RSC Republican Study Committee **Financial Services Working Group**

Congressman Scott Garrett (R-NJ), Chairman — Congressman Tom Price (R-GA), RSC Chairman

February 3, 2010

MISSING FROM THE PRESIDENT'S BUDGET: THE COST OF FANNIE AND FREDDIE

As President Obama unveils his budget for 2011, one item is missing: **accounting for the failures of Fannie Mae and Freddie Mac.**

The Congressional Budget Office (CBO) projects that Fannie Mae and Freddie Mac will cost American taxpayers at minimum, $398 billion. This is almost FOUR TIMES more than the expected ultimate cost of the TARP program!

FANNIE AND FREDDIE Q & A

Q. What are Fannie Mae and Freddie Mac?
A. Government entities that purchase mortgages from lenders.

Q. Why are they problematic?
A. They represent another taxpayer bailout – some of the mortgages they own are bad and the losses to Fannie Mae and Freddie Mac paid for by American taxpayers.

Q. Why should we care?
A. These entities have the potential to create a bigger, farther reaching housing bubble that will cause an even worse economic crisis than the one we are currently experiencing.

Q. So…what?
A. We must reform housing finance to reduce the risk to taxpayers. Barney Frank refuses to even hold hearings on Fannie Mae and Freddie Mac!

FANNIE AND FREDDIE NUMBERS

$21 billion estimated taxpayer subsidy cost for 2010 according to CBO

$64 billion estimated taxpayer subsidy cost for 2011-2020 according to CBO

$291 billion - added to federal debt in 2009 to support GSEs according to CBO

$8.1 trillion - GSE securities outstanding according to data released by the Federal Reserve on December 10, 2009 *(Neither CBO nor OMB incorporates debt securities or mortgage-backed securities issued by Fannie Mae and Freddie Mac in estimates of federal debt held by the public.)*

UNLIMITED Treasury assistance to the GSEs through 2012

A FINAL NOTE ABOUT ACCOUNTING FOR FANNIE AND FREDDIE

The Administration's Office of Management and Budget (OMB) continues to treat Fannie Mae and Freddie Mac as outside the budget, and it records and projects outlays equal to the amount of those cash infusions. As a result, the Administration has not included in its budget figures subsidy costs that would be directly comparable to CBO's $291 billion estimate of such costs in 2009. Instead, because the Treasury provided a total of $95.6 billion in cash outlays to the two entities in fiscal year 2009, the government's final report of spending for 2009 included that amount, which is similar to CBO's August 2009 estimate of cash infusions for that year ($112 billion).

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CBO and the White House debate how much to tell taxpayers.
Accounting for Fannie

THE WALL STREET JOURNAL.
WSJ.com

The Congressional Budget Office has lopped $20 billion off its estimate of the cost of keeping Fannie Mae and Freddie Mac afloat for the next decade—to a mere $79 billion. That will have to pass for good news, even if the estimate comes loaded with caveats. The bigger story is why the White House continues to keep these wards of the state off-budget.

As the CBO notes in a recent background paper, the standards for when to include government-sponsored entities in the budget go back to the 1960s, when a Presidential commission laid out a set of questions.

To wit: "Who owns the agency?" (In the case of Fan and Fred, taxpayers.) "Who supplies its capital?" (Taxpayers.) "Who selects its managers?" (The federal government.) And finally, "Do the Congress and the President have control over the agency's program and budget, or are the agency's policies the responsibility of the Congress or the President only in some broad ultimate sense?" (The feds have control in every sense.)

Since Hank Paulson placed them in conservatorship in September 2008, Fan and Fred have stopped even pretending to be run for profit. Losses have mounted accordingly: Some $291 billion for taxpayers through 2009, $48 billion for the cost of new business in 2009 alone, and $21 billion more this year. Last August, CBO estimated the 10-year cost to taxpayers of keeping Fannie and Freddie afloat at $389 billion.

