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United States Senate
Committee on Banking, Housing and Urban Affairs

Hearing on
Housing Finance Reform: Powers and Structure
of a Strong Regulator.

November 21, 2013

Chairman Johnson, Ranking Member Crapo, and Members of the Committee, thank you for inviting me to testify on the proposed powers of the regulator and the regulatory structure for the secondary market for housing loans. I have represented many clients in the private sector and the public sector in the nearly 30 years that I have worked on housing finance issues, but my comments today are my own views and are not intended to reflect the views of any of my current or former clients. My views expressed today draw upon my experience with financial institution regulatory agencies, both as a lawyer exposed to the savings and loan crisis two decades ago (where I was involved by first representing the regulators as they pursued various wrongdoing in the western United States and then as counsel to this Committee) and then my recent experience as counsel to the Financial Crisis Inquiry Commission and its review of the housing finance problems at our largest financial institutions.

I commend the Committee for undertaking this hearing, and the other hearings related to the permanent replacement of Fannie Mae (Fannie) and Freddie Mac (Freddie) with a new structure to support housing finance through a vibrant secondary market that relies more on private capital, and presents less risk to the American taxpayer. The prior model of Fannie and Freddie, investor owned companies where the senior managers were given financial incentives to take outsized risks, was deeply flawed public policy. The fact that Fannie and Freddie operated for almost their entire existences without a regulator with the strong supervisory powers like the Federal Housing Finance Agency (FHFA) only exacerbated those flaws. However, uniform standardization in home loans and a national platform for issuing securities provided an efficient means for millions of American homeowners to access affordable credit. Before the advent of what effectively became a national market for mortgage loans, there was a lasting and sustained rate differential on mortgage loans in various regions across the country.[1] The development of a national mortgage market was a significant improvement for rural states that were located far from the centers of capital in the United States.

The Committee should analyze both what was good about Fannie and Freddie for American homeowners, and what was bad about Fannie and Freddie for American taxpayers. I urge the Committee to continue its thoughtful and deliberate approach to this problem because the issues involved are complicated, and the outcomes could have a profound impact on the U.S. economy for generations to come. In the fall of 2008, Congress was faced with a crisis and immediate action was needed to stabilize the financial system. As a result of the efforts of the FHFA to stabilize the operations of the conservatorships of Fannie and Freddie, currently we are not in a crisis, and Congress has the luxury of time. Finding the right solution is more important than getting a quick solution.

[1] Indeed, in 1982 the rate differential between the state with the highest mortgage rate and the lowest mortgage rate spiked up to 600 basis points. "The Future of Housing Finance: Who Will Qualify?", Rosen Consulting Group and Ranieri Partners, October 25, 2013, p. 5. Available at http://www.ranieripartners.com/latest-news

In framing my remarks today, I will use S. 1217 as a point of departure. The introduction of S. 1217 by Senator Corker and Senator Warner and their bipartisan cosponsors represents an important first step in raising the issue of creating a permanent replacement for Fannie and Freddie. I do, however, believe there are ways in which the structure proposed in that legislation, especially the regulatory structure, could be improved.

Today, I will present my views with respect to the legislation's impact on safety and soundness supervision of the newly proposed Federal Mortgage Insurance Corporations (FMIC), and the various private entities and businesses in the housing finance sector that could be involved in the securitization process. In looking at S. 1217, I see two primary structural issues for the Committee to consider regarding the regulatory agency:

> First, and most importantly, what is the appropriate level of safety and soundness supervision of the various private entities, such as the mortgage originators, mortgage servicers, and private mortgage insurers, that will be in business with the FMIC?
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> Second, is it sufficient that the FMIC be run by a board of government appointees, or should the FMIC's business of granting a government guarantee on mortgage securities be subject to safety and soundness oversight by a separate federal agency?

