FORDHAM UNIVERSITY SCHOOL OF LAW
140 WEST 62ND ST., NEW YORK, N.Y. 10023

Improving the Regulation of Fannie Mae, Freddie Mac, and the Federal Home Loan Banks

Statement of Richard S. Carnell

Before the Committee on
Banking, Housing, and Urban Affairs
United States Senate

February 10, 2004

SUMMARY

Structuring the Regulator

In designing a new agency to regulate government-sponsored enterprises ("GSEs"), Congress faces six fundamental questions. These questions relate to the agency's jurisdiction, mission, governance, resources, legal authority, and incentives. Structuring the agency so as to give its officers and employees a healthy set of incentives is crucial.

Congress should seek to avoid the sort of structural weaknesses under which the Office of Federal Housing Enterprise Oversight ("OFHEO") has labored since its creation. OFHEO is a small, hyper-specialized agency. Its only function involves overseeing the financial health of Fannie Mae and Freddie Mac, two huge firms with great political clout. It has overly narrow powers and uncertain funding. It is a bureau of the Department of Housing and Urban Development ("HUD"), which has no institutional commitment to safety and soundness and cannot afford OFHEO much protection against pressure from Fannie and Freddie.

The new agency should regulate Fannie Mae, Freddie Mac, and the Federal Home Loan Bank System. The agency should thus take over functions currently performed by OFHEO, the Federal Housing Finance Board ("Finance Board"), and HUD. Having the same agency regulate all three housing GSEs would have no significant disadvantages and would (1) make the agency more independent of the firms it regulates; (2) increase the agency's prominence in ways that should help it attract and retain capable staff; (3) permit economy and efficiency; and (4) facilitate greater consistency in GSE regulation.

In structuring the agency, the paramount goal should be to assure the agency's independence from the firms it regulates. Two possible governance structures offer the best prospects for maintaining such independence. First, making the agency an autonomous bureau of the Treasury Department. Second, placing the agency under a three- or five-member board consisting of one representative each from the Treasury and HUD plus either one or three appointed members nominated by the President and confirmed by the Senate.

The agency should have permanent funding, not dependent upon the appropriations process.

Current law unwisely denies OFHEO some of the safety-and-soundness authority long possessed by bank regulators, and provides weak "prompt corrective action" safeguards. The new agency should have authority to raise capital standards in light of experience. The GSE enforcement and prompt corrective action rules should be strengthened on the lines of their banking counterparts.

Congress should provide a receivership mechanism for dealing with a GSE if its liabilities exceed its assets and it cannot pay its debts as they become due.

The GSEs' Double Game

In managing their relationship to the federal government, the GSEs play an extraordinarily successful double game. They emphatically deny that they have any formal, legally enforceable government backing, leaving the impression that they have no government backing at all. At the same time, they work to reinforce the market perception of implicit government backing. In effect, the GSEs tell Congress and the news media, "Don't worry, the government is *not* on the hook"—and then turn around and tell Wall Street, "Don't worry, the government really *is* on the hook."

Properly Comparing Banks and GSEs

Fannie and Freddie wrongly argue that the federal government gives FDIC-insured banks benefits comparable to or greater than those it gives the two GSEs, and that the GSEs' success simply reflects their greater efficiency. The GSEs have lower overhead than banks because they do a different business than banks—a wholesale rather than retail business. Moreover, the government's perceived implicit backing of Fannie and Freddie actually tends to provide a greater net subsidy than FDIC insurance, for six structural reasons: (1) unlimited coverage of all GSE obligations; (2) no receivership mechanism; (3) no cross-guarantees to protect the taxpayers; (4) company-specific statutes that avoid the discipline of having to comply with the same rules as thousands of other businesses; (5) protection from effective competition; and (6) not having to pay fees or to provide public benefits that would impose significant costs on the GSEs' shareholders.

Systemic Risk

The housing GSEs are often characterized as "too big to fail"—meaning that the government would be forced to rescue them lest their failure unleash "systemic risk" that would harm the nation's financial system and economy. Yet such systemic risk is not inevitable; it results from human decisions. If investors expect the government to rescue troubled GSEs, investors will tend to let GSEs take greater risks than they otherwise would have taken. This weakening of market discipline on GSEs will, in turn, increase the risk that the GSEs will ultimately get into trouble. Thus "too big to fail" and "systemic risk" are to a large extent circular: they have their roots in prevailing expectations, and they easily become self-fulfilling prophecies. But this circularity also has a positive side: by acting in a timely way, the government can correct "too big to fail" expectations. Congress did just that in the FDIC Improvement Act of 1991 (FDICIA), which curtailed "too big to fail" treatment of banks. Proper and timely government action can thus reduce the potential for systemic risk.

TABLE OF CONTENTS

STATEMENT OF RICHARD S. CARNELL

Mr. Chairman, Senator Sarbanes, Members of the Committee:

I am pleased to have this opportunity to discuss ways to improve the regulation of Fannie Mae, Freddie Mac, and the Federal Home Loan Bank System.

As government-sponsored enterprises, these entities are privately owned, profit-oriented corporations that have Congressional charters and receive an array of federal benefits not available to businesses generally. More importantly, capital market participants believe that the government implicitly backs each GSE—and would not let the GSE's creditors go unpaid. This perceived implicit guarantee is the GSEs' most important and most distinctive characteristic. It enables the three housing GSEs to borrow $2.2 trillion at rates below those available to even the most creditworthy fully private borrowers.

For years the GSEs assured us that they met the highest standards of corporate governance, fully complied with generally accepted accounting principles, provided disclosure at least as good as what the federal securities laws required, faced tough and effective safety-and-soundness regulation, and were so well run that no one had any business requiring them to do anything they did not want to do. Recent scandals and other developments cast doubt on these claims and on the adequacy of GSE regulation. The Administration has proposed major reforms of such regulation, including the creation of a new GSE regulatory agency. Treasury Secretary Snow has rightly called for "a strong, credible, and well-resourced regulator" with "powers . . . comparable in scope and force to those of other world-class financial regulators, fully sufficient to carry out the agency's mandate, with accountability to avoid dominance by the entities it regulates."

