Mac – Module D: Treasury's GSE MBS Purchase Program" by Michael Zanger-Tishler and Rosalind Z. Wiggins.
- "The Rescue of Fannie Mae and Freddie Mac – Module E: The Housing and Economic Recovery Act of 2008" by Daniel Thompson.
- "The Rescue of Fannie Mae and Freddie Mac – Module F: The Federal Reserve's Large-Scale Asset Purchase (LSAP) Program" by Daniel Thompson and Adam Kulam.
- "The Rescue of Fannie Mae and Freddie Mac – Module Z: Overview" by Rosalind Z. Wiggins, Benjamin Henken, Adam Kulam, Daniel Thompson, and Andrew Metrick.

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The Conservatorships

At a Glance

Concurrent with the US housing market's collapse, the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac) began to post substantial losses in the last two quarters of 2007. These two government-sponsored enterprises (GSEs), which were thought to be backed by an implicit government guarantee, had $5.3 trillion of guaranteed mortgage-backed securities (MBS) and debt outstanding as of December 2007. Given their size and importance in the secondary mortgage market, the potential insolvency of either GSE threatened to destabilize the entire housing market and the financial system.

Summary of Key Terms	
Purpose: To prevent the housing GSEs from becoming insolvent and to allow these GSEs to continue to maintain the secondary mortgage market, supporting US mortgage lending.	
Announcement Date	September 7, 2008
Operational Date	September 6, 2008
Expiration Date	Indefinite/None announced
Return to Profitability	FY2012
Legal Authority	HERA §1117
Funder	US Department of the Treasury
Conservator	The Federal Housing Finance Agency (FHFA)
Total Investment	$191.5 billion

Recognizing that Fannie Mae and Freddie Mac might not be able to stabilize on their own, financial officials called for legislation to create a new regulator that could marshal taxpayer funds to rescue the GSEs. On July 30, 2008, the government passed the Housing and Economic Recovery Act of 2008 (HERA), which created a new GSE regulator, the Federal Housing Finance Agency (FHFA), and provided Treasury with emergency powers to provide funding to rescue the GSEs, should they need it. Confronted with further deterioration of the two GSEs, the FHFA placed them into indefinite conservatorships on September 6, 2008, as part of a four-part rescue plan to stabilize the GSEs.

As conservator, the FHFA immediately suspended dividends on all outstanding stock, replaced both GSEs' CEOs and boards, and then managed the firms indirectly, promising to preserve their precrisis business operations as much as possible. The Treasury funded the firms in conservatorship pursuant to Senior Preferred Stock Purchase Agreements(SPSPAs), ultimately investing a combined $191.5 billion between 2008 and 2017. While both GSEs remained solvent and continued to maintain a secondary mortgage market throughout the crisis, they reported annual losses until 2012. In February 2012, the FHFA submitted a new plan for conservatorship, which focused more on preparing the GSEs and the secondary mortgage market for operations after conservatorship. As of this case study's publication, however, no plan to end the conservatorships has progressed beyond the drafting phase.

Summary Evaluation

Most scholars and evaluators agree that the conservatorships successfully accomplished short-term emergency goals because Fannie Mae and Freddie Mac remained solvent. The interventions also allowed the GSEs to continue purchasing loans and issuing and guaranteeing MBS to the secondary mortgage market when private-label securitization dried up during the crisis. However, the conservatorships have been criticized for poor oversight and for at times prioritizing the GSEs' financial health over the government's broader crisis-fighting goals.

The Conservatorships: United States Context	
GDP (SAAR, nominal GDP in LCU converted to USD)	$14,681.5 billion in 2007 $14,559.5 billion in 2008 $14,628.0 billion in 2009
GDP per capita (SAAR, nominal GDP in LCU converted to USD)	$47,976 in 2007 $48,383 in 2008 $47,100 in 2009
Sovereign credit rating (five-year senior debt)	As of Q4 2007/2008/2009: Fitch: AAA Moody's: Aaa S&P: AAA
Size of banking system	$9,231.7 billion in total assets in 2007 $9,938.3 billion in total assets in 2008 $9,789.07 billion in total assets in 2009
Size of banking system as a percentage of GDP	62.9% in 2007 68.3% in 2008 66.9% in 2009
Size of banking system assets as a percentage of financial system assets	29.0% in 2007 30.5% in 2008 30.23% in 2009
5-bank concentration of banking system	43.9% of total banking assets in 2007 44.9% of total banking assets in 2008 44.3% of total banking assets in 2009
Foreign involvement in banking system	22% of total banking assets in 2007 18% of total banking assets in 2008 19% of total banking assets in 2009
Government ownership of banking system	0% of banks owned by the state in 2008 0% of banks owned by the state in 2009
Existence of deposit insurance	100% insurance on deposits up to $100,000 in 2007 100% insurance on deposits up to $250,000 in 2008 100% insurance on deposits up to $250,000 in 2009
Sources: Bloomberg, World Bank Global Financial Development Database, Federal Deposit Insurance Corporation.	

I. Overview

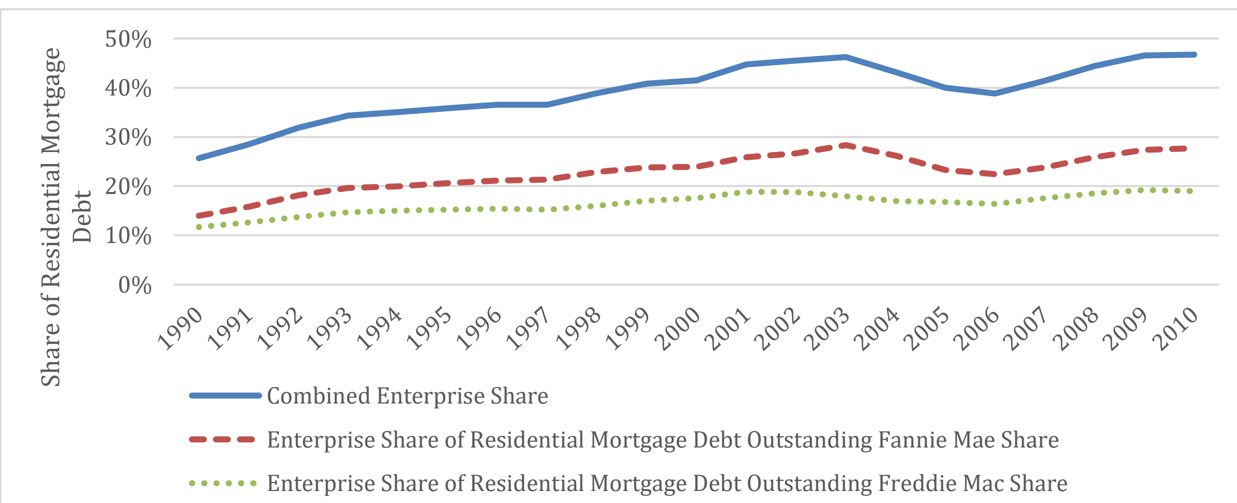
Background

The Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac) are large government-sponsored enterprises (GSEs) that are publicly traded and governed but which were chartered by congressional mandate and are required to satisfy certain government housing goals (FCIC 2011a, 38–39). Many investors believed that the GSEs were backed by an implicit guarantee from the federal government (FCIC 2011a, 39). GSE debt and securities were considered safe and were widely held by US and non-US financial and governmental entities (FCIC 2011a, 39).

Fannie Mae and Freddie Mac's primary business was to buy from originators whole mortgages that met certain criteria (so-called "conforming" mortgages), which they then bundled into mortgage-backed securities (MBS) that they guaranteed and sold (FCIC 2011a, 39). The two GSEs also retained some of these mortgages in their investment portfolios, where they also held agency and non-agency MBS, including nonprime securities (subprime and Alt-A) that they purchased on the open market (FCIC 2011a, 39; FCIC 2011b, 123).

Between 1990 and 2003, the percentage of outstanding residential mortgage debt owned or guaranteed by the GSEs grew from 25.7% to 46.3% (FHFA 2010a). After 2003, the percentage began to decline as nonconforming mortgage origination funded by private-label mortgage-backed securities (PLMBS) increased (Lockhart 2009). As shown in Figure 1, however, the GSE share began to gradually increase again in 2006 after policy changes at the firms reduced underwriting standards, which allowed the GSEs to compete with private firms by buying more nonconforming mortgages, which they could not guarantee as MBS but which they could hold in their portfolios (FCIC 2011b).

Figure 1: Percentage of Outstanding Residential Mortgage Debt Held by the GSEs



Source: FHFA n.d.-b.

Beginning in mid-2007, private-label residential securitization began to shrink to minimal levels because of the housing correction, increasing the GSEs' market share of new loans to 75.6% by year end, which was double the 38% it had been in 2006 (OFHEO 2008, 9–17).

Their market share exceeded 75% during the first half of 2008; the GSEs continued to provide the contracting housing market, which needed liquidity, while also tightening standards for risk management during the 2007–08 market downturn (Lockhart 2008).

As early as mid-2007, the GSEs began to feel the effects of the subprime mortgage crisis as default rates on subprime and nonprime mortgages spiked, causing mortgage lending to slow, the value of mortgage securities to plummet, and private mortgage securitization to evaporate (OFHEO 2008, i–iii). Compounding the effects of the crisis on the firms was their high leverage, which left them especially vulnerable to the market correction (FCIC 2011c, 309). By December 2007, the two companies were highly leveraged—owning or guaranteeing $5.3 trillion of mortgages, with capital of less than 2% (FCIC 2011c, 309). Both GSEs reported billion-dollar losses for fiscal year 2007, the first ever for Freddie Mac and the first in 22 years for Fannie Mae (OFHEO 2008, 10).