<u>Safety and Soundness supervision of private business partners of the FMIC</u>

Under S. 1217, the FMIC would be created with multiple responsibilities, including the power to establish a Mortgage Insurance Fund to charge fees to be deposited in a fund, and to issue a full faith and credit federal guarantee to cover losses on securities insured by private parties, after application of a first loss position by either investors or a guarantor. The FMIC would be governed by a five member board of presidential appointees, subject to Senate confirmation. The FHFA, which has enforcement powers similar to the federal banking agencies, would be abolished.

Given that a federal credit guarantee is involved, it is critical that any supervision of the private entities participating in the securitization be in the hands of a strong, independent federal regulator. During the savings and loan crisis of the 1980s, the country learned the hard way that when providing access to federal guarantees, it may not be prudent to rely on state legislatures and state regulatory officials, with weak federal oversight. In the 1980s, Congress allowed states wide authority to set the investment rules for state chartered savings and loans, but allowed them to have access to federal guarantees for deposit insurance.[2] Before Congress slammed that door

[2] Pub. L. No. 97-320 (Oct. 15, 1982).

shut in 1989,[3] weak state supervisors in just a few states loosened the rules and let a torrent of new operators acquire charters, or buy up existing companies, and then the American taxpayer eventually picked up the tab for $124 billion of losses.[4] State regulators may be appropriate for certain entities, such as companies involved in the life insurance business that are supported by state guarantee funds, but when the fund backing any losses is a federal fund, and the American taxpayer has exposure, prudence demands that a strong federal regulator be in charge.

The legislation establishes a process for the FMIC to establish standards for approving private parties doing business with the FMIC. The private parties participating in the securitization process and subject to government oversight are limited in the legislation to private mortgage insurers, mortgage servicers, bond issuers, and bond guarantors that do business facilitated by the FMIC. The FMIC is given the power to suspend or revoke the authority of those entities to do business with the FMIC, and the power to adopt a civil money penalty process.

I believe this portion of the legislation can be improved substantially by allowing a federal agency with safety and soundness duties more like the federal banking agencies to supervise the activities of the private parties participating in the securitization process.[5] I recommend that three specific changes be considered by the Committee.

First, I would broaden the definition of the private parties in the securitization process that are subject to government oversight, and increase the flexibility of the federal agency to define by regulation the key mortgage securitization participants that are subject to its authority. The specified entities in the legislation—private mortgage insurers, mortgage servicers, issuers[6] and bond guarantors-- should be expanded in the statutory language, and the statute should expressly grant that federal agency the authority to adopt regulations in the future further expanding the list. For example, it is my view that mortgage originators, due diligence firms, and trustees of the securitization trusts holding the mortgages that are underlying the guaranteed securities should be subject to oversight by the federal agency. Securitization trustees occupy a key position from which they could protect investors, but often have little accountability for their actions, and in the past have not shown great vigor in exercising their potential powers. The

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[3] Pub. L. No. 101-73 (Aug. 9, 1989).
[4] "Fuzzy Numbers Lead to Prickly Politics", Steve Sloan, Congressional Quarterly Weekly, (Oct. 30, 2010).
[5] In my view, the abolition of the FHFA is unnecessary and would add further complications to the transition to a system where Fannie and Freddie are replaced permanently with a new organization. My references to a federal agency in this section could mean the FHFA if the Committee determined its abolition was unnecessary and made it the safety and soundness supervisor for both the FMIC and the Federal Home Loan Banks. If the Committee determines not to abolish the FHFA, it also could consider whether the single director should be replaced with a three person board.
[6] I believe the Committee should consider an alternative structure where the FMIC itself is the sole issuer of mortgage backed securities. The primary goal in issuing these securities with a federal guarantee is to have a low cost of funds that is passed onto individuals with home mortgages at a low markup. The structure of the system proposed in the bill would have multiple issuers, and because of the liquidity premium for smaller outstanding issues, such bonds would undoubtedly have a higher interest rates, and a larger bid ask spread, than bonds issued by one large issuer. The FMIC could act as the sole conduit for entities that desire to issue securities, much as the Office of Finance acts as the sole issuer for all the Federal Home Loan Banks. 12 C.F.R. 1273.

federal agency should have the power to take actions that can influence all the key participants in the mortgage securitization market place.