In my testimony today, I will:

(1) identify six fundamental questions Congress faces in structuring a GSE regulator;

(2) offer suggested answers to those questions;

(3) describe the double game by which the GSEs deny that they have "full faith and credit" government backing—in ways that leave the impression that they have no government backing at all—even as they work to reinforce the market perception of implicit government backing;

(4) refute the GSEs' attempt to liken FDIC-insured banks to GSEs and to argue that we should not concern ourselves with GSE subsidies because the government gives banks greater subsidies; and

(5) examine "systemic risk"—particularly the argument that if a GSE got into financial trouble, the government would have no choice but to rescue it, lest its failure unacceptably damage the financial system.

STRUCTURING THE REGULATOR

In designing (or redesigning) a regulatory agency, Congress faces six fundamental questions:

(1) ***Jurisdiction***: Who will the agency regulate?

(2) ***Mission***: What objectives should the agency seek to achieve?

(3) ***Governance***: Who will run the agency, and under what ground rules?

(4) ***Resources***: How will the agency pay its expenses?

(5) ***Legal Authority***: What legal tools will the agency have to do its job?

(6) ***Incentives***: What incentives will the agency's officers and employees have?

I will first briefly analyze OFHEO's structural weaknesses in light of these questions. I will then discuss how to structure a new GSE regulatory agency, considering the first five questions in turn and (in so doing) noting how the answers given to those questions will affect the agency's incentives. For the new agency's incentives will be crucial to the agency's success or failure.

OFHEO's Structural Weaknesses

Congress created OFHEO with significant structural weaknesses. Specifically, the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 ("1992 Act") created a small, hyper-specialized agency—with uncertain funding and overly narrow powers—to regulate two huge, relatively homogeneous firms with great political clout. The Act housed that agency in a department with no institutional commitment to safety and soundness, little credibility to spare, and little ability to protect OFHEO against pressure from Fannie and Freddie. I summarize some of these structural weaknesses and their consequences in the table following this page. Building these weaknesses into OFHEO was a bit like keeping a watchdog hobbled, muzzled, and underfed.

Jurisdiction

The new agency should regulate Fannie, Freddie, and the Federal Home Loan Bank System, taking over the functions currently performed by OFHEO and the Federal Housing Finance Board.[1]

Having a single agency regulate all three housing GSEs would have several advantages over the current system. The General Accounting Office identified and aptly summarized these advantages in its excellent report, *Government Sponsored Enterprises: Advantages and Disadvantages of Creating a Single Housing GSE Regulator* (1997), on which I will draw extensively in this part of my testimony.

[1] I will argue below that the new agency should, ideally, also become responsible for overseeing Fannie and Freddie's housing mission, taking over functions currently performed by HUD.

First, and most importantly, a single regulator would have more independence from the firms it regulates. The Home Loan Bank System has a different business model and different interests than Fannie and Freddie. These differences should create what the GAO called "a healthy tension in the oversight of the [GSEs] that could help prevent the regulator from being 'captured' by the GSEs" (i.e., from identifying with and primarily serving the GSEs' interests).

A similar "healthy tension" in state thrift regulation yielded major benefits during the thrift debacle of the 1980s. The most severe losses among state-chartered, federally insured thrifts occurred in states (e.g., Texas and California) with hyper-specialized regulators that supervised only thrifts. States whose banking commissioners also regulated thrifts had a much better record of keeping thrifts healthy and avoiding costly failures. This difference in outcomes reflected a difference in regulators' incentives. Hyper-specialized thrift-only regulators proved overly reluctant to rein in risky practices, close insolvent thrifts, and require sick thrifts to recapitalize. Such strong measures would have risked alienating thrifts (the regulators' main constituency) and putting the regulators out of business. By contrast, state officials who regulated both banks and thrifts had greater liberty to take tough but necessary action against troubled thrifts. State-chartered banks demanded such action. Moreover, these officials knew that their agencies could, if necessary, survive without a thrift clientele. So regulating both banks and thrifts gave these officials more freedom to do their jobs well. Similarly, regulating all three housing GSEs would give the new GSE regulator more freedom to do its job well than if it regulated only Fannie and Freddie or only the Home Loan Banks.

Second, an agency regulating all three housing GSEs would be larger and (in the GAO's phrase) "more prominent in government" than OFHEO and the Finance Board. This increased stature "could help attract and retain staff with the special mix of expertise and experience needed to examine and monitor these sophisticated GSEs."

Third, a single housing GSE regulator could achieve "some economies and efficiencies" by having staff "share expertise in such areas as examinations, credit and interest rate risk monitoring, financial analysis, and economic research" and by combining "[a]dministrative support functions."

Fourth, such an agency could achieve greater consistency in regulating the three housing GSEs.

The main disadvantage of creating a single regulator would be quite modest: what the GAO called "the short-term disruption that would come with any type of change."

Mission

OFHEO and HUD currently divide regulation of Fannie and Freddie, with OFHEO responsible for safety and soundness and HUD responsible for housing mission. The Finance Board, by contrast, has both types of responsibility for the Home Loan Bank System.

Giving the new GSE regulator both safety-and-soundness and mission responsibilities would have three advantages. First, it would promote accountability by both the regulator and the GSEs. Divided responsibility creates "the potential for the GSEs to try to pit the regulators against each other" (as the GAO's 1997 report noted) or to tell each regulator that a given matter—which may raise both mission and safety-and-soundness issues—falls only within the authority of the other regulator. Second, giving a single agency both responsibilities would simplify compliance by the GSEs. Third, insofar as GSE policy must take account of both mission and safety and soundness, giving one agency both responsibilities would promote better-informed decision-making.

Accordingly, I would support combining both responsibilities in one agency if that can be done under sound governance (discussed below). But sound governance is so critical that it should not be compromised to obtain the more modest benefits of combining the two responsibilities. In any event, the GSEs should have to limit their activities to the secondary market and obtain the new agency's approval before commencing new activities.

Governance

General Approach

The paramount goal in structuring a new GSE regulatory agency should be to assure the agency's independence from the firms it regulates. The housing GSEs are powerful, aggressive, and politically effective. They are adept at capturing or cowing regulators. But a sound governance structure—combined with other reforms (such as having one agency, with permanent funding and adequate legal authority, regulate all three housing GSEs)—can help the agency avoid such capture or intimidation.

Two possible governance structures offer the best prospects for maintaining the agency's integrity, objectivity, and effectiveness.