Deteriorating circumstances made it difficult for the two companies to raise capital and to meet their safety and soundness standards, especially after the near collapse of Bear Stearns in March 2008 due to sudden disruptions in liquidity (FCIC 2011c, 312–18). By the summer of 2008, after having become increasingly reliant on short-term funding, both GSEs became unable to borrow against their securities to garner enough cash in the repo market (FCIC 2011c, 316). Market concerns increased on July 7, 2008, when a Lehman Brothers investment analyst released a report speculating that Fannie Mae and Freddie Mac would not be able to raise additional capital in light of weak market conditions for their stocks and the possible effect of a new accounting standard that would require the firms to bring their off-balance-sheet entities onto their balance sheets (Harting 2008). The GSEs' common share prices dropped by more than 16% as a result (Lockhart 2008).

When Fannie Mae and Freddie Mac posted billion-dollar losses for fiscal year 2007, the market began to recognize that the firms' weakened condition could destabilize the mortgage market and, by extension, the entire financial system (FCIC 2011c, 311–12). Government officials escalated efforts to pass legislation that would permit developing a viable plan that would support the firms and prevent their collapse (FCIC 2011c).

On July 13, 2008, the Federal Reserve Board (Fed) invoked its emergency authority under Section 13(13) of the Federal Reserve Act to authorize lending through its discount window to Fannie Mae and Freddie Mac for a period of 90 days or less (BGFRS 2008). Section 13(13) allows the Fed to lend to any private entity using government or government-guaranteed debt as collateral.[4] In its statement, the Fed said it was concerned about the systemic risks that the companies' difficulties posed, particularly to the functioning of residential mortgage markets (BGFRS 2008). The Fed said its authorization was intended to supplement Treasury's authority to lend directly to the GSEs (BGFRS 2008).

The Fed—in connection with officials from the Office of the Comptroller of the Currency (OCC), Federal Deposit Insurance Corporation (FDIC), and Treasury—undertook a review of the GSEs' operations, which concluded that both GSEs would soon become insolvent (FCIC 2011c, 317–18). During this time, Treasury's advisors from Morgan Stanley also reviewed Fannie Mae and Freddie Mac's business operations, and their assessment corroborated the Fed and the other government officials' conclusions (FCIC 2011c, 317).

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[4] Unlike Federal Reserve Act Section 13(3), which the Fed relied on for many of its crisis programs, Section 13(13) does not restrict lending to emergency situations.

Because of these concerns, and at the behest of financial regulators and Treasury, Congress passed the Housing and Economic Recovery Act of 2008 (HERA)[5] on July 30, 2008 (FCIC 2011c, 316–17). HERA created a new GSE regulator, the Federal Housing Finance Agency (FHFA), with enhanced authorities, provided enhanced resolution options and, importantly, gave the Treasury emergency authority to buy the securities and obligations of the GSEs (FCIC 2011c, 316). Treasury Secretary Hank Paulson hoped that the government's commitment to preserve the GSEs could keep both companies in operation (FCIC 2011c, 316–17). However, the situation continued to deteriorate (Thompson 2021).

Program Description

The FHFA took Fannie Mae and Freddie Mac into conservatorship on September 6, 2008—the first step of a four-part rescue program designed to stabilize the GSEs and avoid their likely collapse (FHFA n.d.-a). Treasury oversaw the other three steps, which were to:

- Enter into Senior Preferred Stock Purchase Agreements (SPSPAs) with each GSE,
- Establish a new secured credit facility that the GSEs could borrow from, and
- Commit to purchase GSE mortgage-backed securities (Frame et al. 2015, 15).[6]

The FHFA stated that:

> The purpose of appointing the Conservator is to preserve and conserve the [Enterprises'] assets and property and to put the [Enterprises] in a sound and solvent condition. The goals of the conservatorship are to help restore confidence in [Fannie Mae and Freddie Mac], enhance [their] capacity to fulfill [their] mission, and mitigate the systemic risk that has contributed directly to the instability in the current market. (FHFA 2008c, 2)

To this end, the FHFA would later define the "central goal" of the conservatorship[7] as "minimizing [GSE] credit losses from delinquent mortgages" (DeMarco 2010). The agency would also guide its decisions about the conservatorship to be consistent with the statutory purpose of the conservator for "reorganizing, rehabilitating, or winding up the affairs of a regulated entity" (HERA 2008, §1367). Although the conservatorship did not have an expiration date, the FHFA and Treasury asserted that the conservatorship was intended as a temporary measure, or, as Secretary Paulson called it, "a time out" (Paulson 2010, 54).

When the FHFA became conservator, it assumed all power previously vested in the GSEs' directors, officers, and shareholders and shifted the firms' focus to align with the goals of the conservatorships (FHFA-OIG 2015, 6–7). (See Appendix A for an overview of the impact of this shift.) As conservator, the FHFA could govern the companies in any legal capacity to stabilize them, and its actions were not subject to judicial review (FHFA-OIG 2015, 7). The

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[5] Public Law 110-289. See Thompson and Kulam (2021) for a detailed discussion of the relevant provisions of HERA.

[6] See Thompson (2021) for discussion of the Senior Preferred Stock Purchase Agreements, Vergara (2021) for the GSE Credit Facility, and Zanger-Tishler and Wiggins (2021) for Treasury's GSE MBS Purchase Program. For a discussion of the overall government effort, see Wiggins et al. (2021).

[7] Fannie Mae and Freddie Mac were put into separate conservatorships. We herein refer to the conservatorships as one due to the similarities across the two structures. Additionally, while the conservatorships are ongoing, our focus is on the crisis period; therefore, we focus on the period through FY2012, when the enterprises returned to profitability.

FHFA immediately replaced the GSEs' boards of directors and CEOs, suspended voting rights, and froze dividends for common and preferred stockholders (Fannie Mae 2008b, 24). Fannie reported in its 2008 10-K that "because we are in conservatorship, we 'will no longer be managed with a strategy to maximize common shareholder returns'" (Fannie Mae 2008b, 24). The GSEs' stock continued to trade, however (FHFA 2008c, 3). While the FHFA suspended the equity shareholders' rights, it protected rights of senior and subordinated debtholders (Fannie Mae 2008b, 24; Frame et al. 2015, 27).

With Treasury serving as a financial backstop (discussed below), the FHFA also declared that the existing GSE capital limits were not binding during the conservatorship and then suspended them altogether, although it continued to monitor them (FHFA 2008d, 11).

Treasury Funding

Concomitant with the establishment of the conservatorships, each GSE entered into a Senior Preferred Stock Purchase Agreement with the Treasury, which committed Treasury to provide up to $100 billion to each firm in exchange for preferred stock and specified warrants, guaranteeing the solvency of each GSE (Thompson 2021, sec. "Program Description"). Treasury later raised the funding ceiling to $200 billion per firm, then effectively committed an unlimited amount for 2010–12, and reinstated a ceiling on newly available funds equal to $200 billion thereafter (Thompson 2021, "Program Description").

For several years, the GSEs ran losses and requested draws pursuant to the SPSPAs (FHFA-OIG 2015, 2–3). In 2012, the SPSPAs were amended to replace the fixed-rate dividend for Treasury's senior preferred stock with a variable dividend, which effectively transferred all of the GSEs' net income to Treasury (Thompson 2021, sec. "Key Design Decision No. 11"). From the beginning of the conservatorship through the third quarter of 2019, the firms paid a combined $301 billion to Treasury in dividends (FHFA 2019).

Commitments. Commitments under the SPSPAs that the FHFA had to ensure the firms adhered to included informing Treasury of any major decisions regarding, and seeking its approval for:

- Ending the conservatorships,
- Making certain executive compensation decisions,[8]
- Permitting certain transfers or sales of assets (except for fair market value and in the ordinary course of business),
- Declaring dividends,
- Deciding other matters regarding equity interests, and
- Allowing mergers and acquisitions (Fannie Mae 2008b, 28–29).

[8] In addition to the requirements under the SPSPAs, the FHFA also had to comply with the requirements of Section 110 of the Emergency Economic Stabilization Act of 2008 (EESA) that obligated it to develop or adopt programs that would minimize foreclosures (DeMarco 2010).

Also, pursuant to the SPSPAs, the FHFA capped each GSE's portfolio at $850 billion and required a 10% annual reduction, to begin in 2010 (UST/Fannie Mae 2008, 9). However, reduction below $250 billion was not required (UST/Fannie Mae 2008, 9). The FHFA also capped each GSE's debt limit to 110% of its debt held on June 30, 2008, which was $859.9 billion for Fannie Mae and $956.5 billion for Freddie Mac (UST/Fannie Mae 2008, 9). The FHFA later amended the terms of the SPSPA covenants several times (Thompson 2021, sec. "Program Description").

Infrastructure of Conservatorships

To manage the conservatorships, the FHFA established the Office of Conservatorship Operations (OCO) (FHFA-OIG 2012a, 20). Consisting of six employees, the OCO served as the point of contact between the FHFA and the GSEs and sought to harmonize GSE operations with FHFA's goals: maintain the GSEs' assets, ensure that the enterprises fulfilled their missions, and advance their departure from conservatorship (FHFA-OIG 2012a, 20–21). In addition to the director of the FHFA, staff from the OCO attended the GSEs' board meetings and many GSE executive management meetings (FHFA-OIG 2012a, 21).

Under the terms of the conservatorship, the agency had some latitude as to how it could manage the firms and opted for an indirect management style (FHFA-OIG 2012a, 22–24). On November 28, 2008, the agency delegated authority to the GSEs' new boards of directors to oversee management, and to the executive management, including the new CEOs, to oversee day-to-day operations (FHFA-OIG 2012a, 22). The FHFA retained authority over certain significant and unusual business decisions, as shown in Figure 2, for which the GSEs were required to request agency approval (FHFA-OIG 2012a, 22–24). Despite the delegation, the FHFA also retained authority, at its discretion, to review any delegated decision (FHFA-OIG 2012a, 22–24).

