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Banks Want Pieces of Fannie-Freddie Pie

By LOUISE STORY

As the Obama administration prepares a report on the future of Fannie Mae and Freddie Mac, some of the nation's largest banks are offering a few suggestions.

Wells Fargo and some other large banks would like private companies, perhaps even themselves, to become the new housing finance giants helping to bundle individual mortgages into securities — that would be stamped with a government guarantee.

The banks have presented their ideas publicly through trade groups. Housing industry consultants and people familiar with recent meetings at the Treasury Department say these banks view the government's overhaul of the mortgage market as a potential profit opportunity. Treasury officials have met with executives from several institutions, including Wells Fargo, Morgan Stanley, Goldman Sachs and Credit Suisse, according to a public listing of the meetings.

The administration's report, to be released later this month, is expected to be sweeping and could address basic questions like whether a government guarantee is needed at all for middle-class homeowners. While other arms of the government are dedicated to making loans available to lower-income borrowers, Fannie and Freddie have helped lower rates for the bulk of homeowners. Some Republicans are trying to narrow this broad role, and on Thursday, several conservative researchers released a proposal on how to do so. But banks, for their part, have told the administration that removing the guarantee would wipe out the widespread availability of the 30-year mortgage, fundamentally reshaping the American housing market. Though some other countries do not promote long mortgages, some analysts warn that such a change would be devastating to the market here. At firms like Goldman, analysts are predicting that a government guarantee on a broad swath of mortgage securities will survive in some form.

A spokesman for the Treasury declined to comment on the administration's plans, but one former Treasury official warned against the banks' proposal.

"I don't think that private shareholder-owned entities should issue federal government guarantees," said Michael S. Barr, who worked on housing issues at the Treasury Department until the end of last month and then returned to his job as a law professor at the University of Michigan. "I think that creates the same conflict we had in the past."

Mr. Barr said that banks with the largest mortgage businesses had suggested that they be allowed to issue the government's guarantee, setting themselves up as a second-generation of Fannie and Freddie. As for the two housing giants, Mr. Barr said, "No one argues for Fannie or Freddie to continue in their current form. It's just not politically plausible."

Fannie and Freddie have been barred from lobbying the administration or Congress about their future since they were placed in government conservatorship more than two years ago. The companies are able to receive unlimited aid from the Treasury Department until the end of 2012. In the meantime, they are administering some of the government's housing programs and enabling the housing market to sputter along through their guarantee of most new mortgages.

The administration's paper about the future of housing policy will probably address what should be done with Fannie's and Freddie's existing assets, a combined $1.5 trillion portfolio. That is entirely separate from the discussion about the future business model. Lawmakers will eventually decide if Fannie and Freddie will survive and if they can compete in the new model.

One trade association, the Mortgage Bankers Association, has suggested to the Treasury Department that the government might want to auction off Fannie and Freddie's assets, including their brands and their mortgage data, to private companies.

Wells Fargo has been most public in its support of the proposals, but JPMorgan Chase and other large banks helped develop the plans within trade groups. Michael J. Heid, the co-president of Wells Fargo Home Mortgage, testified before Congress last year that allowing private companies to issue the guarantee would add "innovation and efficiency" to the process.

Asked about the proposals from the trade associations, Kristin Lemkau, a JPMorgan spokeswoman, said: "While we are members of these groups, we have not endorsed any specific proposal."

Still, some housing experts critical of the idea warn that giving the large banks a bigger role could lead to an even greater concentration in a market already dominated by a few big players. And they warn that the banks are unlikely to add the affordable housing assistance that Fannie and Freddie provided. Furthermore, they do not see why private entities should profit from the government's good credit standing.

Several housing consultants pointed out that the banks' latest proposals resemble ideas that banks circulated in Washington several years before the financial crisis. Back then, companies like General Electric, Wells Fargo, JPMorgan and the American International Group lobbied through a group called FM Watch, warning that Fannie and Freddie had too much power, had taken on too much risk and had unfair advantages in the marketplace. FM Watch disbanded in 2008, when Congress passed legislation requiring more regulation of the two housing giants.

Representatives of the industry say the entities they are now proposing would be less risky because the government would have strict oversight of them as well as the ability to require hefty amounts of capital to back the mortgage bonds. They also say that companies would pay a fee for the government guarantee, which would cover losses above a certain level. That level has not yet been determined.

In at least one version being proposed, the private companies would have to be separate enough from banks that they could not be pulled down by a bank's collapse. Also, the proposals say the government would guarantee only the mortgage bonds, and not the private companies. However, the government never explicitly guaranteed the survival of Fannie and Freddie or their mortgage bonds; nonetheless it ultimately stepped in to back both.

Still, another trade group, the Housing Policy Council, an arm of the Financial Services Roundtable, expects banks to look for ways to become licensed to help issue government-guaranteed mortgage bonds.

"I wouldn't be surprised if some banks did," said John H. Dalton, president of the council and the former president of Ginnie Mae, an arm of the government that backs mortgages.

John P. Gibbons, an executive vice president of capital markets at Wells Fargo Home Mortgage, said the bank is not eager to own one of the new private companies playing this role, but that it would consider doing so if it thought it was necessary for the market.

"In general we still support those positions because we think they are ways of bringing private capital back into mortgage finance," he said.

It is unclear just how profitable the new business may be. Mr. Heid, the Wells Fargo executive, told Congress that private investors in the companies should receive a "reasonable" return, but he did not say how much.

Jay Brinkmann, chief economist of the Mortgage Bankers Association, which has a similar proposal to the Housing Policy Council's plan, said his group is "not trying to protect profits for a handful of banks."

"I don't think anybody is going to be making the kind of profit that Fannie and Freddie were making in their heyday," he said.

Even if large banks are not allowed to give a government guarantee, they might have control over the private companies by investing in them or by placing representatives on their boards.

There is a risk that small banks would be shut out of the market and consumers would face higher costs on their mortgages, said Mark Willis, resident research fellow at New York University's Furman Center for Real Estate and Urban Policy.

"Some fear that a market ruled by a few large banks will limit access to the secondary market by smaller, local institutions," said Mr. Willis, who visited Treasury officials in November to discuss the issues.

Mr. Willis pointed out that the mortgage market has become more concentrated since the financial crisis, as several prominent originators — like Wachovia and Washington Mutual — hit trouble and were sold to larger banks.

If the government decides to continue offering a guarantee for a broad swath of securities backed by mortgages to middle-class homeowners, it does not have to use a private company. A government agency could issue that guarantee, much the way the Federal Housing

Administration does now for borrowers with lower incomes or other factors that disqualify them from conventional loans.

The banks' proposals also throw out Fannie and Freddie's longtime role in affordable housing. Part of the reason the housing giants enjoyed such broad support from lawmakers was because they aided low-income borrowers. Banking associations say that distorted and endangered the two companies and that any new companies should not be saddled with those responsibilities. Instead, the banks say, the private companies could pay a fee to the government to support such lending.