The first approach would make the agency an autonomous bureau of the Treasury Department.[2] The Treasury has an institutional commitment to safety and soundness, and has the will and the institutional credibility to stand up to the GSEs. The GSEs would find the Treasury harder to bully than HUD, OFHEO, the Finance Board, or a new independent agency. I believe that a Treasury-based GSE regulator would also diligently carry out its

---

[2] My confidence in the Treasury may reflect my own association with that department from 1993 through 1999. Yet I had concluded years before—at the time of the thrift debacle—that the Treasury was the best place to house GSE regulation.

responsibilities for the GSEs' housing mission. The myth of the Treasury as hostile to housing and eager to choke off housing finance is just that: a myth, popularized decades ago by thrift lobbyists intent on keeping thrift regulation a lax, cozy backwater. The Treasury's Office of Thrift Supervision ("OTS") has performed both safety-and-soundness and housing-mission responsibilities for over 14 years, without anti-housing bias (and with greater competence than the independent agency it replaced).

The second approach would place the new agency under a three- or five-member board. The board would include one representative each from the Treasury and HUD. It would also include either one or three appointed members nominated by the President and confirmed by the Senate. An appointed member would serve as chair of the board and executive head of the agency. The Treasury, HUD, and the appointed member(s) would each bring their own perspectives and expertise to bear.

I view a three-member board[3] as preferable to a five-member board. A larger board would (other things being equal) have more difficulty making decisions and be more vulnerable to capture or manipulation by the GSEs. Moreover, the two additional appointed positions on a five-member board would probably offer too little challenge to attract and retain the most talented, energetic people. The chair would head the agency, and the Treasury and HUD members would have their own responsibilities. But how would the two extra appointed members occupy themselves? Would they end up half-idle, hobnobbing with the GSEs, intriguing against other board members, or attempting to micromanage the agency's staff? The prospect of such high-level underemployment would hinder the recruitment and retention of able, independent individuals.

Regulatory Autonomy

The Administration has opposed making the new agency a bureau of the Treasury unless the agency must clear its regulations and Congressional testimony through the Treasury. The Administration gives two reasons for requiring such clearance—and thus treating the new agency differently than the Treasury's Office of the Comptroller of the Currency ("OCC") and Office of Thrift Supervision.[4] First, because the new agency would regulate only a few firms, all very large, it would be particularly vulnerable to "capture" by those firms. This vulnerability (in Secretary Snow's words) "makes the oversight of overall policy development by the Treasury Department vital." Second, "it is vitally important that the Treasury Department be able to monitor the new regulator's policies to ensure that such policies are not reinforcing any such market misperception of an implied guarantee."

---

[3] The Pension Benefit Guaranty Corporation provides a precedent for a three-member board that draws a majority of its members from executive departments. The PBGC board consists of the Secretaries of Labor, Treasury, and Commerce. 29 U.S.C. § 1302(d).

[4] The Treasury cannot "delay or prevent the issuance of any rule or the promulgation of any regulation" by the OCC or OTS. No one can require clearance of those agencies' Congressional testimony. 12 U.S.C. §§ 1, 250, 1462a(b)(4).

I concur in both arguments: a specialized GSE regulatory agency would be acutely vulnerable to capture; and the Treasury should be able to monitor a Treasury bureau's policies to ensure that they do not reinforce market misperception of an implied guarantee. But these arguments do not necessarily show that Treasury clearance of regulations and testimony is essential—or that autonomy of the general type enjoyed by the OCC and OTS would not work. Both the OCC and OTS are (in the words of the OTS statute) "subject to the general oversight of the Secretary of the Treasury." 12 U.S.C. §§ 1, 1462a(b)(1). This oversight offers some protection against capture and should help ensure that the agency's policies do not reinforce the market misperception. Insofar as the Treasury remains concerned about the misperception, the Treasury itself can speak out any time, which would correct the misperception far more effectively than vetting regulations and testimony. Moreover, the GSEs' aggressiveness and political clout—and the new agency's consequent need for support—would give the agency reason to consult and cooperate with the Treasury even if the agency did not need formal Treasury clearance of regulations and testimony.

Requiring Treasury clearance of the new agency's Congressional testimony could cause delay, as Treasury officials who might otherwise have little interest in the agency's work scrutinized the testimony to make sure it would not embarrass the Treasury Secretary or the Administration. One persistently tardy participant in a clearance process can make testimony persistently late despite the other participants' best efforts. Note, moreover, that if the Secretary cannot control the agency's testimony, then it is harder (although not impossible) to blame the Secretary for that testimony.

A stronger case exists for Treasury clearance of the new agency's regulations (although I don't regard such clearance as essential). Such clearance would help guard against capture. It need not cause delay, as regulation-writing takes time and rarely has the short deadlines typical in preparing Congressional testimony.

In any event, Treasury clearance of regulations should not derail GSE reform legislation. Congress can develop middle-ground options, such as (1) setting a time limit on Treasury review, or (2) permitting the new agency to proceed with a proposed regulation unless the Treasury expressly disapproves the regulation within a specified time period and publishes specific written reasons for its disapproval. Such an intermediate option would make Treasury review of the agency's regulations more than merely advisory, while providing safeguards against delay or unreasoned disapproval.

Resources

Like the OCC and OTS, OFHEO pays its expenses using fees collected from the firms it regulates; it receives no general tax money. But unlike the OCC and OTS, OFHEO needs an annual appropriation to set and collect such fees. Fannie and Freddie have used the appropriations process both to pressure OFHEO (just as thrifts used the process to pressure the old Federal Home Loan Bank Board) and to limit OFHEO's capacity to undertake more rigorous scrutiny of the GSEs. To reinforce the new agency's independence from the firms it regulates, Congress should end this reliance on appropriations.

Legal Authority

Capital, Enforcement, and Prompt Corrective Action

The Federal Housing Enterprises Financial Safety and Soundness Act of 1992 drew on banking law to strengthen the safety-and-soundness regulation of Fannie and Freddie. The 1992 Act required new capital standards. It included prompt corrective action provisions to encourage the GSEs to correct capital deficiencies. It authorized OFHEO to take administrative enforcement action against unsafe practices.

But at the insistence of Fannie and Freddie, the 1992 Act unwisely tended to deny OFHEO authority possessed by bank regulators. As a result, OFHEO has (in Tom Stanton's phrase) "a sort of parody of the authority of the federal bank regulators." The limits on OFHEO's authority contrast sharply with the goal of creating "a strong, world-class regulatory agency" with powers "comparable in scope and force to those of other world-class financial regulators."

