U.S. Department of the Treasury
Office of Public Affairs

Press Release: January 14, 2021
Contact: Treasury Public Affairs, (202) 622-2960

Treasury Department Blueprint on Next Steps for GSE Reform

On January 14, 2021, Treasury and the Federal Housing Finance Agency (FHFA) agreed to amend the Preferred Stock Purchase Agreements (PSPAs) to move Fannie Mae and Freddie Mac (the GSEs) toward capitalization levels that are consistent with their size, risk, and importance to the U.S. economy. These amendments to the PSPAs are consistent with objectives set forth in Treasury's September 2019 Housing Reform Plan.

The conservatorships of the GSEs were not meant to be indefinite. Before the GSEs can operate outside of conservatorship, however, significant issues remain to be addressed. Additional reforms will be necessary to implement a shareholder-owned governance structure that attracts private capital and promotes market discipline while fulfilling their charter mandates, including to promote access to mortgage credit throughout the nation.

Treasury and FHFA have been working to identify and assess strategic options to terminate the conservatorships and raise capital, including identifying any necessary legislation for reform of the GSEs. The PSPA changes today provide a roadmap for Treasury, in consultation with FHFA, to work to restructure Treasury's investments in the GSEs and to deliver a proposal describing this work to Congress by September 30, 2021. While Treasury will continue to evaluate potential administrative actions to end the conservatorships, Treasury maintains that Congress is best positioned to adopt comprehensive housing finance reform.

The work of Treasury and FHFA should seek to facilitate the GSEs' orderly exit from conservatorship, ensure Treasury is appropriately compensated, and permit the GSEs to raise third-party capital and make distributions as appropriate. Five key considerations should inform Treasury's continued work with FHFA. Addressing these issues will bolster reform, whether administrative or legislative, and should help achieve the bipartisan support necessary to make reform successful and durable.

- **Build GSE Equity Capital**: The GSEs should continue to build – or, when appropriate, raise – sufficient equity capital to facilitate their ability to operate through a severe downturn.

Consistent with the findings of the Financial Stability Oversight Council in September 2020, FHFA's recently finalized capital framework promotes taxpayer protection and the GSEs' ability to continue to meet their missions. The PSPA changes announced today will promote the GSEs' recapitalization by ending the net worth sweep and permitting the GSEs to retain capital up to their regulatory capital requirements under FHFA's new framework.

- **Determine GSE Capital Structure**: Third-party capital, raised in the equity markets, would expedite the GSEs' ability to meet their regulatory capital requirements. However, the current capital structures of the GSEs, and pending litigation related to the conservatorships and previous amendments to the PSPAs, complicate the GSEs' valuations and capital-raising processes. These issues must be addressed to facilitate the GSEs' capital restructuring and eventual exit from conservatorship. The changes announced today include a commitment for Treasury to work to address its interests in the GSEs in a way that facilitates the GSEs' orderly exit from conservatorship, ensures that Treasury is appropriately compensated, and permits the GSEs to raise third-party capital and make distributions as appropriate.

- **Set Commitment Fee for Ongoing Government Support**: Treasury supports legislative reform that authorizes an explicit, full faith and credit federal guarantee for the GSEs' mortgage-backed securities. Taxpayers should be compensated for this support consistent with the pricing for guarantees of similar risk. Today, taxpayers support the GSEs through $254 billion of remaining funding commitments under the PSPAs. Under the PSPA changes announced today, to compensate taxpayers for this support, Treasury and FHFA will determine and impose a periodic commitment fee once the GSEs have retained capital up to their regulatory capital requirements under FHFA's new framework.

- **Establish Appropriate Pricing Oversight**: The GSEs have significant pricing power over mortgage credit in the United States, due to their size and privileged access to federal support. Post-conservatorship, FHFA should continue its conservatorship-era practice of pricing oversight. This oversight should not seek to cap the GSEs' returns in a way that sacrifices safety and soundness in order to achieve policy objectives, or that forces taxpayers to bear undue risk for their ongoing support of the GSEs. Additionally, pricing oversight should seek to prevent the benefits of federal support from being used to compensate management or shareholders rather than supporting borrowers and renters. The PSPA changes announced today codify an important conservatorship-era GSE reform by prohibiting volume-based pricing discounts for loans delivered to the GSEs through their cash windows.

- **Assess Appropriate Market Concentration**: Further study is needed to determine the optimal number of mortgage guarantors to achieve the GSEs' mission. There are currently two chartered GSEs, but legislative reform could authorize FHFA to charter additional competitor guarantors to the GSEs and direct FHFA to re-charter each GSE on the same charter available to these potential competitors. A less concentrated secondary market could foster competition and promote innovation, with respect to not only the underwriting and pricing of mortgage loans, but also the services provided to lenders. However, given high barriers to entry, even with FHFA chartering authority, additional entrants may not be forthcoming. Therefore, appropriate consideration should also be given to whether consolidation of the GSEs' operations into a single entity would more efficiently fulfill their mission and promote the interests of stakeholders, including taxpayers.