Figure 2: GSE: Nondelegated Authorities Requiring Conservator Approval

1. Actions involving capital stock, dividends, the Senior Preferred Stock Purchase Agreements, increases in risk limits, material changes in accounting policy, and reasonably foreseeable material increases in operational risk
2. Creation of any subsidiary or affiliate or any substantial transaction between the enterprise and any of its subsidiaries or affiliates, except for transactions undertaken in the ordinary course of business
3. Matters that related to conservatorship, such as the initiation and material actions about significant litigation addressing the actions or authority of the conservator, repudiation of contracts, qualified financial contracts in dispute due to conservatorship status, and counterparties attempting to nullify or amend contracts due to conservatorship status
4. Actions involving hiring, compensation, and termination benefits of directors and officers at the executive vice president level and above
5. Actions involving the retention and termination of external auditors and law firms serving as consultants to the enterprises' respective boards of directors
6. Settlements in excess of $50 million of litigation, claims, regulatory proceedings, or tax-related matters
7. Any merger with (or purchase or acquisition of) a business involving more than $50 million
8. Actions that in the reasonable business judgment of the enterprises' respective boards of directors were likely to cause significant reputational risk

Source: FHFA-OIG 2012b, 6–7.

The FHFA chose its style of conservatorship to achieve efficiency, concordant goals, and operational savings (FHFA-OIG 2012a, 23–24). The GSEs and their employees knew their businesses and were well equipped to continue to carry out normal business operations (FHFA-OIG 2012a, 23). The GSEs' objectives in conservatorship were the same as the government's objectives (FHFA-OIG 2012a, 23). Additionally, creating and staffing an FHFA unit large enough to directly oversee the entities' normal operations would have required significant expense (funded by the taxpayers), and then there was a likelihood of overlap (FHFA-OIG 2012a, 23–24). Moreover, given that the term of the conservatorships was unknown, the efficacy of creating such a unit was questionable (FHFA-OIG 2012a, 23–24).

In July 2009, the FHFA established a Conservatorship Governance Committee (CGC) composed of senior FHFA executives whose goal was to "ensure coordination on regulatory or supervisory matters that might need to be brought to the attention of the conservator" (FHFA-OIG 2012a, 21). The committee met weekly to coordinate issues related to the GSEs' operations and decision-making authorities, and received notifications from the enterprises and the OCO about imminent issues (FHFA-OIG 2012a, 20-21; FHFA-OIG 2012b, 10).

Upon delegation, the FHFA directed the GSEs to implement internal processes for seeking conservator approval for the nondelegated authorities (FHFA-OIG 2012a, 19–21). In 2010, the FHFA established a formal tracking system to organize the large volume of requests and manage their resolutions (FHFA-OIG 2012a, 20–21).

In December 2011, the OCO sought to clarify the protocol for seeking FHFA approval and created a "one-entry" submission process (FHFA-OIG 2012b, 8). Any communications conducted outside this process (with limited exceptions) were not considered valid (FHFA-OIG 2012b, 8). Executive compensation issues and certain legal issues still had to be approved by the FHFA's Offices of Policy and Analysis and its general counsel, respectively (FHFA-OIG 2012b, 8).

FHFA employees who were not part of OCO participated in the conservatorship activities through resolving requests for approval and/or providing information to the OCO (FHFA-OIG 2012b, 9–11). In addition to its rights and duties as conservator, the FHFA continued its role as GSE regulator. While the FHFA could request information from Fannie Mae and Freddie Mac as conservator, it continued to gather information and conduct safety and soundness measures using its regulatory apparatuses, particularly the Division of Enterprise Regulation (DER), a unit charged with fulfilling the agency's regulatory responsibilities toward the GSEs (FHFA-OIG 2012b, 11, 32).

The relationship between the FHFA's conservatorship and supervision duties was described by the FHFA as follows:

> FHFA's supervision staff does not participate in corporate decision-making or management functions, but maintains a detailed, current understanding of Enterprise business operations and risk management and brings a supervisory perspective to bear in engaging with the Enterprises and FHFA conservatorship staff. FHFA strives to strike a balance so that supervision and conservatorship activities are sufficiently separate to ensure supervisory independence, but Division staff coordinates to an appropriate degree so that there is the benefit of intra-agency collaboration on significant risk matters impacting the Enterprises. (FHFA-OIG 2012b, 32)

One example of this "intra-agency collaboration" is that the OCO relied on the DER's regulatory review of the GSEs' finances rather than conducting a separate review (FHFA-OIG 2012b, 32).

On June 20, 2011, the FHFA issued a final rule that clarified its conservatorship and receivership authorities (FHFA-OIG 2012a, 21).[9] The agency also periodically augmented its directions to the GSEs with "Letters of Instruction" (FHFA-OIG 2015, 12–13).

Despite the FHFA's efforts to manage the conservatorship, a 2012 FHFA Office of Inspector General (FHFA-OIG) audit report concluded that the agency "can better accomplish its oversight mission by proactively exerting greater control over its conservator approval process" (sec. "At a Glance"). The authors criticized the agency for being passive in its oversight and for not ensuring that it reviewed significant matters, that its directives were adhered to, or that its processes were followed (FHFA-OIG 2012b, sec. "At a Glance"). For example, Freddie Mac did not establish internal procedures for requesting approvals until May 2011, and Fannie Mae had not established any such written procedures by 2012 (FHFA-OIG 2012b, 7–8). As a result, communications were scattered: GSEs filed requests to the agency in a decentralized manner, there was no single point of contact at either firm, and the GSEs did not apply consistent application criteria when deciding which requests ought to be sent to the conservator for approval (FHFA-OIG 2012b, 7–8). FHFA-OIG also found flaws in the processes that had been established, such as weak documentation and record-keeping practices (FHFA-OIG 2012b, 12–25). FHFA-OIG concluded that the OCO did not have a full grasp of the conservatorship issues being addressed by FHFA and recommended improvements:

> Specifically, FHFA-OIG recommends that the Agency: (1) revisit FHFA's non-delegated authorities to ensure that significant Enterprise business decisions are sent to the conservator for approval; (2) guide the Enterprises to establish processes to ensure that actions requiring conservator approval are properly submitted for consideration; (3) properly analyze, document, and support conservator decisions; and (4) confirm compliance by the Enterprises with conservator decisions. (FHFA-OIG 2012b, sec. "At a Glance")

The FHFA agreed with most of the recommendations and acted to adopt them (FHFA-OIG 2012b, sec. "Appendix A"). In 2013, the conservatorship offices were merged into a newly formed Division of Conservatorship, which employed 25 persons compared to the prior six (FHFA-OIG 2015, 14).

Operational Emphasis Shifted during Conservatorships

Under the conservatorship, the FHFA directed the GSEs to continue their key business operations and MBS securitizations (FHFA 2008d, 92). No restrictions were placed on the amount of MBS that the GSEs could issue or guarantee (FHFA 2008d, 92). During the early phase of the conservatorship, the FHFA focused the GSEs on stemming credit losses and reducing their retained portfolios, which many investors thought had become outsized and were a source of significant losses (DeMarco 2010, 5). The FHFA also committed to having the GSEs fulfill their affordable housing goals throughout the duration of the conservatorship (DeMarco 2010, 7). (See Figure 5 for a description of how the FHFA's strategic objectives evolved over time.)

Some of the steps taken to implement these objectives included the FHFA tightening GSE underwriting standards, which raised the average FICO credit score of guaranteed mortgages by 35 to 40 points over the following two years (FHFA 2011, iv). The FHFA also shifted guarantee fee calculations from loan volume to underlying loan risk and eliminated

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[9] See 12 C.F.R., Part 1237 (FHFA-OIG 2012a, 21).

preferential underwriting standards for certain entities (MBA 2017, 6). Also, the FHFA requested that Fannie Mae and Freddie Mac "become much more aggressive and innovative in their approaches to loan modification activities to reduce preventable foreclosures" (FHFA 2008d, 14).

The FHFA's conservatorship infrastructure evolved in tandem with its theory of operations. In February 2012, the FHFA submitted to Congress a new strategic plan for the conservatorship, which incorporated policy recommendations circulated by the Obama administration and Congress (FHFA 2012a, 4). The political aspirations for the GSEs were to build a new infrastructure for the secondary mortgage market and to significantly shrink the GSEs' operations and role in the housing markets (see Figure 3) (FHFA 2012a, 4). Notably, the 2012 strategic plan did not carry over the explicit objective regarding fulfilment of the affordable housing mission.[10]

Figure 3: FHFA Objectives for the Conservatorships of Fannie Mae and Freddie Mac

2010	2012	2014
1. Pursue loan modification and mitigate credit losses from delinquent mortgages	1. Build a new infrastructure for the secondary mortgage market	1. Maintain, in a safe and sound manner, foreclosure prevention activities and credit availability for new and refinanced mortgages to foster liquid, efficient, competitive, and resilient national housing finance markets
2. Reduce retained portfolios by 10 percent per year, beginning this year from YE2009 maximum allowed balances of $900 billion, per SPSPAs	2. Contract the GSEs' dominant presence in the marketplace while simplifying and shrinking their operations	2. Reduce taxpayer risk through increasing the role of private capital in the mortgage market
3. Prohibit new products as inconsistent with the purposes of the conservatorships	3. Maintain GSE foreclosure prevention activities and credit availability for new and refinanced mortgages	3. Build a new single-family securitization infrastructure for use by the enterprises and adaptable for use by other participants in the secondary market in the future
4. Ensure fulfillment of the affordable housing mission		

Sources: DeMarco 2010; FHFA 2012a; FHFA 2014.

Both GSEs reported profits for several quarters during fiscal year 2014. After the close of that year, with their future still undecided, the FHFA submitted an updated strategic plan that preserved the three key objectives from the 2012 plan (FHFA 2014, 5). The goal of the updated plan was "overseeing the conservatorships of the Enterprises in their current state

[10] This change presumably reflects the stance adopted by the Obama administration in February 2011, when it submitted a report to Congress titled "Reforming America's Housing Finance Market." In the report, the Administration proposed winding down Fannie and Freddie and giving the affordable housing mission to the Federal Housing Administration (FHA) (UST 2011, 18–22).

and ensuring that the Enterprises' infrastructure meets the needs of their current credit guarantee businesses and other operations" (FHFA 2014, 5).