Bank regulators have broad authority to prescribe capital standards, including authority to impose new standards or toughen existing standards. 12 U.S.C. §§ 1831o(c)(1), 3907(a). OFHEO, by contrast, faces major constraints on the form and content of capital standards, including an extraordinarily complex Congressionally dictated stress test. §§ 4611-4612. The new regulator needs authority to raise capital standards in light of experience.

OFHEO has much weaker enforcement authority (§§ 4631-4636) than federal bank regulators (§ 1818), as shown in the table following this page. For example, bank regulators can issue a cease-and-desist order against any "unsafe and unsound practice." OFHEO can issue such an order only if the conduct jeopardizes a GSE's capital. Bank regulators can bar any officer, director, or employee of an FDIC-insured institution from working at that or any other federally insured institution if the individual committed misconduct (e.g., breaking the law) that (1) enriched the individual or caused loss to the institution, and (2) involved personal dishonesty or demonstrated willful or continuing disregard for institution's safety and soundness. OFHEO has no such authority. Bank regulators can impose civil money penalties of up to $25,000 per day for lawbreaking that enriches the violator or breaches the violator's fiduciary duties. OFHEO cannot impose civil money penalties on these grounds. Bank regulators can impose civil money penalties of up to $1 million per day for (1) knowingly breaking the law or breaching fiduciary duty, and thereby (2) substantially enriching the violator or causing the institution substantial loss. OFHEO cannot impose civil money penalties on these grounds.

Fannie and Freddie face prompt corrective action rules (§§ 4614-4619, 4622) conspicuously weaker than those governing FDIC-insured depository institutions (§ 1831o). For example, an undercapitalized bank cannot increase its total assets unless (1) the bank has an acceptable capital restoration plan, (2) the asset growth comports with the plan, and (3) the bank's capital ratio increases at a rate sufficient to enable the bank to become adequately capitalized within a reasonable time. § 1831o(e)(3). Yet no statute bars Fannie and Freddie from continuing to grow while undercapitalized, even if they have no capital restoration plan or if the growth conflicts with such a plan (§ 4615). The prompt corrective action statute authorizes growth restrictions only against a significantly or critically undercapitalized GSE, and makes such sanctions purely discretionary. §§ 4616(b)(2), 4617(b), (c)(2). Similarly, a bank cannot pay dividends if the bank is or would become undercapitalized, whereas even an undercapitalized GSE may be able to pay dividends as long as the dividends are not so large as to render the GSE significantly undercapitalized. §§ 1831o(d)(1)(A), 4515(a)(2).

The GSE enforcement and prompt corrective action rules should be strengthened in line with their banking counterparts.

Receivership

There are two basic ways to deal with a firm if its liabilities exceed its assets and it cannot pay its debts as they become due: liquidation and reorganization. Liquidation involves selling the firm's assets and using the proceeds to pay creditors. Reorganization involves scaling back the firm's liabilities, such as by turning some of the firm's debt into equity.

Liquidation or reorganization mechanisms exist for most firms. A court can liquidate a business corporation under chapter 7 of the Bankruptcy Code or (with enough creditors' approval) reorganize the corporation under chapter 11. The FDIC can liquidate or reorganize an insolvent FDIC-insured bank or thrift. The Federal Housing Finance Board can liquidate or reorganize a Federal Home Loan Bank.

But in the case of Fannie and Freddie, no adequate legal mechanism exists for dealing with a GSE if its liabilities exceed its assets. The Bankruptcy Code does not apply.[5] Although OFHEO can appoint a "conservator" to take control of the GSE, the conservator cannot require creditors to exchange debt for equity or to accept less than full payment of their claims.[6] Thus if the GSE's assets fall short of its liabilities, the

---

[5] Specifically, the Bankruptcy Code does not permit Fannie or Freddie to become a debtor in a bankruptcy proceeding, whether voluntarily or involuntarily. As federal instrumentalities, Fannie and Freddie are "governmental units" under § 101(27) of the Bankruptcy Code and thus under § 101(41) are not a "person." Under § 109(a) only a "person" can become a "debtor" in a bankruptcy proceeding. See 11 U.S.C. §§ 101(27), (41), 109(a).

[6] Under 12 U.S.C. § 4620(a), a conservator generally "shall have all the powers of the shareholders, directors, and officers of the enterprise under conservatorship and may operate the enterprise in the name of the enterprise." But a firm's shareholders and managers have no power to require creditors to exchange debt for equity or to accept only partial payment of their claims.

Nor does § 4620(f) authorize OFHEO to write down creditors' claims. Under § 4620(f) OFHEO "may require a conservator to set aside and make available for payment to creditors any amounts that the Director determines may safely be used for such purpose." Using this authority, OFHEO could require a conservator to make larger or earlier payments to creditors than the conservator might otherwise make. But conservator has no power to resolve the shortfall.[7] The insolvent GSE would remain adrift in legal uncertainty until Congress enacted special legislation.

This lack of an orderly "receivership" mechanism—i.e., mechanism for using the insolvent GSE's assets to satisfy the GSE's creditors—is a serious gap in current law, with potentially serious consequences for financial markets. So long as the gap remains, the GSE regulator will not truly have powers "comparable in scope and force to those of other world-class financial supervisors, fully sufficient to carry out the agency's mandate."

Congress can fill the gap in at least two ways: (1) by authorizing the GSE regulator to commence a bankruptcy proceeding against an insolvent GSE; or (2) by authorizing the regulator to appoint a receiver to deal with the GSE under a specialized set of rules such as those applicable to failed banks. Either approach can do the job.

Regulating GSEs but having no receivership mechanism is like investing in an elaborate fire-protection system—complete with firewalls, smoke detectors, heat sensors, alarm bells, and sprinklers—but failing to mount a crucial fire door on its hinges. Like fire-safety measures, GSE safety-and-soundness regulation serves dual purposes. Fire-safety measures protect a building by preventing and extinguishing fires there; they also protect other buildings by inhibiting the spread of fire. Similarly, GSE regulation seeks not only to keep the GSEs themselves safe but to protect the financial and housing sectors from damage that might result from a GSE's failure. Bank regulation serves similar purposes and did so even before federal deposit insurance: seeking both to protect banks' depositors and other creditors and to prevent bank failures from causing broader economic harm. A receivership mechanism, by providing an orderly means for dealing with a failed GSE's obligations, would help limit and contain the harm resulting from a GSE's failure.

