FLORIDA LEGAL SERVICES, INC.

*Community Justice Project*
MIAMI ADVOCACY OFFICE
3000 Biscayne Boulevard, Suite 102
Miami, Florida 33137
Telephone: 305-573-0092
Fax: 305-576-9664

April 15, 2013



Mr. Edward DeMarco
Acting Director
Federal Housing Finance Agency
400 7th St., S.W.
Washington, D.C. 20024

Re: Housing Trust Fund

Dear Mr. DeMarco:

I am writing on behalf of the National Low Income Housing Coalition and the Right to the City Alliance, an alliance of nonprofit and advocacy organizations representing numerous low income residents desperately in need of affordable housing. I am writing to express their concern with your continuing failure to abide by the terms of the Housing and Economic Recovery Act of 2008 (HERA), specifically your failure to transfer the required share of the new business of the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac) to the Housing Trust Fund. As you know Section 1337 of Federal Housing Enterprises Financial Safety and Soundness Act, as amended by Section 1131 of HERA, 12 U.S.C. 4567, (hereafter "Section 1337 of HERA" or "the Act") requires the transfer of a portion of .042% of the new business of both Fannie Mae and Freddie Mac into the Housing Trust Fund. Your continuing failure to do so is a direct violation of the terms of the Act, results in the loss of many hundreds of millions of dollars dedicated by Congress to those most in need of housing and must cease immediately.

As you are aware, shortly after the two GSEs, Fannie Mae and Freddie Mac, were placed in conservatorship they were ordered by your agency to suspend any payments to the Housing Trust Fund under Section 1337 of HERA. The actual text of the suspension has not been released so I am unaware as to its exact wording. But regardless of its initial reasoning or bases for suspension, it can no longer be justified (if, indeed, it could ever have been justified) and must cease immediately. The manner of the suspension and its

continued implementation is contrary to the express provisions of the law and beyond any powers of conservatorship. On behalf of my clients I am therefore demanding the immediate cessation of the suspension and the repayment into the Housing Trust Fund of all of the suspended payments since, at a minimum, the first quarter of 2012.

Section 1337 of the Act provides that both GSEs shall:

> "set aside an amount equal to 4.2 basis points for each dollar of unpaid principal balance of its total new business"

and 65% of that amount is transferred to the Secretary of Housing and Urban Development under Sec. 1337(a)(1)(B)(i) to fund the Housing Trust Fund which was set up pursuant to Section 1338 of the Act. [1] Section 1338 then goes on to require that funds allocated to the Housing Trust Fund be utilized in grants to the States to "increase and preserve the supply of rental housing for extremely low and very low income families including homeless families", Sec. 1338(a)(1)(A), and "to increase homeownership for extremely low and very low income families," Sec. 1338(a)(1)(B).

I am aware that when initially placed in conservatorship, both GSEs required a significant infusion of capital. That capital was secured through the Senior Preferred Stock Purchase Agreements through which the U.S. Treasury made available a potential investment line of approximately $200 billion. According to the terms of the agreement, the GSEs were required to pay to the Treasury a yearly dividend of 10% of the amount of capital invested in the GSEs, which they have done. I am also aware that the GSEs were required several times during the past four years to access this investment line from the Treasury Department.

For reasons which are unclear but seem designed solely to ensure that the GSEs do not substantially recapitalize, the Preferred Stock Agreement was modified at the end of 2012 to change the "dividend" from 10% to the *entire earnings* of the GSEs. Because it is a "dividend" this payment in no way decreases the amount that the Treasury invested in the GSE stock, it simply dramatically increases the dividend to this one class of stock and substantially prevents the retention of earnings by the GSEs for recapitalization.

This change in the dividend prevents the development of any recapitalization since all earnings are being returned to the Treasury. More importantly, the amount of those additional earnings demonstrate that the mandated allocation could have been made to the Housing Trust Fund without impacting the GSEs in any way.

---

[1] Sec. 1337(e) provided for an initial additional set aside for the HOPE for Homeowners Program, 12 U.S.C.A. § 1715z-23, a program which terminated in September 2011. I therefore did not include those deductions in calculating the amount allocated to the Housing Trust Fund in 2012.