Outcomes

Due to the conservatorships and the four-part rescue plan, the GSEs continued to operate after conservatorship similarly to how they did before conservatorship because they maintained their key role in the secondary mortgage market and successfully prevented its collapse (FHFA 2008d, 86–88). As private-label securitization had evaporated, the role of the GSEs became even more critical during the months following September 2008, and the percentage of new mortgages that they purchased increased (FHFA 2008d, 86–88, 91).

Immediately following the conservatorship announcement, market demand for GSE debt seemed to increase (FOMC 2008, 4). However, given the restrictions on dividends and voting rights for common shareholders imposed by the conservatorship, and that the SPSPAs established a stock class senior to all existing GSE classes of stock, the common stock of the two GSEs—which had already fallen more than 95% since the previous year—continued to lose value (FOMC 2008, 4; Thompson 2021, sec. "Key Design Decision No. 4").

Mortgage yields also fell for a brief period. The Monday following the announcement of the conservatorships, the rates on Fannie Mae's five-year debt and its mortgage-backed securities MBS dropped about 30 basis points and 50 basis points, respectively, relative to yields on five-year Treasuries (Frame et al. 2015, 22). In response to the drop in MBS yields, conforming mortgage rates fell by 40 basis points (Frame et al. 2015, 22). Following Lehman Brothers' collapse on September 15, mortgage rates rose above pre-conservatorship levels (Frame et al. 2015, 22–23).

On November 25, 2008, hoping to ease yield levels down, the Fed introduced its large-scale asset purchases, which enabled the central bank to purchase up to $500 billion in MBS and $100 billion of GSE debt (later raised to $1.25 trillion in MBS and $175 billion of GSE debt) (CBO 2010, 10). By March 2009, GSE mortgage yields had fallen 150 basis points (Lockhart 2009).

One of the GSEs efforts to strengthen their financial positions was to enforce representations and warranties made by loan originators, which meant that Fannie and Freddie tried to shift credit losses (stemming from defaulted mortgages) to the originators that relied on poor documentation and underwriting standards (Frame et al. 2015, 27–28). This practice led originators to tighten underwriting standards and increased the cost of mortgage lending, which some critics identified as inconsistent with the GSEs' broader housing objectives (Frame et al. 2015, 27–28). However, tightened underwriting standards led to an increase in the percentage of mortgages purchased by the GSEs with a loan-to-value ratio of 80% or less—from 76% to 89% from 2007 to 2009 (Fannie Mae 2009, 151; Freddie Mac 2009, 151). Nevertheless, the GSEs continued to report losses for nearly four years after the conservatorship's implementation, mainly due to continued mortgage defaults (particularly in single-family credit guarantees), falling housing prices impacting their securitization businesses and portfolios, and the cost of annual dividends on senior preferred stock, which the GSEs paid to Treasury (Frame et al. 2015, 25).

The GSEs have each significantly reduced the sizes of their portfolios and outstanding debt since the beginning of conservatorship, as shown below in Figure 4. During this period, they also have maintained or slightly increased the amount of their MBS issuances, which increased their market share of mortgage securitization after private-label activity began to decline in 2007 (OFHEO 2008, 9–17). Additional nonmonetary changes occurring under conservatorship are shown below in Figure 5.

The fiscal year 2012 marked a turning point for Fannie Mae, Freddie Mac, and the FHFA's conservatorship operations: for the first time since 2008, the GSEs did not require additional Treasury funds to cover their losses (FHFA 2012c, 16). Pursuant to the third amendment to the SPSPAs, all profits were paid to Treasury (FHFA 2012c, 87).

In each statement of strategic objectives, the FHFA emphasized that conservatorship was not a long-term strategy for the GSEs. Because the firms were chartered by Congress, the agency was limited in its options for rehabilitation (Frame et al. 2015, 18–21). The FHFA could only release the firms from conservatorship back to their previous structures, which was politically contentious, and the potential merits of reprivatization were unclear (Frame et al. 2015, 18–21). By the time the GSEs began realizing a profit in FY2012, they collectively owed the government $189.5 billion (liquidation preference plus initial investment pursuant to the SPSPAs) (Thompson 2021, sec. "Outcomes"). Although the GSEs have paid Treasury a combined $292.3 billion in dividends (through the fourth quarter 2018), such payments did not reduce their debt but did keep them from retaining earnings and building their capital (Thompson 2021, sec. "Key Design Decision No. 11").

Since the conservatorship began, many individuals and entities, mainly shareholders, have sought damages from the FHFA, and several of these cases remain unresolved (Solomon and Zaring 2015, 372–78). Several governmental and private parties have proposed plans to end the conservatorships and reform the entities, which would require congressional action (Solomon and Zaring 2015, 419–26). At this time, however, the GSEs remain in conservatorship (Thompson 2021, sec. "Outcomes").

Figure 4: GSE Sizes (in billions of USD)

	Fannie Mae			**Freddie Mac**		
Date	**Portfolio**	**MBS/Guarantees**	**Debt**	**Portfolio**	**MBS/Guarantees**	**Debt**
2008	$761.4	$2,559.5	$843.0	$736.9	$1,834.4	$814.9
2010	$802.9	$2,642.8	$830.2	$710.2	$1,763.7	$742.6
2012	$654.3	$2,694.8	$664.1	$568.0	$1,591.7	$570.3
2014	$438.1	$2,768.3	$479.0	$413.6	$1,646.4	$439.5
2016	$306.5	$2,861.3	$353.6	$308.1	$1,817.9	$381.5

Note: "Date" reflects GSE size in September of the year listed.
Sources: Fannie Mae 2008a; Fannie Mae 2010; Fannie Mae 2012; Fannie Mae 2014; Fannie Mae 2016; Freddie Mac 2008; Freddie Mac 2010; Freddie Mac 2012; 2014; Freddie Mac 2016.

Figure 5: GSE Programs and Operations before and after the Conservatorship

GSE Reform: Quick View		
	GSEs Pre-Conservatorship	**GSEs in Conservatorship**
Investor purpose	Growth of stock returns/risks	Conservation of assets
Regulatory limitations on pricing	No	Yes
Retained investment portfolio	Large	Reduced
Capital standards	Low capital levels on both retained/guaranteed risk	Reduce capital cushion to zero by 2018
SF risk transfers to private market	Front-end only (MI and lender recourse)	Testing back-end structures in addition to front-end
MF risk transfers to private market	Lender risk share	Lender and capital markets risk share/transfer
Number of entities	Two	Two
New guarantor entrants permitted	No	No
SF lender access	Preferential pricing and underwriting by loan volume	Guarantee fee and underwriting variances restricted
Support for single-family TBA market	Yes	Yes
Support for multifamily finance	Yes	Yes
Preserve operational infrastructures and processes	Yes	Yes
Affordable housing mission	Yes	Yes

Terms: SF (single family), MI (mortgage insurance), MF (multifamily), TBA (To be announced). Source: MBA 2017, vii.

II. Key Design Decisions

1. The Housing and Economic Recovery Act passed in July 2008 constituted an essential step to establish and finance the conservatorship.

The government passed HERA in July 2008 to provide enhanced resolution alternatives to the GSEs' regulator in light of the severely weakened condition of the firms, their critical role in the stability of the mortgage and housing markets, and the stresses then impacting those markets (among other things) (Frame et al. 2015, 14). Prior to HERA, OFHEO (Office of Federal Housing Enterprise Oversight, former GSE regulator) could have taken the firms into conservatorship, but there existed no viable funding to support such a move, largely rendering the authority ineffective (Frame et al. 2015, 5). Also, the GSEs were exempt from the US bankruptcy code, and there was no authority for OFHEO to place them in receivership (Frame et al. 2015, 18–21). HERA created a new regulator, the FHFA, and provided mechanisms for Treasury to fund the firms during an emergency period, ensuring their solvency during a conservatorship (Frame et al. 2015, 18–21). HERA also provided the FHFA expanded authority to place the firms into receivership if necessary (Frame et al. 2015, 18–21). (See Thompson and Kulam (2021) for more information regarding HERA.)

2. Federal officials placed Fannie Mae and Freddie Mac into conservatorship instead of nationalizing them or placing them into receivership.

W. Scott Frame et al. (2015) dismiss the claim that Treasury could have stabilized the GSEs by simply buying their debt or MBS without a formal apparatus (21). Noting the amount of capital required to stabilize the GSEs, Frame et al. argue that the Treasury needed a mechanism to ensure that it could continuously fund the GSEs in the needed amounts (which were unknown at the time, but estimates of which were in the tens of billions) (Frame et al. 2015, 21). As such, Treasury required a government intervention to establish and operate such a mechanism (Frame et al. 2015, 19). Operating with the common understanding that the government needed to save the GSEs, Frame et al. identify three options that government officials could have taken.

Nationalization. The first option was nationalization, which Frame et al. (2015) define as purchasing and controlling at least an 80% equity stake in each company (21). The government considered this option the least favorable because the government would have been compelled to assume all liability for Fannie Mae and Freddie Mac and to consolidate their operations onto its balance sheet (Frame et al. 2015, 21).

However, the definition of the term "nationalization" is fluid, unlike the definitions of "conservatorship" and "receivership" (which are discussed later) (Elliott 2009, 7). For the purposes of this paper, "nationalization" refers to the government gaining a controlling interest in a company (one that might be greater than 50% but less than 80%) such that it is empowered to make or influence critical decisions about how the company operates. Nationalization can be accomplished in a variety of ways but does not denote application of a specific, prescribed administrative process, such as conservatorship or receivership, or the FDIC bank resolution process, although such processes may be employed (Elliott 2009, 13–15).

In light of this working definition, the government could have nationalized the GSEs by making—via Treasury—a substantial financial contribution and gaining via contractual agreement (such as a stock purchase agreement, memorandum of understanding, or shareholders' agreement) certain constraints on the GSEs operations (Lockhart 2018, 12). (Also see Appendix B.) However, taking control of the GSEs without the benefit of a known and predictable framework could have created operational and legal messes (Jester et al. 2018, 7). Treasury's ability to operate the companies would still have been subject to management's compliance with the operative contract and complicated by the need to comply with various regulations regarding preservation of the GSE charters (Lockhart 2018, 12). Treasury Secretary Paulson was of the opinion that such an arrangement would not adequately protect the taxpayers and, thus, would not agree to contribute capital to the GSEs without their being in a conservatorship or receivership (Jester et al. 2018; Lockhart 2018, 12).