THE GSEs' DOUBLE GAME

In General

In managing their relationship to the federal government, the GSEs play an extraordinarily successful double game: they deny that they have any formal, legally enforceable government backing, even as they work to reinforce the market perception of *implicit* government backing. Let's look more closely at the two parts of the double game.

First, the GSEs emphatically deny that they have any formal, legally enforceable government backing—in itself, a valid point. But the GSEs make this point in ways designed to convince the uninitiated that the GSEs enjoy *no government backing at all* (an

---

the statute in no way suggests that by accepting such payments creditors would waive their right to eventual payment in full.

[7] A conservator might, in theory, attempt to get all of the GSE's creditors to agree to scale back their claims. But obtaining the creditors' unanimous consent would be impracticable given the large number of creditors and the incentive for some creditors to threaten to veto the deal unless they received favored treatment.

implication directly conflicting with the second part of the double game). The GSEs stress that "Every one of our debt securities clearly states, in plain English, it is not backed by the full faith and credit of the government."[8] They argue that they operate "with entirely private capital" and that their activities "are entirely supported by [their] revenue . . . and the capital of private investors and are *not in any way guaranteed by the federal government*."[9]

Second, the GSEs work to reinforce the perception of implicit government backing. Consider three examples involving Fannie. In the first example, Fannie sought legislative history stating that Fannie and Freddie "are *implicitly backed by the full faith and credit of the U.S. Government*."[10] In the second example, Fannie attacked Treasury Under Secretary Gensler as "irresponsible" and "unprofessional" when he testified before a House subcommittee on March 22, 2000, that "the government does not guarantee [GSEs'] securities."[11]

In the third example, Fannie argued in a 1998 letter to the Office of the Comptroller of the Currency that "all GSE issued securities merit" more favorable treatment under the federal banking agencies' risk-based capital standards than all "AAA-rated [non-GSE] asset-backed securities." Thus the mere fact that a GSE issues a security makes that security more creditworthy than any non-GSE security. An IOU issued by a financially troubled GSE (such as the Farm Credit System before its 1987 bailout) would, under Fannie's reasoning, still be more creditworthy than a top-tier asset-backed security guaranteed by the nation's healthiest fully private corporation. Fannie based this argument squarely on what it calls "the implied government backing of Fannie Mae":

> GSE issues generically, and Fannie Mae-guaranteed MBS in particular, are viewed by the capital markets as *near proxies for Treasury securities* in terms of credit worthiness.
>
> . . .
>
> Fannie Mae standard domestic obligations, like Treasuries, typically receive no rating on an issue-by-issue basis, because investors and the rating agencies view the *implied government backing of Fannie Mae* as a sufficient indication of the investment quality of Fannie Mae obligations. …[12]

---

[8] Franklin D. Raines, Remarks at Conference on Money Markets and the News: Press Coverage of the Modern Revolution in Financial Services, March 19, 1999.

[9] Fannie Mae, FM Watch Observer: Glossary of Terms, www.fmwatch-observer.com/glossary.html (emphasis added).

[10] When I worked for this Committee on a Glass-Steagall repeal bill in 1987-88, Fannie asked that I include such language (emphasis added) in a draft section-by-section analysis, which I declined to do.

[11] K. Day, Remarks Put Pressure on Fannie, Freddie Bonds, WASH. POST, Mar. 24, 2000, at E1; J. Kosterlitz, Siblings Fat and Sassy, 32 NAT'L JOURNAL 1498 (2000).

[12] Letter from Anthony F. Marra to OCC, Feb. 3, 1998 (emphasis added).

Thus Fannie contended that in assessing credit quality, investors and rating agencies do not (and presumably need not) look beyond "the implied government backing of Fannie Mae," which in Fannie's view renders Fannie's securities "near proxies for Treasuries." These assertions are all the more remarkable in that Fannie made them in a formal comment letter to a bureau of the Treasury. We may reasonably infer that when Fannie meets with rating agencies and securities analysts—out of earshot of government officials—it makes arguments at least as strong as those quoted above.

This double game lets the GSEs have it both ways. In effect, the GSEs tell Congress and the news media, "Don't worry, the government is *not* on the hook"—and then turn around and tell Wall Street, "Don't worry, the government really *is* on the hook." The GSEs play this game unchallenged, year after year.

Fannie's CEO, Franklin D. Raines, recently seemed to question the "theory . . . that there is an 'implied guarantee' that the government would repay our creditors if we failed." In a February 6 speech at the American Enterprise Institute, Mr. Raines declared:

> [S]ome assert that we have an "implied guarantee" that the market relies on. Yet it is not clear what an implied guarantee means. We do not know who is making the implication or exactly what is being guaranteed. Indeed, Treasury Secretary Snow has testified that there is no implied guarantee.
>
> I believe that *the true value of our charter does not rest on a government guarantee of our obligations—implied or otherwise*.
>
> Instead, our charter signifies that the government places such a high value on our mission of expanding homeownership and affordable housing, that it goes to extraordinary lengths to ensure that the private management of our operations is closely supervised, and that our private capital is matched to our risks, even under extraordinary circumstances—all to ensure our continued success.
>
> This is the pact that the federal government has with investors. It does not cost taxpayers anything. And so far, it has worked very well. *This pact ensures that it is private capital that is at risk, not the taxpayer*. [Emphasis added.]

I urge the Committee to follow up on this statement by having Fannie and Freddie answer three simple questions:

1. Do capital market participants err in perceiving the federal government as implicitly backing Fannie and Freddie?

2. Do you believe that the government in any way implicitly backs Fannie and Freddie?

3. If Fannie and Freddie were to default on their obligations, would the government have any moral obligation to assure that Fannie and Freddie's creditors got paid?

Ineffective Statutory Disclaimers

In seeking to limit the taxpayers' exposure to the GSEs, Congress has enacted three disclaimers of liability. But the phrasing of these disclaimers, far from hindering the GSEs' double game, fits it neatly.

First, the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 declares that "neither the enterprises [i.e., Fannie and Freddie] . . . , nor any securities or obligations issued by the enterprises . . . , are backed by the full faith and credit of the United States." 12 U.S.C. § 4501(4). But this disclaimer merely restates the obvious: that the government has no formal, legally enforceable liability for the GSEs' securities. It does not disclaim implicit backing, nor does it signal that market participants err in perceiving such backing. It thus avoids the real issue.