While your 2011 Annual Report to Congress provides precise older data for the calculation of the Housing Trust Fund payment, the 2012 Annual Report is not currently available. However, more recent 2012 data is available in the Securities and Exchange Commission filings by the GSEs. Unfortunately the data provided in the SEC filings does not precisely track the language of the statute but it is sufficient to permit approximate calculations. The Fannie Mae SEC filing for the year 2012, states that the new business activity for Fannie Mae in 2012 was approximately $900 billion and the new business activity for Freddie Mac in 2012 was approximately $531 billion. Thus the combined new business of the GSEs in 2012 was approximately $1.4 trillion. The .042% set-aside of $1.4 trillion is $590 million. Thus in 2012, approximately $590 million should have been made available under Section 1337, with approximately $382 million of that amount going to the Housing Trust Fund.

Those same filings note that in 2012 Fannie Mae paid over $11.6 billion to the Treasury under the now superseded 10% dividend agreement. However, those reports also note that Fannie Mae made over $17.2 billion in earnings that year and thus, had an additional $5.6 Billion in earnings (which will be paid into the Treasury in the future) far more than is necessary to fund the entire Housing Trust Fund payment for that year. While we believe the actual amount of the contribution to the Trust Fund would be higher, the above calculation amply demonstrates that the payment into the Trust Fund would not impact the operation of the GSEs in any way.

While the propriety of your decision to minimize the recapitalization of the GSEs is beyond the concerns raised by my clients, they do object strongly to its implementation which will result in the diversion of funds clearly appropriated by Congress to the Housing Trust Fund. Again, as the figures in the SEC filing demonstrate, following the law and funding the Housing Trust Fund would not impact the balance sheet of the GSEs at all but rather simply reduce the amount paid to the Treasury by the amount provided to the Housing Trust Fund.

I am aware that Section 1337(b) provides that under certain circumstances the payments may be temporarily suspended based on narrowly defined findings made by the Director of the FHFA. I do not believe that that Section supports your decision to suspend payments to the Housing Trust Fund. Under Section 1337(b) the Director can only *temporarily* suspend payments to the Housing Trust Fund and then *only* if the Director finds that such allocations:

(1) are contributing or would contribute to the financial instability of the enterprise;
(2) are causing or would cause the enterprise to be classified as undercapitalized; or
(3) are preventing or would prevent, the enterprise from successfully completing a capital restoration plan under Section 1369C.

First, I can find no evidence that the actual required findings were made by you, as the Director of the FHFA. The SEC filings by the GSEs repeat the permissible statutory bases for a suspension and then simply state that the GSEs were instructed by your

agency to suspend the payments. The only mention of the suspension in the reports to Congress is two sentences in the 2008 report which state:

"Consistent with its responsibilities, FHFA suspended Enterprise contributions to the Housing Trust Fund in view of the Enterprises' losses and required draws on the Treasury Department's Senior Preferred Stock Purchase facility." Report to Congress 2008 at p.8

and

"[I]t was not in the Enterprises' best interests to begin setting aside money for the Housing Trust and Capital Magnet funds as required by Section 1337 of the Federal Housing Enterprises Financial Safety and Soundness Act of 1992, as amended." Report to Congress 2008 at p.81.

Neither these two statements nor the description of your instructions to the GSEs conform to the findings required by Section 1337. First, they are not *temporary* nor has the suspension been *temporary*. Section 1337 recognizes that the status of the GSEs is not static and thus requires that any suspension be *temporary*. In addition, they are demonstrably unsupportable given the situation of the GSEs over the past year and a half. During that time, it would simply not be rationally possible to find that payments into the Trust Fund could "contribute to the financial instability of the enterprise." As demonstrated above, the GSEs in 2012 had many times more in earnings than they were required to pay into the Trust Fund. Even after the change in the dividend calculation, reducing the amount paid into the Treasury could not possibly affect the financial stability of the GSEs. Nor could there be a finding that the payments impact the ability of the GSEs to recapitalize – the second and third potential findings. The change to the dividend agreement with Treasury in 2012 reflects *your* decision to substantially prevent their recapitalization. Thus, payment into the Trust Fund of the amount required by the statute will simply reduce the amount paid to Treasury, but it will not in any way impact the internal bureaucratic decision to prevent recapitalization.