Receivership. After the passage of HERA, receivership was a second viable option available to the government (Frame et al. 2015, 18). The intent of a receivership is to wind down an organization rather than merely stabilize it and have it continue operations (Jester et al. 2018, 7). Under HERA, invoking a receivership would mean the application of timelines and the need for a bridge entity since the GSEs could be dissolved only by an act of Congress (Frame et al. 2015, 18–19). Additionally, the FHFA would be compelled to reform the firms as they were released from receivership, which would have been required in five years

(Frame et al. 2015, 20). However, the structure of the GSEs had been debated for years, and Congress had yet to resolve those concerns (Frame et al. 2015, 20).

Dan Jester served in Paulson's Treasury during the rescue and, with other Treasury officials, questioned the feasibility of setting up the receiverships in time to be effective (Jester et al. 2018, 7). They doubted the GSEs would acquiesce to such a forceful intervention and worried the firms would respond by filing lawsuits and drumming up congressional opposition to it (Jester et al. 2018, 7). Secretary Paulson also worried that receiverships might also "spook the markets" and might put some debtholders at risk, increasing instability of some banks and other financial institutions (Lockhart 2018, 12). Moreover, even if the receiverships were put in place, Jester et al. expressed doubt that the FHFA—a new agency with "no institutional experience managing a receivership"—was up to the task of overseeing the successful implementation of one (Jester et al. 2018, 7).

Conservatorship. The final option was conservatorship. Although a conservatorship could last indefinitely, it was seen as a temporary measure that would allow the government to take control of the companies and stabilize them for continued operation, while Congress considered how to address the more contentious structural aspects of the GSEs' special status (Frame et al. 2015, 20; Jester et al. 2018, 7). Conservatorship also was seen as an option that could be implemented swiftly, which was important given the rising number of concerns at other major financial institutions that were debtholders (Frame et al. 2015, 20; Jester et al. 2018, 7–8).

Most importantly, however, conservatorship allowed the GSEs to continue their operations and supply the secondary mortgage market, something critically needed as the private market severely contracted (Frame et al. 2015, 26–27; Jester et al. 2018, 7). The efficacy of this option hinged on the Treasury's ability to finance the conservatorship, which was made possible by HERA (Frame et al. 2015, 19). Frame et al. (2015) note that if the Treasury could not have financed the conservatorship, then receivership would have been the best option (20). HERA also included a clause that allowed the FHFA to later place the GSEs into receivership from conservatorship (Frame et al. 2015, 21). However, James Lockhart, then director of the FHFA, stated that this was something that his agency never seriously considered (Lockhart 2018, 8–10). See Appendix B for a comparison of the attributes of the three possible solutions and see Wiggins et al. (2021) for further discussion of the conservatorship decision.

3. Government officials kept the conservatorship decision secret to prevent the agencies from exerting political pressure.

Secretary Paulson identifies secrecy, speed, and timing as the three aspects in the execution of Fannie Mae and Freddie Mac's conservatorship that avoided a protracted battle with the GSEs, news leaks to the public, and a major market swing (Paulson 2010, chap. 1). After keeping the conservatorship discussion (and later the conservatorship decision) a secret for several weeks, Paulson, FHFA Director Lockhart, and Fed Chairman Ben Bernanke presented the option to Fannie Mae and Freddie Mac's CEOs with no warning (Paulson 2010, chap. 1). These officials knew that the CEOs might fight to keep their positions and thus gave them no time to publicize the conservatorship or solicit assistance from their political contacts on Capitol Hill (Paulson 2010, 75–76). Paulson feared that if either CEO decided to resist the conservatorship, they could delay its implementation and instigate panic in the markets (Paulson 2010, 75–76).

Federal officials also met with Fannie Mae's CEO and executive board first, since they anticipated that Fannie Mae's team would be more resistant to the idea (Paulson 2010, 83–

84). Federal officials took caution to avoid any press coverage of the event and selected the FHFA's office as the location for their private meetings with Fannie Mae and Freddie Mac (Paulson 2010, 83–84). They arranged for the first meeting with Fannie Mae to start at 4:00pm on Friday, September 5 so that the markets would have closed before the meeting had finished (Paulson 2010, 83–84). After each meeting, they informed members of the House Financial Services Committee and Senate Banking Committee, so that they would not be surprised when the news broke to the public (Paulson 2010, 87–93). Lockhart and Paulson announced the conservatorships as part of a four-part rescue plan for the GSEs on Sunday, giving the public an opportunity to react before markets reopened on Monday (Paulson 2010, 95–98).

4. The FHFA replaced the GSEs' Boards of Directors and CEOs.

When the FHFA placed Fannie Mae and Freddie Mac into conservatorship, it also replaced the firms' CEOs and appointed new nonexecutive chairmen of the boards (FHFA 2008b). Secretary Paulson expressed the gravity of the intervention to justify firing the GSEs' CEOs (Paulson 2010, 93–94). When asked for his rationale to fire Fannie Mae's CEO, he replied, "I don't think that you could do something this drastic and not change the CEO" (Paulson 2010, 93–94). FHFA director Lockhart justified removing the GSE boards with similar logic and noted, "Although it is not necessary in a conservatorship, new boards are being formed as a matter of good governance" (Lockhart 2008).

As conservator, the FHFA ascended to all authority of the boards and management but eventually delegated some of that authority back to the new board and management while retaining a right of review (DeMarco 2010, 3–4). Even under conservatorship, in exercising their authority, the GSE officers remained "subject to the legal responsibility to use sound and prudent business judgment in their stewardship of their companies" (DeMarco 2010, 3).

5. The FHFA protected all classes of GSE creditors but not shareholders.

The FHFA adopted this approach to save money, to increase public confidence in the two GSEs, and most importantly, to keep the GSEs operating. After enacting the conservatorship, the FHFA froze the GSEs' dividend payments and shareholder voting rights (except for Treasury's senior preferred stock) (Fannie Mae 2008b, 21). The FHFA estimated that freezing dividends would save the GSEs about $2 billion in reserve capital annually (FHFA 2008b). The GSE stock remains outstanding, but there is no guarantee that it will be restored to its full rights when the firms exit the conservatorships (Fannie Mae 2008b, 50; FHFA 2008c, 3).

Given Treasury's funding commitment to guarantee GSE solvency (up to the stated limits), the GSE bondholders were protected (Jester et al. 2018, 8–9). Federal officials recognized that protecting bondholders was critical to minimize immediate risks to the financial system, to protect future investors in debt and MBS, and to quiet any concerns about the government's credibility (Lockhart 2009; Paulson 2010; UST 2008). On the day after Fannie and Freddie entered conservatorship, FHFA announced that conservatorship did not change the legitimacy of current and future financial contracts (FHFA 2008a; Lockhart 2008). Important factors supporting the government's decision to protect all holders of debt and MBS included: (1) the sheer size of the GSEs' liabilities, (2) the nature of the bondholders, and (3) the GSEs' close alignment with the government (Jester et al. 2018, 8–9; UST 2008).

GSE debt and obligations benefited from an "implied government guarantee," which helped them enjoy a robust market with their debt being widely held (Frame et al. 2015, 1). Much of this debt was held by foreign central banks and foreign and domestic financial institutions that believed that GSEs' securities were effectively risk-free (UST 2008). Secretary Paulson felt that allowing the international debtholders to suffer losses could undermine foreign investors' confidence in the United States' creditworthiness, which could cause a run on the dollar or a Treasury sell-off (CBO 2010, 22; Paulson 2010, 77–78). Also, many domestic banks, which were already under stress, held GSE debt due to favorable capital rules (Rice and Rose 2016, 7–9).

The government's actions, in essence, made the implied guarantee firm, which seems to have increased confidence in the GSEs, which Lockhart (2008) and Frame et al. (2015, 22) argue is evidenced in falling yields—at least before Lehman Brothers collapsed. (See also Wiggins et al. [2021] for further discussion of these points.)

6. The FHFA established a limited infrastructure to manage the conservatorships.

To manage the conservatorships, the FHFA established a new infrastructure[11] consisting of the Office of Conservatorship Operations and the Conservatorship Governance Committee (FHFA-OIG 2012a, 20–21). The OCO acted as the liaison and administrator between the GSEs and the FHFA, relying on FHFA resources to resolve issues (FHFA-OIG 2012a, 20–21). The CGC was composed of senior FHFA executives whose goal was to "ensure coordination on regulatory or supervisory matters that might need to be brought to the attention of the conservator" (FHFA-OIG 2012a, 21).

Because the OCO employed only six people, the OCO also relied on the regulatory resources throughout the FHFA to evaluate the GSEs' success in achieving these goals and address conservator issues (FHFA-OIG 2012a, 21; FHFA-OIG 2012b, 22–23). One audit report highlights the possible tensions that may arise from FHFA's status as both conservator and supervisor: "For example, FHFA could potentially be faced with criticizing its own actions or those of its senior officials" (FHFA-OIG 2012a, 30). The Office of Inspector General also noted that the conflict was partly addressed by the delegation of most management decisions to the enterprises' boards and managers (FHFA-OIG 2012a, 30).

The FHFA defended its original structure and claimed that the unknown duration of conservatorship prevented the agency from making long-term investments in its own infrastructure (FHFA-OIG 2012a, 31–32).

Nevertheless, the FHFA agreed with most of the OIG recommendations and took steps to implement them (FHFA-OIG 2012b, 31–37). As it became more apparent that the GSEs would not soon exit the conservatorship, the FHFA refined its strategic plans and evaluation mechanisms by developing a reporting scorecard; establishing an approval tracking and resolution process; and in 2013, consolidating all conservator functions into a Division of Conservatorship, which employed 25 people as compared to the previous six-person OCO (FHFA-OIG 2012b, 9–11; FHFA-OIG 2015, 11, 14).