If this new secondary market structure is meant to last, then the federal agency must be given the power to adapt to changing times and changing financial markets. Otherwise, over time, the agency will be left writing rules applicable to horse drawn buggies as Google powered self driving cars cruise the freeways.

Second, I would grant the federal agency the express power to examine and inspect the books and records of all the entities that participate in the mortgage securitization, and afford the agency examiners who do that inspection the same powers and protections that are afforded to national bank examiners.[7] Federal bank examiners today essentially have unfettered access to all the materials and documents available to the senior managers of the banks they inspect, even materials that are subject to litigation privileges. The federal examiners need access to this information, which is often in the form of confidential reviews and reports, to fully inform their views, and the private parties need to know that divulging such information does not impair existing litigation privileges.

Third, the proposed legislation grants the FMIC the power to set standards for private parties and suspend them from doing business with the FMIC if they violate those standards. That is a blunt weapon. Instead of relying upon a concept of program suspension for private parties that violate the agency's standards, supplemented with a general grant of power to create a civil money penalty system, I would create an express enforcement system modeled after the federal banking laws, with the power to take action for violations of law and regulation, and also for engaging in unsafe and unsound practices. That final phrase, "unsafe and unsound practices", is a key weapon in the arsenal of the bank regulatory agencies. It was added to the federal banking laws in 1966 at the request of the federal banking regulators and allows them to address developing practices and conditions.[8] The remedies available to the federal agency in enforcing its authority should include cease and desist powers,[9] temporary cease and desist powers,[10] the power to take action against individuals (referred to as institution affiliated parties) to prohibit such individuals from engaging in further business related to the Mortgage Insurance Fund,[11] and

[7] 12 U.S.C. 481. The relevant criminal code provisions in Title 18 of the United States Code should also be amended.

[8] The broad context of this term was set forth in testimony during legislative hearings that has been accepted by courts as a guiding principle. "Generally speaking, an 'unsafe or unsound practice' embraces any action, or lack of action, which is contrary to generally accepted standards of prudent operation, the possible consequences of which, if continued, would be abnormal risk of loss or damage to an institution, its shareholders, or the agencies administering the insurance fund." Financial Institutions Supervisory Act of 1966, Hearings on S. 3158 before the House Committee on Banking and Currency, 89th Cong., 2d Sess. At 49-50 (1966)(statement of Federal Home Loan Bank Board Chairman Horne).

[9] 12 U.S.C. 1818(b).

[10] 12 U.S.C. 1818(c).

[11] 12 U.S.C. 1818(e), (f) and (g).

a civil money penalty system with express amounts and tiers similar to those of the federal banking agencies.[12]

Cease and desist authority allows a federal regulator to take more precise action than relying upon the blunt action of causing the private business to be barred from doing any further work on mortgage securitizations that have the benefit of a federal guarantee. Certainly there would be instances in which the offenses do not warrant causing the private entity to be barred from all further work, but nonetheless call for remediation. And, as is the common practice with the federal banking regulators, instead of actually using the statutory power to issue a cease and desist order, in most instances a consent agreement would be negotiated between the private business and the federal agency setting forth the scope of the appropriate remedial action. This is a much more effective tool than relying upon the brinksmanship of threatening to bar the private party from engaging in business with the entity providing the federal guarantee.

<u>Separation of the Business of Guaranteeing the Securities and Supervising the Entity that Makes Guarantees</u>

S. 1217 grants the FMIC the power to issue the guarantee of mortgage securities and does not subject the FMIC to supervision by a separate safety and soundness regulator. Instead, the legislation creates a board of directors composed of Presidential appointees, and relies upon them to be self policing when extending a government guarantee on mortgage securities. I am troubled by this framework.