My clients have requested that I pursue this claim to a final resolution. I am aware of the limitations on obtaining court review of the decisions of the conservator. However, I do not believe they should limit review of this decision. The only person authorized to suspend payments under the statute is the Director, not the conservator, and thus the limitation should not operate to prevent review of the Director's findings or decision. Moreover, to the extent that your agency, as the conservator, usurped the statutory power of the Director without separate findings by the Director, it is a direct violation of the statute. In *Leon County, Florida et al. v Federal Housing Finance Agency, et al.*, 700 F.3d 1273 (11th Cir. 2012); the plaintiffs alleged that the actions of the FHFA violated certain requirements of the law. The Eleventh Circuit determined that the challenged

policy was an action of the conservator which is not subject to judicial review. However, the court went on to state:

> The FHFA cannot evade judicial scrutiny by merely labeling its actions with a conservator stamp. Congress did not intend that the nature of the FHFA's actions would be determined based upon the FHFA's self-declarations because the distinction between regulator and conservator would be one without a meaning or effect. Moreover, "if the FHFA were to act beyond statutory or constitutional bounds in a manner that adversely impacted the rights of others, § 4617(f) would not bar judicial oversight or review of its actions." *In re Fed. Home Loan Mortg. Corp. Derivative Litig.*, 643 F.Supp.2d 790, 799 (E.D.Va.2009) (citation omitted), *aff'd sub nom. La. Mun. Police Emps. Ret. Sys. v. Fed. Hous. Fin. Agency*, 434 Fed.Appx. 188 (4th Cir.2011) (per curiam). With that concern in mind, we must consider all relevant factors pertaining to the directive to determine whether it was issued pursuant to the FHFA's powers as conservator or as regulator. These would include, for example, its subject matter, its purpose, its outcome, and whether it involves a matter in which public comment might be relevant, appropriate, useful or intended by Congress.
>
> *Id.* at 1278.

*See also Town of Babylon v. Federal Housing Finance Agency*, 699 F.3d 221 (2d Cir. 2012). *County of Sonoma v. Federal Housing Finance Agency*, --- F.3d ----, 2013 WL 1130925 (9th Cir. 2013). That same standard as applied to the present case justifies court review. The GSEs have a preexisting statutory obligation to make the payments to the Housing Trust Fund. Pursuant to Section 1337, only you, acting as the Director, had the power to suspend those payments and then only after making certain findings. The GSEs did not have authority to suspend those payments on their own. The conservator only assumes the powers held by the entity itself. *Sharpe v. F.D.I.C.*126 F.3d 1147 (9th Cir. 1997) *abrogated in part on other grounds by McCarthy v. FDIC*, 348 F.3d 1075 (9th Cir.2003) (The conservator only assumes the powers held by the entity itself.) It would follow that the conservator in this case did not have the power to suspend payments. Therefore, if it was the conservator's action alone it was contrary to statute and thus, pursuant to *Leon County*, *supra*, subject to review. If you, as the Director, actually made the findings required by statute, the propriety of those findings would not be precluded from review by 12 U.S.C. 4617(f), since you were acting as Director not as conservator. Thus I do not believe the limitations on judicial review prevents courts from intervening to prevent a violation of the statute.

The loss of these hundreds of millions of dollars will prevent housing for literally tens of thousands extremely low income households each year these funds are withheld. (The White House conservatively estimates 16,000 extremely low income families per year could receive housing with every $1 billion in the Housing Trust Fund.) The Housing Trust Fund program was specifically designed to direct funds to the lowest income

households and to leverage other funding so as to greatly expand its impact. Your refusal to release these funds, even if eventually reversed, will prevent the development of this desperately needed housing precisely when it is most needed.

Thus my clients must demand that you immediately suspend any additional payments to the Treasury until you have determined the amount owing to the Housing Trust Fund and further immediately calculate and pay into the Housing Trust Fund the amounts required by Section 1337 for, at a minimum, the first through fourth quarter of 2012 and all time periods thereafter. My clients have requested me to not take any further action until April 30, 2013 to provide you with sufficient time to bring your conduct in line with the statute.

Thank you for your attention to this matter. I look forward to hearing from you.

Sincerely,

Charles F. Elsesser Jr.
Attorney at Law

cc: The Honorable Jacob Lew, Secretary of the U.S. Treasury
The Honorable Shaun Donovan, Secretary of the U.S. Department of Housing and Urban Development
Gene Sperling, Director, National Economic Council, The White House
Cecelia Muñoz, Director, Domestic Policy Council, The White House