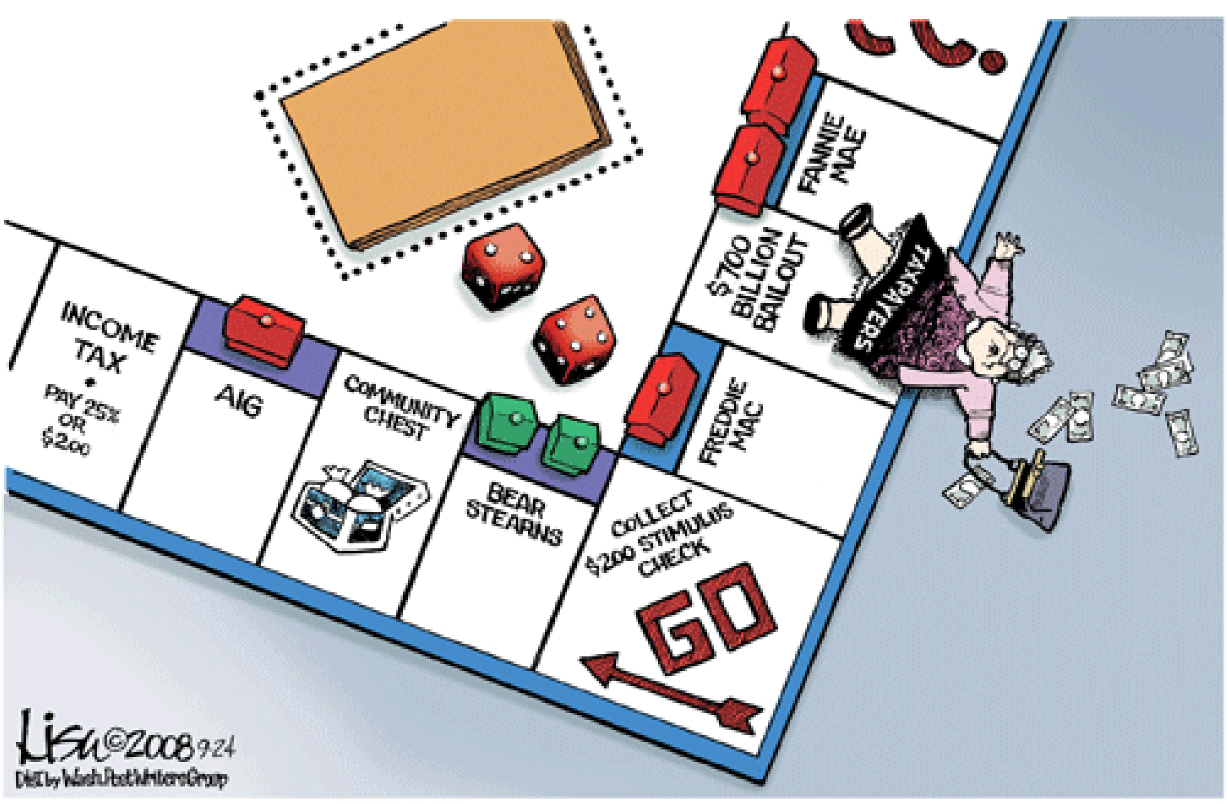
Yesterday's estimate reduces that by some 5%, but this assumes the companies will stabilize at a loss rate of nearly $8 billion a year on average over the next decade. CBO bases its projection on an expectation that the housing market will "normalize" as the recession ends. However, there is no more normal in a housing market that now depends almost entirely on government subsidies. The full cost of subsidizing mortgages via Fannie and Freddie, the FHA and Ginnie Mae remains hidden and off the official balance sheet, so there is little political pressure to stop the losses.

As the CBO notes, Fannie and Freddie "purchase mortgages at above-market prices," driving down interest rates and passing some of the savings to home buyers. That subsidy is felt right away, but the risks in providing it are stored up over time, and their real costs may not be felt for years or even decades—as was the case in the years leading up to their spectacular collapse in 2008.

Yet this is precisely the fiction that the Obama Administration seeks to preserve by keeping the cost of Fan and Fred off the government's books. The Administration's budget accounting assumes Fannie and Freddie are private companies. So under its preferred treatment, the only recognized cost to taxpayers is the money that is being pumped in to keep them afloat—$110 billion so far.

That's plenty as it is, but in the wake of their government takeover, there is no justification for pretending that their risks aren't taxpayer risks. This is all the more true with the likes of New York Senator Chuck Schumer giving the companies marching orders to rescue tenants in the Stuyvesant Town development in Manhattan.

We suspect the real reason the White House wants Fan and Fred off budget is to disguise their real costs to taxpayers. They have become off-the-books subsidy engines for the housing lobby, and it is easier to push off the recognition of their losses to some future Administration and Congress rather than pay for them today. The new age of transparency has once again died aborning.



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