A review of the history of the housing finance system shows why this proposed approach might be troublesome. The recent crisis is not the first time that the housing GSEs have faced significant financial troubles. By 1981, Fannie Mae, which had a Chief Executive Officer that was a presidential appointee, and presidentially-appointed members serving on its board of directors, was insolvent on a market value basis.[13] Fannie Mae continued to generate cumulative net losses in 1981, 1982, 1984 and 1985.[14] At that time, Fannie Mae had no independent safety and soundness supervisor with strong enforcement tools; its operations were subject to "light touch" supervision by HUD until Congress created the Office of Federal Housing Enterprise Oversight in 1992.[15] While the specific manner in which Fannie Mae blew a hole in its balance

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[12] 12 U.S.C. 1818(i)(2).

[13] "Regulating Housing GSEs: thoughts on institutional structures and authorities," Lawrence J. White and Scott W. Frame, Federal Reserve Bank of Atlanta Economic Review, April 2004, fn. 6.

[14] "Government Sponsored Enterprises: The Government's Exposure to Risks," General Accounting Office, GGD-90-97 (Aug. 1990), p.9. Freddie Mac, which in the early 1980s was a subsidiary of the Federal Home Loan Banks and was not investor owned like Fannie Mae was at that time, and Freddie "was consistently profitable throughout the 1980s . . . [avoiding] most interest rate risk . . . and . . . [with] credit losses . . . lower than industry average." Id. at 8. However, Freddie Mac was not subject to stringent safety and soundness standards, and operated with razor thin capital (0.62 percent of its assets and outstanding MBS at the end of 1989). Id.

[15] Federal Housing Enterprises Financial Safety and Soundness Act of 1992, Pub L. No. 102-550 (Oct. 28, 1992) Title XIII. Even then, this new agency was hobbled with statutory restrictions giving it far less authority (compared to the federal banking regulators) to supervise the safety and soundness of Fannie Mae and Freddie Mac.

sheet back in the 1980s (holding long term assets in portfolio that it financed with short term debt) would not be available to the proposed FMIC, the similar structural incentives are in place for excessive risk taking. History has shown that merely having a presidentially appointed executive and some presidentially appointed directors did not restrain that organization's push to zealously expand its business.

In the 1980s, there was no strong independent federal regulator to restrain the Freddie or Fannie business managers' zealous push to expand their book of business. As the GAO said in the early 1990s, the multiple roles given to HUD created an inherent conflict of interest.[16] HUD was a promoter of housing, yet it had a role as safety and soundness regulator of Fannie and Freddie. Multiple conflicts arise in this scenario. HUD's conflict at that time is evidenced by its response to the 1990 GAO report, in which it argued that Fannie's and Freddie's miniscule then existing capital (each had less than 1 percent of capital to back its assets and outstanding mortgage backed securities) was more than enough to meet any stringent capital standards.[17]

In another context, the GAO has previously noted that making operational business decisions and being an arms' length safety and soundness supervisor are incompatible. In 1993, GAO issued a report noting that the Federal Housing Finance Board still had several governance functions with respect to the operations of the Federal Home Loan Banks (such as approving budgets and dividends), and was also charged with being the safety and soundness supervisor of the Federal Home Loan Banks.[18] GAO recommended that safety and soundness supervision should be done by a single independent regulator, and that the governance decisions should be given to the Federal Home Loan Banks and their shareholders.[19] Congress wisely followed the advice of

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[16] "Government Sponsored Enterprises: The Government's Exposure to Risks", General Accounting Office, GGD-90-97 (Aug. 1990), p. 11.

[17] "Government Sponsored Enterprises: The Government's Exposure to Risks", General Accounting Office, GGD-90-97 (Aug. 1990), p. 152.

