A Fannie Mae Shareholder Says a Future Draw from Treasury Should be Considered "A Return of Stolen Money"

NEW YORK, Jan. 2, 2018 – Amid recent press reports that because of the reduction in the corporate income tax rate which took effect yesterday, Fannie Mae and Freddie Mac may require a one-time Treasury draw to offset the de-valuation of certain tax assets, Gary Hindes – a shareholder of both companies – says any such payments by Treasury should be characterized as "a return of stolen money".

On September 6, 2008, the federal government seized Fannie and Freddie (the "GSEs") and forced them into Conservatorship. "The original takeover wasn't the 'bailout' they claimed it was at the time; it was a stick-up," Hindes asserts, pointing to the fact that while both companies had been incurring losses due to the housing downturn, they still had the highest capital ratios in their histories, were flush with cash, and had successfully tapped the public securities markets just three days earlier, selling $5.7 billion of unsecured bonds rated AA+ by S&P and AAA by Fitch. The offering was oversubscribed.

Shortly after seizing control and ousting their CEOs, the Federal Housing Finance Agency ("FHFA"), purporting to act as Conservator, ordered the companies to book several non-cash accounting charges, ultimately resulting in Treasury's purchasing $187 billion of preferred shares (bearing a 10 percent dividend) so they could maintain a positive net worth. (AIG and the banks which received federal assistance under the Troubled Asset Relief Program would be charged half that.) By the summer of 2012, however, the housing market had turned around, the accounting entries had to be reversed, and Fannie and Freddie suddenly became massively profitable. Within days of the announcement of second quarter earnings – which far surpassed the dividend – the Conservator agreed to a demand by Treasury to change the dividend to a new rate equal to 100 percent of the companies' earnings and net worth – in perpetuity. By the end of the current quarter, it is estimated that the government will have received over $100 billion more from the GSEs than the $187 billion it provided them. But the terms of the agreement struck between FHFA and Treasury mandate that none of the $287 billion can be used to retire Treasury's preferred shares. Hence, the government's position is that the two companies will continue to owe it $187 billion – and must give it all their profits for the rest of time.

"It was a mafia-type 'loan' from the beginning," Hindes says. "What responsible board of directors – or in this case, a 'Conservator', no less – would borrow $187 billion and agree that no matter how much money they repay the lender, not a dime can be applied towards principal? I mean, who does that? And here's a reality check for you: who borrows that kind of money and pays it all back in just four years? Answer: someone who never needed it in the first place. It was 'cookie jar accounting'."

Under the terms of the FHFA/Treasury deal, Fannie and Freddie were to have seen their capital drained down to zero by year-end 2017. However, on December 21, Treasury agreed to allow each company to maintain $3 billion in capital. That will mean $6 billion in equity for the two combined, against $5 trillion of assets — for a capital ratio of 0.1 percent. (Their capital will continue to round to zero, instead of being precisely zero.) Everything above that will be swept to the government – in perpetuity.

"The idea all along was to saddle Fannie and Freddie with concrete life preservers so that they could not 'escape, as it were'," Hindes said, quoting from an August 18, 2012 White House email to a Treasury official. "And so far, it's worked."

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See also:

The Case of the Concrete Life Preserver

http://delawarebayllc.com/images/The_Case_of_the_Concrete_Life_Preserver.pdf

The Takeover and the Terms

https://howardonmortgagefinance.com/?s=the+takeover+and+the+terms

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