Second, a statutory section entitled "Protection of taxpayers against liability" declares that the 1992 Act "may not be construed as obligating the Federal Government, either directly or indirectly, to provide any funds" to Fannie or Freddie "or to honor, reimburse, or otherwise guarantee any obligation or liability" of Fannie or Freddie. § 4503. This disclaimer also avoids the real issue. No one argues that the 1992 Act *created* implicit backing where it did not already exist. Market participants had long believed such backing to exist under the GSEs' charters. Congress did not act to correct that perception.[13]

Third, each firm's securities must include "appropriate language . . . clearly indicating" that the securities "are not guaranteed by the United States and do not constitute a debt or obligation of the United States or of any agency or instrumentality thereof" other than the GSE in question. §§ 1455(h)(1), 1719(b), (d)-(e). This requirement repeats the fundamental weakness of the first disclaimer: it disclaims formal, legally enforceable liability, even as it fails to disclaim implicit backing. "Indeed, the disclaimer itself hints at a special federal relationship; completely private firms do not need to disclaim federal backing because no one believes such backing exists."[14]

No one argues that the government has any formal, legally enforceable liability for the GSEs' securities. Thus the disclaimers ignore the real issue: whether the government, although not legally bound to rescue the GSEs, would nonetheless do so (e.g., because it felt a moral obligation for their debts or feared that a GSE default might damage the nation's financial system).

---

[13] The second disclaimer also replicates the weakness of the first disclaimer in declaring that the 1992 Act "may not be construed as implying that any such enterprise . . . , or any obligations or securities of such an enterprise . . . , are backed by the full faith and credit of the United States." § 4503.

[14] Ronald C. Moe & Thomas H. Stanton, *Government-Sponsored Enterprises as Federal Instrumentalities: Reconciling Private Management with Public Accountability*, 49 PUB. ADMIN. REV. 321, 323 (1989).

Subsidy Denial

The GSEs' double game helps the GSEs argue that they get little or no government subsidy. Yet no one can honestly dispute that Fannie and Freddie receive valuable benefits not available to businesses generally. These benefits include exemption from most state and local taxes and exemption from the registration and reporting requirements of the securities laws. The benefits also include a conditional line of credit at the U.S. Treasury and special rules relating to the GSEs' securities—for example, rules that: equate those securities with U.S. Treasury securities for some purposes; permit issuance and transfer of those securities over the system used for issuing and transferring U.S. Treasury securities; and fail to limit FDIC-insured banks' investments in those securities. This special treatment strongly abets the market perception of implicit federal backing. The Congressional Budget Office's reports and testimony demonstrate the great value of these special benefits.

Yet Fannie, in particular, insists that it receives no subsidy. Relying on a narrow dictionary definition to the effect that a "subsidy" is "monetary assistance granted by a government to a person or private commercial enterprise," Fannie asserts: "Fannie Mae does not receive a penny of public funds. To the contrary, last year our federal tax liability was $1.6 billion. True subsidies also are tangible. Fannie Mae's government benefits are not."[15] Fannie's reasoning—that a subsidy involves only a tangible payment of money by the government—produces absurd results. If Congress were to exempt Fannie from ever again having to pay any corporate income tax, that would supposedly not be a subsidy because it involves no cash payment to Fannie. Similarly, if a foreign government gave an energy-intensive, capital-intensive export industry unlimited access to free electricity and no-interest loans, that would supposedly not be a subsidy, either. These examples highlight the unreality of Fannie's arguments.

Curbing the Double Game

I suggest that any GSE legislation:

(1) correct the faulty statutory disclaimers of federal liability for Fannie and Freddie (discussed above);

(2) correct sloppy language in the Secondary Mortgage Market Enhancement Act of 1984 stating that for some purposes Fannie and Freddie securities "shall be considered to be obligations issued by the United States," 15 U.S.C. § 77r-1(a)(1)-(2);

(3) prohibit any GSE from representing that the U.S. Government directly or indirectly backs the GSE (except in discussing formal, legally enforceable obligations of the government) with the intent to induce anyone to rely on that representation in connection with the purchase or sale of any security; and

---

[15] Timothy Howard, *Fannie Mae's Benefits to Home Buyers: The Business Perspective*, 37 FED. RESERVE BANK CHI. ANN. CONF. BANK STRUCTURE & COMPETITION 68, 69 (2001).

(4) prohibit any government agency or official from characterizing GSE securities as government securities.

PROPERLY COMPARING BANKS AND GSEs

Fannie and Freddie often argue that the federal government gives FDIC-insured banks[16] benefits comparable to, or even greater than, those it gives Fannie and Freddie; that concern about subsidies to Fannie and Freddie is accordingly unwarranted and even hypocritical; and that any greater financial success shown by Fannie and Freddie simply reflects their greater efficiency.

Let's start with the issue of efficiency. Fannie and Freddie have lower overhead than banks because they do a different business than banks. Most banks do a predominantly retail business. To deal directly with large numbers of small customers, they have more offices and larger staffs than they otherwise would. By contrast, Fannie and Freddie do a wholesale business, which enables them to have lower overhead.

Now let's turn to the issue of relative subsidy. FDIC insurance has a different set of costs and benefits than the government's sponsorship of Fannie and Freddie. You might expect FDIC insurance to provide a greater net subsidy.[17] After all, FDIC insurance is established by law and carries the government's full faith and credit. Yet the government's perceived implicit backing of Fannie and Freddie actually tends to provide a greater net subsidy than FDIC insurance, for six structural reasons.[18]

1. Unlimited Coverage. Federal deposit insurance applies only to deposits and then only up to a $100,000 limit. The FDIC can protect a failed bank's uninsured deposits and nondeposit creditors (such as bondholders) only under very narrow circumstances. By contrast, the government's perceived implicit backing of GSEs has no limits: it applies to all of a GSE's obligations, with no dollar ceiling.

---

[16] For simplicity I use "banks" to refer to all FDIC-insured depository institutions, including thrift institutions.

[17] The gross subsidy represents the total value of the special benefits provided by the federal government—benefits not available to businesses generally or even financial institutions generally. The net subsidy represents the difference between the gross subsidy and the offsetting costs that the entity must incur as a bank or GSE—costs not imposed on financial institutions generally.

[18] I have set forth these arguments more fully in *The Structure of Subsidy: Federal Deposit Insurance Versus Federal Sponsorship of Fannie Mae and Freddie Mac*, in SERVING TWO MASTERS, YET OUT OF CONTROL: FANNIE MAE AND FREDDIE MAC 56-83 (2001).