[18] "Federal Home Loan Bank System: Reforms Needed to Promote its Safety, Soundness and Effectiveness," General Accounting Office, GGD-94-38 (Dec. 1993).

[19] Id. at 4-5. Although my testimony today focuses on the FMIC and the supervision of the various private parties with which it will do business, I also would suggest that having the FMIC be responsible for running the Mortgage Insurance Fund, and being the safety and soundness supervisor of the Federal Home Loan Banks raises some conflicts that are parallel to the conflict that were in place when the Federal Home Loan Bank Board was responsible for running the FSLIC insurance fund (that insured savings and loans deposits), and supervising the Federal Home Loan Banks. When the FSLIC was running low on funds to close troubled savings and loans, it lowered collateral standards applicable to FHLBank loans to savings and loans, and pressured them to make loans that they would not otherwise make. I believe the Committee should consider allowing the FHFA to continue to exist, and act as the safety and soundness supervisor for the FMIC, the private parties involved in FMIC securitization, the Federal Home Loan Banks, and its Office of Finance. The Office of Finance issues bonds on behalf of all the Federal Home Loan Banks, and is subject to FHFA enforcement actions because Congress defined it as an entity affiliated party. 12 U.S.C. 4502(11). A graphic depiction of the current regulatory system, the system proposed by S. 1217, and an alternative structure are set forth in Exhibits A, B and C to this testimony.

If the Committee were to adopt the alternative approach, it could consider whether the best way to structure the FMIC's guarantee operations would be as a government corporation (the GNMA model), or as a member owned cooperative (the FHLBank model). The primary benefit of the industry cooperative model is that it requires the industry to have "skin in the game" in the form of stock purchased in the cooperative in order to do business with

GAO, and later eliminated the governance powers that the FHFB had previously held.[20]

In the current context, an organization charged with ensuring the availability of mortgage credit to the maximum extent possible will want looser underwriting standards so more families can have access to housing; a safety and soundness regulator will want tighter underwriting standards to prevent losses during economic downturns. This proposed structure puts the FMIC in an inherent conflict of interest. In running the business of guaranteeing securities and setting the standards for the private parties involved in the securitization, they would naturally want the business to expand as much as possible to provide as many benefits to as many American households as possible; a safety and soundness regulator, on the other hand, should want the standards to provide protection to prevent losses when an economic downturn occurs. This fundamental tension is why I believe the roles should be separated into separate organizations.

Some have suggested that the deposit insurance model, with a special purpose government backed corporation providing a guarantee of insured deposits should provide comfort to those considering the proposed model of the FMIC operating without independent oversight from a separate safety and soundness supervisor. To this I say please examine the results of such specialized deposit insurance systems that have been run by special purpose corporations in the housing finance system: there are some rather spectacular failures. The most famous of these, of course, is the Federal Savings and Loan Insurance Corporation, which collapsed for good in 1989, and caused an enormous loss for the taxpayers.

But the FSLIC failure was not an isolated incident. Into the mid-1980s there were several states that had state laws creating deposit insurance programs funded by assessments on state chartered housing lenders. By 1985, all but one of these programs had failed, or were closed before they failed.[21] Some of these were operated exclusively with state chartered thrift members on the board of directors,[22] and some had directors appointed by the state government.[23] But because none of them charged their members enough for their deposit insurance, they all failed.

Even the fiscal history of the FDIC should not give great comfort to those saying putting government appointed directors on the board of a governmental entity giving credit guarantees is sufficient protection in all contexts. At the end of 2009, the Deposit Insurance Fund managed by

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the cooperative. It is not clear to me that there would be enough critical mass of business for the mutual securitization company for small companies envisioned by section 215 of the proposed bill to ever begin operation.

[20] Pub. L. No. 106-102 (Nov. 12, 1999).