7. The FHFA managed the conservatorship indirectly, delegating significant authority to the new boards of directors and CEOs.

The FHFA's inspector general (IG) noted that a conservator generally can take one of three approaches: "Actively managing every aspect of an entity's operations; Monitoring the conserved entities' decision-making and stepping in when it feels it is appropriate; or

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[11] The FHFA described efforts to enhance its governance practices through various white papers and annual reports (FHFA-OIG 2015, 13).

deferring to the conserved entity on most decisions and stepping in only in cases of greater significance" (FHFA-OIG 2012a, 22). The IG noted that FHFA had taken the third approach.

> FHFA has determined to (1) delegate authority for general corporate governance and day-to-day matters to the Enterprises' boards of directors and executive management, and (2) retain authority for certain significant decisions. (FHFA-OIG 2015, 11–12)

Within three months of establishing the conservatorships, the FHFA had delegated significant authority to the new boards of directors and CEOs (FHFA-OIG 2012a, 22, 30). It did this as an efficient way to run the massive businesses consistent with the tenets of the conservatorship—to manage the firms as going concerns, stabilize them financially, and return them to independent operation (FHFA-OIG 2012a, 23). However, it's important to note that the FHFA retained authority over a group of key business decisions, for which it required the GSEs to seek prior approval (FHFA-OIG 2012a, 19–20). These powers were referred to as nondelegated authorities (FHFA-OIG 2012b, 6). Among other things, these included capital actions, compensation policies, and other large transactions, including legal settlements, merger activities, and deals with subsidiaries (FHFA-OIG 2012a, 19–20). (See Figure 2 for a summary of the nondelegated authorities.) In addition to specified nondelegated authorities, the FHFA retained the right to review (and to overturn) any other business decision it deemed important along the way (DeMarco 2010, 3–4).

The FHFA cited three reasons in defense of its style of conservatorship: efficiency, concordant goals, and operational savings (FHFA-OIG 2012a, 23–24). The GSE employees knew the business and were well equipped to continue to carry out normal business operations (FHFA-OIG 2012a, 23). The goals of the enterprises were consistent with those of the conservatorships, i.e., return the firms to stability: "FHFA views part of its 'preserve and conserve' mandate to include preserving the entities as private companies with the capacity and responsibility to make business decisions following normal corporate governance procedures" (FHFA-OIG 2012b, 31). Acting Director Edward J. DeMarco suggested that delegating authority to GSEs created operational savings because FHFA avoided duplicating work that the GSEs were already doing (FHFA-OIG 2012a, 23–24).

Instead, the FHFA communicated with the GSE employees about the conservatorship and tried to maximize retention (FHFA-OIG 2012a, 13). The OCO and the CGC worked to ensure that the firms were operating in a manner consistent with their delegations of authority, the stated conservator goals, and the overall objectives of the conservatorship (FHFA-OIG 2012a, 20–21).

However, the OIG found that the agency's practices were flawed:

> FHFA-OIG's reports consistently have revealed two trends: (1) the Agency, in its role as a conservator, does not independently test and validate Enterprise decision-making; and (2) the Agency, in its role as a regulator, is not proactive in its oversight and enforcement. In addition, FHFA may not have enough examiners to meet its oversight responsibilities. (FHFA-OIG 2012a, 2)

As a result of these procedures, the OIG criticized FHFA for not overseeing several major decisions that the GSEs made (FHFA-OIG 2012b, 12–13). These included changes to Fannie's single-family underwriting standards and the High Touch Servicing Program, whereby Fannie Mae transferred $1.5 billion in mortgage servicing rights to third-party specialty servicers (FHFA-OIG 2012b, 12–13). The inspector general also found that the agency often failed to question decisions that were submitted to it for approval and relied too often on management's decision without an independent proof or business case (FHFA-OIG 2012b, 20–22).

Additionally, the OIG concluded that the agency could better accomplish its oversight mission by proactively exerting greater control over its conservator approval process:

> Specifically, FHFA-OIG recommends that the Agency: (1) revisit FHFA's non-delegated authorities to ensure that significant Enterprise business decisions are sent to the conservator for approval; (2) guide the Enterprises to establish processes to ensure that actions requiring conservator approval are properly submitted for consideration; (3) properly analyze, document, and support conservator decisions; and (4) confirm compliance by the Enterprises with conservator decisions. FHFA agreed with most of FHFA-OIG's recommendations." (FHFA-OIG 2012b, sec. "At a Glance")

8. The FHFA directed the GSEs to continue fulfilling their statutory purposes, including their support for affordable housing.

The GSE intervention was designed to keep the firms in operation so that they could "continue to fulfill their mission of providing stability, liquidity, and affordability to the [mortgage] market" (FHFA 2009a, ii). As a result, under the conservatorship, the FHFA directed the GSEs to continue their key business operations and MBS securitizations and placed no restrictions on the amount of MBS they could issue or guarantee (FHFA 2008d, 92). Under the SPSPAs, they also were allowed to expand their portfolios for a short time—up to a limit of $850 billion—before having to start reducing them in 2010 (UST/Fannie Mae 2008, 9). The GSEs' ability to continue operations was especially critical early in the conservatorship; when private-label securitization shrank during the global credit crisis, the GSEs assumed a still larger role in the housing market and purchased a greater proportion of new mortgages (OFHEO 2008, 9–17).

The GSEs' housing mission was also targeted to assist with the government's wider foreclosure prevention efforts. At the end of 2008, FHFA reported the GSEs were "playing an important role in assisting the federal government in foreclosure mitigation activities" (FHFA 2009a, 4). Less than one year after the conservatorship began, the GSEs started to participate in the Home Affordable Refinance Program (HARP) and Home Affordable Modification Program (HAMP) (FHFA 2010b, 7–8). HARP and HAMP were intended to serve the dual goals of limiting GSE credit losses and alleviating wider mortgage market stress, both of which were important for the GSEs' long-term stability (DeMarco 2010, 5; FHFA 2009a, 85–87; FHFA 2010b, 7–8).

During the mortgage crisis, the government continued to prioritize affordable housing goals and relied on Fannie Mae, Freddie Mac, and the Federal Home Loan Banks to meet them (CBO 2010, vii; Lockhart 2009). Through HERA, FHFA received the authority to enforce these goals (which had previously rested with the US Department of Housing and Urban Development) but mandated a change in the way they were structured beginning in 2010 (FHFA 2010b, 3–4). Within the first year of the conservatorship, the FHFA adjusted its affordable housing goals to account for prevailing market conditions (Lockhart 2009). By the end of 2010, a new structure was in place, and the GSEs were required to meet four core single-family goals, one multifamily "special affordable" goal, and two related subgoals, on an annual basis (FHFA 2011, 97).

9. The FHFA revised the GSEs' executive compensation policies while the conservatorship created challenges for employee retention and hiring.

Through HERA, the FHFA had the power to review any decision affecting executive compensation and could amend GSE compensation practices as it saw fit[12] (FHFA 2009a, 84).

During the conservatorship, acting FHFA Acting Director DeMarco (who replaced Lockhart in September 2009) identified enabling the GSEs to retain and recruit talented executives as key to fulfilling his agency's mission as conservator (DeMarco 2011). Without competent executives, the two firms were at high risk of running into trouble yet again—an operational risk that could result in more losses and potentially add billions of dollars to the steep price taxpayers already had paid (DeMarco 2011).

Early in the conservatorship, the GSEs endured "key person risk" to their human resources (FHFA 2010b, 17–18, 41). FHFA officials argued that potential downsizing, possible dechartering, and general public scrutiny could have motivated executives to leave (FHFA 2010b, 17–18, 41). To offset its key person risk, the FHFA set out to adjust executive compensation policies to give talented executives more of an incentive to stay (FHFA 2010b, 17–18, 41).

After consulting with Treasury (including the Special Master for TARP Executive Compensation) and the boards of both firms, and retaining a private consulting firm (Hays Group) to serve as advisor, the FHFA instituted a three-pronged executive compensation policy at both firms (DeMarco 2011). FHFA designed the new system to both motivate high-performing executives to stay and curb the GSEs' pre-conservatorship excesses (DeMarco 2011). For example: FHFA prohibited the golden parachutes that were formerly promised to outgoing CEOs and other senior executives (DeMarco 2011). Although prior executive compensation policies included company stock, FHFA pivoted to a cash-only compensation scheme because regulators sought to prevent executives from taking excess risks to raise the low prices of their company shares (DeMarco 2011).

The new system provided for three components of executive compensation—(1) base salary, (2) deferred salary, and (3) performance-based incentives—and was modeled after policies put in place at "institutions receiving exceptional TARP assistance" (DeMarco 2011). Important aspects of these components are highlighted below:

- Except for a few top executives, maximum base salaries was set at $500,00—less than half of what they were prior to conservatorship.
- Performance-based compensation was determined using only two years of results given the lack of a clear long-term plan for the firms.
- Deferred salary was paid out a year after the base portion and was to be forfeited by officials choosing to leave before the year's deferred payments were due.

[12] These broad authorities over executive compensation were granted as part of the arrangement enabling Treasury to purchase GSE obligations. Like Treasury's purchasing authority, these powers were temporary and set to expire December 31, 2009. However, on a permanent basis, HERA gave the FHFA other powers over executive compensation, including the authority to withhold executive compensation and prohibit severance payments. For more information, see Sections 1113, 1114, and 1117 of HERA (Public Law 110-289).

- Deferred payments made up the largest portion of top executives' total compensation packages. (DeMarco 2011)

In March 2011, the FHFA-OIG published a report analyzing the executive compensation policies put in place at both entities and criticized the FHFA for its lack of formal enforcement of the new policies (FHFA-OIG 2011, sec. "At a Glance"). The report advised the FHFA to: (1) make information on GSE executive compensation more accessible to the public (and "more user-friendly") and (2) develop formal control mechanisms to better enforce the entities' compliance with the new policies (FHFA-OIG 2011, 20–22).