Most of these structural reasons hold true for the Federal Home Loan Banks, which also enjoy exemption from the federal income tax. But the Home Loan Banks do face the possibility of receivership, and must pay 10 percent of their net income to an affordable housing program and another 20 percent toward interest payments on debt securities issued to help finance the thrift clean-up. 12 U.S.C. §§ 1430(j), 1433, 1441b(f)(2)(C), 1446.

2. No Receivership Mechanism. When an FDIC-insured bank fails, the FDIC becomes receiver for the bank: it takes control of the bank, gathers the bank's assets, and pays the bank's creditors in a specified order of priority. The bank's depositors must get paid in full before the bank's other creditors can get paid at all. If the bank's liabilities exceed its assets, its shareholders lose their ownership interest, its nondeposit creditors normally incur a partial or total loss, and its uninsured depositors often incur some loss. Similarly, when an ordinary nonfinancial company fails, it is liquidated under chapter 7 of the Bankruptcy Code. The bankruptcy court appoints a trustee, who takes control of the company, gathers its assets, and pays creditors in a specified order of priority. The lack of any receivership mechanism for Fannie and Freddie reinforces the market perception that the government would assure full payment of each firm's creditors.

3. No Cross-Guarantees to Protect Taxpayers. Federal deposit insurance involves strong safeguards designed to ensure that banks—rather than the taxpayers—bear any losses incurred in protecting insured depositors. Banks must normally pay premiums large enough to ensure that the FDIC's insurance funds have at least $1.25 in reserves for each $100 of insured deposits. This obligation to pay premiums gives each insurance fund a claim on the capital and earnings of all banks insured by that fund—and in effect creates a network of indirect cross-guarantees among FDIC-insured banks. Thus each member of the Bank Insurance Fund is liable for ensuring that the FDIC can protect insured depositors at every other BIF member bank. As long as the fund can replenish its reserves, its existence precludes any loss to the taxpayers.

No similar cross-guarantees reduce the government's risk-exposure to Fannie and Freddie. The two GSEs pay no insurance premiums and have no insurance fund. The two GSEs do not even cross-guarantee each other. If one GSE failed, the survivor would have no responsibility to pay the failed GSE's creditors.

4. Special Deals Instead of General Rules. To a much larger degree than banks, Fannie and Freddie reap the benefits of special, company-specific laws and avoid the discipline of generic law. Instead of operating under laws applicable to thousands of businesses, the two GSEs often get to operate under statutes designed for them alone.

5. Protection from Effective Competition Subsidizes GSE Shareholders. Federal and state regulators routinely issue bank charters to qualified applicants. Once chartered, a bank can typically engage in a wide range of activities statewide and even nationwide. No longer does each bank charter require special legislation. No longer do regulators grant charters sparingly so as to limit competition with existing banks. Entry into banking is relatively easy, and banking law affords banks little protection against competition. Thus if banks receive a net federal subsidy, they should generally face enough competition to force them to pass the subsidy through to their customers.

Fannie and Freddie, by contrast, enjoy significant protection against competition. Their government sponsorship reduces their borrowing costs and increases the value of their guarantees to such an extent that no fully private firm can compete against them effectively. And only Congress can charter a competing GSE. By impeding competition with Fannie and Freddie, these constraints on entry increase the potential for the two GSEs' government benefits to end up in the hands of their shareholders rather than their customers.

6. Free Ride. Banks must normally pay for deposit insurance. They must also comply with an array of restrictions and requirements not applicable to businesses generally. But Fannie and Freddie pay no fee for their government sponsorship. They make no payments to an insurance fund or affordable housing fund. They need not provide public benefits that impose significant costs on their shareholders. HUD's affordable housing goals are so weak that Fannie and Freddie can meet them without doing more for affordable housing than banks do. I believe that the two GSEs would have a profit motive to do their affordable housing business in any event, even without a government subsidy.

Considering the great value of the benefits Fannie and Freddie receive from the government, they should be doing *far* more to increase home ownership at the margin (e.g., by the lower middle class, the working poor, and members of certain historically disadvantaged minority groups).

SYSTEMIC RISK

GSEs are often characterized as "too big to fail"—meaning that if they neared default on their debts, the government would have to rescue them lest their failure unleash "systemic risk" that would gravely damage the nation's financial system and economy.

Discussions of systemic risk (whether in the GSE or the bank context) often have a tone of inevitability. But systemic risk is not a force of nature like earthquakes, hurricanes, and tornados. It results from human decisions: for example, decisions by market participants and government officials about how to structure the financial system, what risks to take, and how to respond to problems. If investors expect the government to protect them from the full pain of downside scenarios, they will tend to take greater risks than they otherwise would have taken. Thus "too big to fail" and "systemic risk" are to a large extent *circular*: they have their roots in prevailing expectations, and they easily become self-fulfilling prophecies. Insofar as investors expect the government to rescue troubled GSEs, market discipline on GSEs will weaken, which will tend to increase the risk that the GSEs ultimately will get into financial trouble.

If a GSE's troubles coincide with a broader financial crisis, government officials will face additional pressures to rescue the GSE. For if during the crisis those officials seriously upset established expectations, they may create contagious uncertainty about the government's willingness to meet other expectations. A crisis is thus a particularly inopportune time for attempting to reeducate market participants about the scope of the government's undertakings. So if the government tacitly accepts "too big to fail" expectations during good times, it may find itself constrained during a crisis to rescue a GSE against its better judgment.

But the circularity of systemic risk also has a positive side: if the government acts in a timely way, it can correct "too big to fail" expectations. Congress did just that in the FDIC Improvement Act of 1991 ("FDICIA") by curtailing the practice of treating FDIC-insured banks as "too big to fail."[19] FDICIA's "least-cost resolution" rule allows the FDIC to protect a failed bank's uninsured depositors and nondeposit creditors only if doing so is the "least costly to the deposit insurance fund of all possible methods" for meeting the FDIC's obligation to insured depositors. 12 U.S.C. § 1823(c)(4). The rule has a narrow systemic-risk exception, which has never been used.[20] Before FDICIA, the FDIC was spending extra money from the deposit insurance fund to protect uninsured depositors at banks as small as $500 million in total assets. But less than one year later, when an $8.8 billion bank group in a swing state failed just a few days before the 1992 Presidential election, the FDIC did not protect uninsured depositors and financial markets took that action in stride. By giving clear and timely notice of the new policy, Congress had succeeded in changing market participants' expectations. Proper and timely government action can thus reduce the potential for systemic risk.[21]

Effective safety-and-soundness regulation of the GSEs can further reduce that risk. Yet we should beware of relying excessively on regulation. Regulation did not prevent the U.S. banking system from collapsing in 1933. Regulation did not prevent the 1980s thrift debacle, with its $125 billion cost to the taxpayers. Regulation did not prevent the bank failures of the 1980s and early 1990s, which depleted the FDIC's Bank Insurance Fund. Nor, more recently, did OFHEO detect Fannie and Freddie's accounting problems, even though it had examiners scrutinizing each GSE year-round. The failings of regulation underscore the need to maintain market discipline on the GSEs and other large financial institutions.