[21] "Mass. Thrifts to Seek U.S. Insurance," Laurie Cohen, Chicago Tribune (May 24, 1985), p. C1 (Ohio, Maryland, North Carolina, and Massachusetts deposit insurance systems were closed in 1985, and only the Pennsylvania Savings Association Insurance Corp. remained open). The Nebraska Depository Insurance Guaranty Corporation had declared bankruptcy in 1983. "After the Ohio bank run, extend federal insurance to all banks," R. Richardson Pettit, N.Y. Times (March 24, 1985), p. 2.

[22] The fund established by Ohio had all its directors elected by state thrifts. "The Ohio Deposit Guarantee Fund – The Ohio Alternative to FSLIC," Ronald Alexander, 15 Akron L. Rev. 431, 436 (1982).

[23] The ineffectual Maryland Savings-Share Insurance Corp., for example, had 3 of its board members appointed by the Governor of Maryland. "Toothless Watchdog Shares Blame," R.H. Melton and John Mintz, Washington Post, (Dec. 26, 1985) p. A1.

the FDIC had a negative balance of $20.9 billion.[24] One must question whether that negative balance would have been substantially larger but for the extraordinary steps taken in 2008 by Congress, the Federal Reserve and the FDIC to pump hundreds of billions of dollars into the financial system. Although the FDIC system of deposit insurance has been a dramatic success in protecting small savers and stabilizing the American banking system, there are issues that should cause the Committee to be careful in exporting that model into other areas. In the years leading up to the recent crisis, from 1996 to 2006, the overwhelming majority of banks paid nothing for their deposit insurance from the FDIC.[25] A former FDIC Chairperson noted in testimony before this Committee over a decade ago that the statutory model then in effect did not allow the FDIC to "price risk appropriately," and that underpriced deposit insurance premiums had a number of negative effects.[26]

The proposed legislation partially addresses this problem by setting reserve ratios for the new Mortgage Insurance Fund that appear to be floors, not caps, but I would go further and direct the federal agency to establish a meaningful minimum non-zero charge for the fees charged to purely private parties for the federal guarantee that applies even after the targeted reserve ratios have been met.

Conclusion

Because of the stability of the marketplace resulting from the conservatorships of Fannie and Freddie being overseen by the FHFA, Congress has the luxury of taking its time to get these issues right. In 1982, Congress first attempted to fix the problems of a broken housing finance system, and the struggling FSLIC, by expanding the powers of savings and loans. While accepted portfolio theory recognizes that diversification of investment classes can lower risk, the realities of the marketplace often steam roll theory. If those expanded powers had been limited by requiring them to be exercised only through acquisitions by existing commercial banks with experience in making those types of investments it might have worked. Instead, the law expanding savings and loan powers was exploited by a group of real estate developers who seized control of traditional savings and loans, operated under light touch supervision, and used them to fund their risky ventures. Congress back then certainly did not intend to invite rogue agents into the system, but flawed reliance on weak supervision created a perfect storm. The "cure" created by Congress in 1982 exacerbated the problem several fold, and the final cost to the federal government to make good on the insured deposits of failed savings and loans far

[24] "FDIC insurance premiums not likely to change soon, Gruenberg says," Ken McCarthy, SNL Bank and Thrift Daily (Oct. 9, 2013).
[25] In 2006, the FDIC adopted a premium for 2007 in which banks had to pay at least 5 basis points. "FDIC Fees: A 5-BP Floor and Most to Pay More," Joe Adler, American Banker (Nov. 3, 2006), p.1.
[26] Prepared Testimony of FDIC Chairperson Tanoue, United States Senate Committee on Banking, Housing and Urban Affairs, June 20, 2001. The FDIC Chairperson also noted that the FDIC's system was pro-cyclical, exacerbating downturns, because "premiums are volatile and are likely to rise substantially during an economic downturn when financial institutions can least afford to pay higher premiums." Subsequent legislation and actions by the FDIC have reduced, but not eliminated, those distortions.