FHFA balanced the need to attract and retain qualified leadership with mandatory restrictions on executive compensation, which was a challenge for both the firms and their conservator. In 2019, audits by the FHFA-OIG found that FHFA's approval of senior executive succession planning at both firms had "acted to circumvent the congressionally mandated cap on CEO compensation" (FHFA-OIG 2019a, 1–4; FHFA-OIG 2019b, 1–5).[13] The firms disagreed with the auditor's conclusions (FHFA-OIG 2019a, 1–4; FHFA-OIG 2019b, 1–5).

10. After enacting the conservatorship, the FHFA maintained transparency.

The FHFA has used plans, reports, and scorecards to disseminate information and increase public transparency regarding the conservatorships. On December 15, 2008, the FHFA released its first annual performance plan, for fiscal year 2009. The plan outlined the FHFA's objectives for the GSEs and detailed how it would use its resources to achieve those objectives (FHFA 2008e). Beginning in 2010, the FHFA also released a quarterly Conservator's Report on the Enterprises' Financial Performance, which summarized the fiscal health of both enterprises under conservatorship; the report lasted through the first quarter of 2013 (FHFA 2013). In 2012, the FHFA began to release an annual scorecard, which was designed to make the FHFA's duties and objectives more transparent for the public (FHFA 2012b; FHFA 2021). The FHFA also continued the practice of publishing the GSEs' annual examination results within the annual reports to Congress.

Through its regular reports, the FHFA identified at least two reasons for governing the GSEs transparently: (1) to increase public confidence in the GSEs and foster secondary mortgage market activity, and (2) to inform taxpayers FHFA's efforts to prevent foreclosure (FHFA 2008d, 137–46; FHFA 2009b, 61–62). In addition, DeMarco, who replaced Lockhart in 2009 as FHFA acting director, acknowledged that taxpayer funds kept Fannie Mae and Freddie Mac in operation (DeMarco 2010, 3). For this reason, DeMarco pledged to outline how the FHFA had limited, and would continue to limit, GSE losses (DeMarco 2010). Additionally, as the GSEs by their size were systemic in nature, many investors around the world were paying attention to developments with respect to the conservatorships (Paulson 2010, 77–78).

III. Evaluation

W. Scott Frame et al. (2015) argue that the conservatorships succeeded as emergency interventions successfully stabilizing the GSEs (30). First, the intervention prevented agency debtholders and MBS holders from experiencing losses at a time when such institutions were already being challenged to navigate the worsening crisis, shielding the vast number of counterparties from negative impacts and containing the GSEs' weaknesses from bringing

[13] See FHFA-OIG 2019a for the latest report on Fannie Mae and FHFA-OIG 2019b for the latest report on Freddie Mac.

down the entire financial system (Frame et al. 2015, 26–27). In addition, a 2010 Congressional Budget Office (CBO) report claimed that, in general, replacing an implicit government guarantee with an explicit guarantee, as was done in the intervention, was likely to improve the liquidity of the GSEs' MBS by ensuring a more robust market by attracting a broader and more stable group of investors (CBO 2010, 17). However, the report also cautions that other countervailing factors must also be considered to gauge the true effect (CBO 2010, 17).

Second, the program allowed the GSEs to continue purchasing loans and issuing and guaranteeing MBS, which maintained the flow of funding and helped to stabilize the mortgage market (Frame et al. 2015).

Frame et al. (2015) note that the FHFA's focus on the financial health of the GSEs may have limited the overall mortgage supply; as the FHFA urged Fannie Mae and Freddie Mac to return defaulted mortgages to their originators or sellers, originators tightened underwriting standards (27–28). While stringent underwriting standards helped to reduce the GSEs' losses, they also shrank the supply of mortgage credit, which, Frame et al. (2015) argue, contributed to the market's slow recovery (27–28). In contrast, the Mortgage Bankers Association (MBA) contends that the FHFA's decision to abolish preferential underwriting standards facilitated small lenders' higher postcrisis market share of mortgage origination and refinancing (MBA 2017, 6). In addition, Winston Sale argues that the FHFA cut the GSEs' affordable housing goals to stabilize the market during the crisis (Sale 2009, 300–07).

Some scholars find that FHFA actions have weakened other sectors of the economy. Tara Rice and Johnathan Rose contend that the conservatorship weakened the balance sheets of banks exposed to GSE preferred shares (2016, 86). They argue that the FHFA's decision to suspend dividends on preferred shareholders harmed already struggling banks, particularly community banks, which held large quantities of GSE stock (Rice and Rose 2016, 86). Fifteen banks closed because of this decision, the authors suggest, and two more were forced to sell themselves (Rice and Rose 2016, 86).

From a governance and operational standpoint, several audits by the FHFA's Office of Inspector General found that the FHFA "can better accomplish its oversight mission by proactively exerting greater control over its conservator approval process" (FHFA-OIG 2012b, sec. "At a Glance"). OIG also found that FHFA did not properly monitor several components of GSE operations, which resulted in both companies taking inappropriate financial risks (FHFA-OIG 2012b, sec. "At a Glance"). For example, a 2015 audit noted that the FHFA lacked a formal review process for the GSEs' compensatory fee settlements and large mortgaging service transfers (FHFA-OIG 2015, 15–16). The OIG also found that the FHFA did not have an apparatus to measure properly the GSEs' performance levels or a system to monitor all company operations (FHFA-OIG 2015, 15–16). In 2014, for instance, the FHFA did not detect that Fannie Mae and Freddie Mac had over-reimbursed their lender-based insurance servicers by approximately $159 million ($89 million for Fannie Mae and $70 million for Freddie Mac) (FHFA-OIG 2015, 16).

Other factors cited by the OIG and the FHFA that have impacted the efficacy of the conservatorship:

- The unique size of the GSEs, which were factors larger than any other entity to have been previously resolved by the government;
- The unique nature of Fannie Mae and Freddie Mac as GSEs, which presented operational challenges and limited the conservator's exit strategies;

- The fact that the FHFA was a newly established agency, which at the time of the conservatorship was forming itself;
- Significant turnover of GSE personnel, particularly at the management levels, despite retention efforts; and
- Tensions between the FHFA's role as regulator and conservator. (FHFA-OIG 2012a, 26–33)

Scholars generally find that the conservatorship has been unsatisfactory with respect to the longer-term objective of resolving the GSEs' structural issues and removing the enterprises from conservatorship (Frame et al. 2015, 27–30). Despite the government's intention to use the conservatorship temporarily, they remain in effect more than 12 years later.

While the GSEs continue to operate under conservatorship, Congress has yet to resolve the longer-term questions of how to terminate the conservatorships or what would be a new form for the entities (Frame et al. 2015, 30). The FHFA cannot discharge the GSEs from conservatorship without Treasury's approval, and all parties seem to agree that releasing the GSEs from the conservatorship in their current form, with their quasi-public/private hybridity and implicit government guarantee intact, would not be ideal (FHFA-OIG 2012a, 31–32). It is unlikely that the conservatorships will end until Congress agrees on what form the entities should have upon release from the FHFA's control (FHFA-OIG 2015, 6).

Despite these views, Jester et al. are of the opinion that enacting the conservatorships without developing a plan to exit them was entirely appropriate at the time, as the Treasury was focused on stemming the crisis rather than solving the broader policy issues that had helped to instigate the GSEs' demise (Jester et al. 2018, 16–17).

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V. Key Program Documents

Summary of Program

Christopher Dickerson to James B. Lockhart: Proposed Appointment of the Federal Housing Finance Agency as Conservator for Fannie Mae (09/06/2008) – *Memo from Christopher Dickinson to James Lockhart that includes reasons for conservatorship and the background of the case.* https://ypfs.som.yale.edu/node/3373.

Christopher Dickerson to Daniel Mudd (09/04/2008) – *Midyear report that classifies Fannie Mae as critically undercapitalized, which would give FHFA Director Lockhart discretion to take Fannie Mae into receivership (see Key Design Decision No. 2 for more information).* https://ypfs.som.yale.edu/library/fhfa-dickerson-ltr-fannie-mae-mudd-mid-year-letter.

Christopher Dickerson to Richard Syron (09/04/2008) – *Midyear report that classifies Freddie Mac as critically undercapitalized, which would give FHFA Director Lockhart discretion to take Freddie Mac into receivership (see Key Design Decision No. 2 for more information).* https://ypfs.som.yale.edu/library/fhfa-dickerson-ltr-freddie-mac-syron-mid-year-letter.

Fact Sheet: Questions and Answers on Conservatorship (09/07/2008) – *Defines conservator, its function, goals, and other generally asked questions.* https://ypfs.som.yale.edu/library/fact-sheet-questions-and-answers-conservatorship.

Implementation Documents

Conservatorship Strategic Plan 2012 – *Focuses on shrinking the GSEs' role in the mortgage market while continuing to provide an adequate supply to the market.* https://ypfs.som.yale.edu/library/strategic-plan-enterprise-conservatorships-next-chapter-story-needs-ending.

Conservatorship Strategic Plan 2014 – *Focuses less attention on reducing the size of Fannie and Freddie's market share.* https://ypfs.som.yale.edu/library/2014-strategic-plan-conservatorships-fannie-mae-and-freddie-mac.

Letter: Edward DeMarco to Committee on Banking, Housing and Urban Affairs and Committee on Financial Services (DeMarco 2010) – *Outlines the FHFA's commitment to scale back the GSEs' portfolios and establish a new process for product review.* https://ypfs.som.yale.edu/node/3433.

Legal/Regulatory Guidance

Emergency Economic Stabilization Act of 2008 (§1424) – *Mandates that the FHFA act to prevent foreclosures.*
https://ypfs.som.yale.edu/node/3365.

Housing and Economic Recovery Act of 2008 (HERA 2008, §1117) – *Legally authorizes the FHFA to take Fannie and Freddie into a conservatorship.*
https://ypfs.som.yale.edu/library/housing-and-economic-recovery-act-2008.