---

[19] In context of a failed FDIC-insured bank, "too big to fail" treatment involves spending extra money from the deposit insurance fund to protect deposits above the $100,000 limit on deposit insurance coverage. It may also involve extra spending to protect nondeposit creditors.

[20] The systemic-risk exception becomes an option only if recommended to the Secretary of the Treasury by two-thirds majorities of both the Federal Reserve Board and the FDIC's Board of Directors. The secretary can make the exception only if the secretary determines, "in consultation with the President," that least-cost resolution of a given institution "would have serious adverse effects on economic conditions or financial stability." The secretary must document the determination. The General Accounting Office must review and report on the exception, including the potential for it to diminish market discipline and encourage unsound risk-taking. To recoup the additional cost of deviating from least-cost resolution, the FDIC must levy a special assessment on insured depository institutions. § 1823(c)(4)(G). Congress designed these rules to promote accountability and make the process sufficiently unpleasant that systemic-risk exceptions would be made rarely (if at all) and never lightly.

[21] By engineering a bailout of Long Term Capital Management in 1998, the Federal Reserve Bank of New York squandered some of FDICIA's hard-won gains. Yet the dramatic change in how the FDIC dealt with failed banks during the early 1990s shows that progress can be made in curtailing too-big-to-fail treatment.

MISCELLANEOUS

Ending the Government's Role in Appointing GSE Directors

Under current law, federal officials appoint some members of each housing GSE's board of directors. For both Fannie and Freddie, the President appoints five of each GSE's 18 directors. 12 U.S.C. §§ 1452(a)(2)(A), 1723(b). The Federal Housing Finance Board appoints six of each Home Loan Bank's 14 directors. § 1427(a).

The Administration rightly proposes to end governmental appointment of GSE directors (and, as an initial step in that direction, has indicated that it will no longer appoint directors of Freddie). Government-appointed directors face a conflict of interest. They presumably have some duty to serve the public. Yet under corporate law they presumably also have fiduciary duties to their corporation's shareholders. These duties conflict whenever the shareholders' interests run counter to some broader public interest: e.g., when the shareholders' interest in maximizing profits conflicts with the public interest in protecting the taxpayers or promoting affordable housing. In 1988 Freddie's directors concluded that their fiduciary duties compelled them to side with the shareholders against the taxpayers.[22] In any event, government appointments to GSEs' boards of directors have served more as political plums than as vehicles for upholding the public interest.

Ending such appointments—so that GSE shareholders would elect all GSE directors—would remove the conflict of interest. By strengthening shareholders' control over each GSE, ending such appointments could also help shareholders hold management more accountable and thus promote better corporate governance.

Complying with Securities Laws

The GSEs' statutory exemption from the registration and reporting requirements of the federal securities laws is an anachronism and deserves to be repealed. The exemption sends the wrong signal: that GSEs are so "special," so close to the government, that investors in their securities have no need for the protections afforded by those requirements.

Opportunities for Immediate Administrative Action

Regulators can and should act now to improve the regulation of Fannie and Freddie.

---

[22] The three members of the old Federal Home Loan Bank Board—appointed by the President and confirmed by the Senate—served ex officio as Freddie's board of directors. Freddie's preferred share price had more than doubled in response to a proposal to allow anyone to own Freddie shares. (By severing Freddie's historic link to the thrift industry, the proposal would free Freddie to increase its profits by amassing a large portfolio of mortgage-backed securities.) Senate Banking Committee Chairman William Proxmire developed a plan to grant the relief desired upon payment of a fee to reduce the taxpayers' bill for the thrift clean-up. But Freddie's management convinced Freddie's directors that their fiduciary duties compelled them to oppose the Proxmire plan.

First, to help avoid unhealthy concentrations of credit risk among FDIC-insured banks, the federal banking agencies should prescribe guidelines for banks' credit exposure to individual GSEs and to GSEs generally.[23]

Second, the Securities and Exchange Commission should prohibit mutual funds whose portfolios consist largely of GSE securities from mislabeling themselves as "Government" or "U.S. Government" funds.[24]

Third, the Federal Reserve Board should proceed with its proposal to curtail so-called "daylight overdrafts" by GSEs.

Fourth, HUD should tighten its scrutiny of the GSEs' mission, using its authority to review activity-expansion, prescribe affordable-housing goals, and interpret relevant statutes.

CONCLUSION

The GSEs argue as though the present is always the wrong time to enact any reform that they do not want, such as reform that benefits taxpayers or homebuyers rather than the GSEs' managers and shareholders. In the GSEs' view, either (1) there is no acute problem warranting reform, or (2) reform now would crimp housing markets and risk destabilizing the financial system. But now is the right time to act—to correct the deficiencies in GSE regulation before a crisis hits or another scandal breaks.

---

[23] Regulators could, for example, prescribe rules or guidelines under section 305(b)(1)(A)(ii) of FDICIA, which requires risk-based capital standards to "take adequate account of … concentration of credit risk." Regulators could also issue more specific examination standards.

[24] The SEC prohibits a mutual fund from having "name suggesting that the Fund … [is] guaranteed … by the United States government." 17 C.F.R. § 270.35d-1. But many mutual funds that invest predominantly in GSE securities nonetheless call themselves "U.S. Government Securities Funds." To take what is probably an extreme example, the Pacific Capital U.S. Government Securities Cash Assets Trust had 98.8 percent of its assets in GSE securities as of September 30, 2003; it evidently held no U.S. government securities at all. See http://www.aquilafunds.com/ourcompany/moneyfunds.htm (semi-annual report), at 9.