exceeded the final cost to the federal government of the extraordinary measures taken under TARP.[27]

I am very concerned about the potential for a similar exacerbation of current problems. Certainly the existing problems that created insolvencies at Fannie and Freddie are significant and demand a permanent solution, but let the cure not be worse than the disease. Some type of federal backing of the mortgage market appears to be a necessity if Congress desires American homeowners to have continued access to 30-year fixed rate mortgages at an affordable cost.[28] But great care must be taken in designing a system where as yet unknown private parties will have access to a federal guarantee. Whatever you design will be a huge magnet for those trying to exploit the system to make a quick profit and leave the taxpayers holding the bag.

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[27] Recent calculations indicate that net TARP outflows have been approximately $40 billion. See, http://www.projects.propublica.org/bailout/ . In constant dollars, in 2009 the cost of the savings and loan crisis was estimated at $293 billion. http://www.propublica.org/special/government-bailouts

[28] The 30 year fixed rate mortgage was first introduced by the FHA. "Private Risk, Public Risk: Public Policy, Market Development, and the Mortgage Crisis", Daniel Immergluck, 36 Fordham Urb. L. J. 447, 456 (April 2009). By 1970, FHA still accounted for 30 percent of single family loans. Id. at 457.

Exhibit A

Current Structure of Housing Finance System

Federal Housing Finance Agency

Examination Powers & Safety and Soundness Supervisor for Fannie, Freddie, the FHLBanks and FHLB Office of Finance

Fannie Mae

Owned by Public

Holds Assets in Portfolio

Purchases Mortgages from Public

Issues Securities to Public

Freddie Mac

Owned by Public

Holds Assets in Portfolio

Purchases Mortgages from Public

Issues Securities to Public

Federal Home Loan Banks

Owned by Members

Holds Assets in Portfolio

Makes Loans to Members

FHLB Office of Finance

Joint Office of FHLBanks

Issues FHLB debt securities to Public

Exhibit B

S. 1217 Proposed Structure of Housing Finance System

Federal Mortgage Insurance Corporation

Examination Powers & Safety and Soundness Supervisor of FHLBanks and Office of Finance

Sets Standards for Issuers and Others involved in Securitization of Guaranteed MBS

Guarantees MBS created by private parties through Mortgage Insurance Fund to extent loss exceeds first loss position of either private investor or private Bond Guarantor

Approved PMI Companies

Issues insurance on FMIC eligible mortgages where the Loan to Value Ratio exceeds 80 percent

Approved Issuers

Issues Covered Securities to Public with Guarantee from FMIC

Federal Home Loan Banks

Owned by Members

Holds Assets in Portfolio

Makes Loans to Members

Approved Mortgage Servicers

Services Eligible Mortgages underlying Covered Securities

Approved Bond Guarantors

Primary Guarantor on Cover Securities that stands in front of FMIC guarantee

FHLB Office of Finance

Joint Office of FHLBanks

Issues FHLB debt securities to Public

Exhibit C

Alternative Structure of Housing Finance System

<u>Federal Housing Finance Agency</u>

Examination Powers & Safety and Soundness Supervisor of FHLBanks, Office of Finance, FMIC and Private Parties involved in securitization

<u>Federal Mortgage Insurance Corporation</u>

Guarantees MBS created by private parties through Mortgage Insurance Fund to extent loss exceeds first loss position of either private investor or private Bond Guarantor

<u>Approved PMI Companies</u>

<u>Approved Issuers</u>

<u>Approved Bond Guarantors</u>

<u>Approved Mortgage Servicers</u>

<u>Approved Trustees</u>

<u>Approved Due Diligence Firms</u>

<u>Approved Originators</u>

<u>Federal Home Loan Banks</u>

Owned by Members

Holds Assets in Portfolio

Makes Loans to Members

<u>FHLB Office of Finance</u>

Joint Office of FHLBanks

Issues FHLB debt securities to Public