Press Releases/Announcements

Meeting the Challenges of the Financial Crisis (Lockhart 2009) – *Outlines actions taken by the FHFA, Treasury, and the Fed in the first six months of conservatorship.*
https://ypfs.som.yale.edu/library/meeting-challenges-financial-crisis

Statement by Secretary Henry M. Paulson, Jr. on Treasury and Federal Housing Finance Agency Action to Protect Financial Markets and Taxpayers (UST 2008) – *Treasury press release that announces the four-part rescue plan for the GSEs, including the conservatorship.*
https://ypfs.som.yale.edu/library/statement-secretary-henry-m-paulson-jr-treasury-and-federal-housing-finance-agency-action-0.

Statement of FHFA Regarding Contracts of Enterprises in Conservatorship (FHFA 2008a) – *Asserts that both GSEs will honor existing contracts and are able to enter new contracts.*
https://ypfs.som.yale.edu/library/statement-fhfa-regarding-contracts-enterprises-conservatorship.

The Appointment of FHFA as Conservator for Fannie Mae and Freddie Mac (Lockhart 2008) – *Outlines the weaknesses of OFHEO (former GSE regulator) and explains why the FHFA decided to enter Fannie and Freddie into a conservatorship.*
https://ypfs.som.yale.edu/node/3405.

Media Stories

As Crisis Grew, a Few Options Shrank to One (09/07/2008) – *Generally represents the media reaction and level of public understanding just after the conservatorship was enacted.*
https://ypfs.som.yale.edu/library/crisis-grew-few-options-shrank-one.

In Rescue to Stabilize Lending, U.S. Takes over Mortgage Finance Titans (Stephen Labaton and Edmund L. Andrews, 09/08/2008) – *Generally represents the media reaction and level of public understanding just after the conservatorship was enacted.*
https://ypfs.som.yale.edu/library/rescue-stabilize-lending-us-takes-over-mortgage-finance-titans.

Key Academic Papers

After the Deal: Fannie, Freddie, and the Financial Crisis Aftermath (Solomon and Zaring 2015) – *Explains the legal ramifications of the conservatorship, with particular emphasis on the 2012 amendment*.
https://ypfs.som.yale.edu/node/3364.

Effect of the Conservatorship of Fannie Mae and Freddie Mac on Affordable Housing (Sale 2009) – *Explains how the conservatorship affected the GSEs' affordable housing goals.*
https://ypfs.som.yale.edu/node/3420.

The Rescue of Fannie Mae and Freddie Mac (Frame et al. 2015) –*Addresses the causes of the conservatorship and evaluates the program's efficacy in the short run and the long run.*
https://ypfs.som.yale.edu/node/3415.

When Good Investments Go Bad: The Contraction in Community Bank Lending after the 2008 GSE Takeover (Rice and Rose 2016) – *Examines and evaluates the effects the conservatorship, mainly from the perspective of banks.*
https://ypfs.som.yale.edu/node/3419.

Reports/Assessments

2008 Annual Report to Congress (OFHEO 2008) – *Covers basic operations, market contractions, financial health of the GSEs, and risk. See subsequent years' reports below.*
https://ypfs.som.yale.edu/library/ofheo-2008-ofheo-report-congress.

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2015 (FHFA 06/15/2016).
https://ypfs.som.yale.edu/node/3394.

2016 (FHFA 06/15/2017).
https://ypfs.som.yale.edu/node/3395.

2008 Performance and Accountability Report (FHFA 2008d) – *Describes factors leading up to conservatorship, operations of the FHFA, goals of the FHFA, and management strategies. See subsequent years' reports below.*
https://ypfs.som.yale.edu/node/3375.

2009 (FHFA 2009b).
https://ypfs.som.yale.edu/node/3376.

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https://ypfs.som.yale.edu/node/3363.

GSE Reform: Creating a Sustainable, More Vibrant Secondary Mortgage Market (MBA 2017) – *Develops a new GSE structure that could be sustainable for the GSEs after the conservatorship.*

https://ypfs.som.yale.edu/node/4371.

Housing Finance at a Glance: A Monthly Chartbook [sic] (Urban Institute 01/2016) – *Includes annualized data on market indicators, GSE portfolios limits, mortgage originations, et cetera.*
https://ypfs.som.yale.edu/library/housing-finance-glance-monthly-chartbook.

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VI. Appendixes

Appendix A: Changes to Company Focus under Conservatorship

Topic	Before Conservatorship	As of February 26, 2009
Authority of Board of Directors, management and shareholders	• Board of Directors with right to determine the general policies governing the operations of the corporation and exercise all power and authority of the company, except as vested in shareholders or as the Board chooses to delegate to management • Directors with duties to shareholders • Board of Directors delegated significant authority to management • Shareholders with specified voting rights	• FHFA, as conservator, succeeded to all of the power and authority of the Board of Directors, management and the shareholders • The conservator has delegated authority to a newly constituted Board of Directors. The Board is required to consult with and obtain the consent of the conservator before taking action in specified areas. The conservator may modify or rescind this delegation at any time • Directors do not have any duties to any person or entity except to the conservator. • The conservator has delegated authority to management to conduct day-to-day operations so that the company can continue to operate in the ordinary course of business. The conservator retains overall management authority, including the authority to withdraw its delegations to management at any time • Shareholders have no voting rights
Structure of Board of Directors	• 13 directors: 12 independent plus President and Chief Executive Officer; independent, non-executive Chairman of the Board • Seven standing Board committees, including Audit Committee of which four of the five independent members were "audit committee financial experts"	• 10 directors: 9 independent plus President and Chief Executive Officer; independent, non-executive Chairman of the Board. Up to three additional Board members may be added by the Board subject to approval of the conservator • Four standing Board committees, including Audit Committee of which three of the four independent members are "audit committee financial experts"
Capital	• Statutory and regulatory capital requirements • Capital classifications as to adequacy of capital issued by FHFA on quarterly basis	• Capital requirements not binding • Quarterly capital classifications by FHFA suspended
Net Worth(1)	• Receivership mandatory under Regulatory Reform Act if FHFA makes a written determination that we have net worth deficit for 60 days	• Conservator has directed management to focus, to the extent it does not conflict with our mission, on maintaining positive net worth • Receivership mandatory if FHFA makes a written determination that we have net worth deficit for 60 days(2)
Management Strategy	• Maximize shareholder value over the long-term • Fulfill our mission of providing liquidity, stability and affordability to the mortgage market	• Directed to provide liquidity, stability and affordability in the mortgage market and immediately provide additional assistance to this market and the struggling housing market, and to the extent not in conflict with our mission, to maintain positive net worth • No longer managed with a strategy to maximize common shareholder returns • Focus on foreclosure prevention

Source: Fannie Mae 2008*b*.

Appendix B: Rescue Options (after the Passage of HERA)

	Nationalization	Receivership	Conservatorship
Legal authority	HERA	HERA	HERA
Overseer	Secretary of Treasury	FHFA director[1]	FHFA director[1]
Agency	Treasury	FHFA	FHFA
Discretionary appointment	Yes	Yes[2]	Yes[2]
Mandatory enactment	No	Yes[3] (1) GSE could not pay back debt (60 calendar days; 30 days if classified as "critically undercapitalized") (2) GSE assets were less than outstanding debt	No
Rights	Negotiated right to appoint directors and approve certain aspects of company as negotiated in contract providing for equity injection or liquidity assistance	All company operations; subpoena rights	All company operations; subpoena rights
Powers	Customary authority as negotiated: e.g., limits on payment of dividends, mergers, acquisitions, sale of assets, change in business, executive compensation, approval of conservatorship or receivership without Treasury approval	All powers of shareholders, officers, and directors with respect to the GSE and its assets	All powers of shareholders, officers, and directors with respect to the GSE and its assets
Main duties	Monitor company compliance with guiding contact	Prepare for liquidation/restructuring[4]	Maintain the GSEs' solvency and preserve their assets and property
Receivership option	Possible	N/A	Yes
Liquidation option	No	Yes	No
Bridge entity	Possible	Yes, if organizing a new enterprise	No

Rights and claims of stockholders and creditors to GSE assets	Subject to Treasury rights under governing contract. Usually conscribed	Terminates automatically, except for those related to payment, which falls to the FHFA director's discretion	At discretion of FHFA director
Option of parties to net, terminate, or liquidate assets	Possible	Yes (after 5pm the following day)	No
GSE assets and liabilities	Remain on GSE balance sheet if Treasury control is <80%. If Treasury interest is ≥80%, would be consolidated onto government's balance sheet.	GSE charters, assets in danger of default, and liabilities in danger of default would be transferred to a limited-life entity	Remain on GSE balance sheet
Treasury's emergency authority (expiring December 31, 2009)	Effects funding unless keepwell-type funding agreement	Effects funding unless keepwell-type funding agreement	Effects funding unless keepwell-type funding agreement
Termination	At discretion of US Treasury but subject to application of FHFA time periods	(1) Liquidation (2) Two years after the creation of the bridge entity (could be extended three more years)	(1) Receivership (2) At discretion of FHFA and Treasury

[1] *In consultation with the chairman of the Federal Reserve.*
[2] *FHFA director could take either GSE into conservatorship or receivership for any of the following reasons: (a) Assets were less than its obligations; (b) substantial dissipation of assets; (c) unsafe or unsound condition; (d) cease and desist orders; (e) concealment or refusal to provide the books, papers, etc.; (f) inability to pay obligations or meet the demands of creditors; (g) losses that would deplete capital, with little chance of recapitalization; (h) any legal violations; (i) by request of its board of directors or shareholders; (j) undercapitalization; (k) critical undercapitalization; and/or (l) money laundering.*
[3] *At the discretion of the FHFA director.*
[4] *In order to restructure the GSEs into new entities, the FHFA and Treasury required congressional approval to revoke the GSEs' charters. Until that point, the charter would remain in the bridge entity.*
Compiled by Daniel Thompson.
Sources for receivership and conservatorship: HERA 2008, Frame et al. 2015.
Sources for nationalization: Elliott 2009, Frame et al. 2015.