



U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, DC 20410-8000

ASSISTANT SECRETARY FOR HOUSING-
FEDERAL HOUSING COMMISSIONER

JAN 9 2006

Mr. Daniel H. Mudd
Chairman and Chief Executive Officer
Fannie Mae
3900 Wisconsin Avenue, NW
Washington, DC 20016-2892

Dear Mr. Mudd:

By this letter, the Department of Housing and Urban Development is informing Fannie Mae of the results of the Department's review of Fannie Mae's single-family real estate-owned ("REO") activities. HUD requested information and documents regarding Fannie Mae's REO activities on April 6, 2005, particularly information regarding REO services for properties secured by mortgages in which Fannie Mae holds no legal or beneficial ownership interest at the time that the services are rendered ("third-party REO"). Fannie Mae provided the requested information, including a legal opinion regarding Fannie Mae's authority to offer third-party REO services, by letter dated April 27, 2005.

The Department has completed its review of this information and has determined that Fannie Mae's Charter Act does not authorize Fannie Mae to perform third-party REO services. Specifically, the Department has determined that the third-party REO disposition agreements with

, and certain features of the two agreements with , do not directly serve the purposes for which Fannie Mae was created, nor do they fall within the scope of the express or incidental powers and authority of Fannie Mae under its Charter Act and, accordingly, are not authorized.

An activity is consistent with Fannie Mae's Charter Act (the "Charter Act") only if: (a) it is authorized by Fannie Mae's express powers under the Charter Act and (b) it furthers one or more of the purposes set forth in section 301 of the Charter Act. The statutory purposes in section 301 of the Charter Act all relate to the creation, through Fannie Mae, of secondary market facilities for residential mortgages. Consequently, while section 302(b)(2) of the Charter Act expressly authorizes Fannie Mae to "purchase, *service*, sell, lend on the security of, or otherwise deal in" conventional mortgages, this authority must directly relate to, and be an integral part of, Fannie Mae's secondary market facilities. (Emphasis added.)

Moreover, it is the Department's view that section 309(a) of the Charter Act, which authorizes Fannie Mae to do all things "necessary or incidental" to the conduct of its business, does not provide an independent authorization for program operations. Those incidental activities undertaken by Fannie Mae in the conduct of its business must bear a direct relationship to the express authorities and the programs undertaken pursuant to such authorities.

The Department acknowledges that servicing includes the conduct, when necessary, of post-foreclosure property disposition services. However, consistent with the above standards, the Department has determined that Fannie Mae may conduct REO disposition services only for properties whose mortgages were purchased by Fannie Mae for its secondary market operations and in which Fannie Mae continues to hold a legal or beneficial ownership interest at the time that it performs the REO services.

In applying this standard to the facts presented, the Department has determined that the [redacted] agreements are not authorized under the Charter Act.¹ Although Fannie Mae previously purchased the mortgages for its secondary market operations, it does not have either a legal or beneficial ownership interest at the time it conducts its REO disposition services. Instead [redacted] have repurchased the mortgages, which extinguishes Fannie Mae's legal and beneficial ownership interest in those mortgages. Accordingly, Fannie Mae must terminate the [redacted] agreements immediately.

Fannie Mae also has [redacted] agreements with [redacted] for mortgages held by trusts and serviced by [redacted]. The first agreement pertains to the [redacted] transaction, in which Fannie Mae acquired a [redacted] interest in a pass-through security collateralized by certain [redacted] mortgages. The [redacted] agreement pertains to the [redacted] transaction, in which Fannie Mae issued guaranteed securities indirectly backed by a subset of mortgages from the [redacted] transaction. Fannie Mae purchased these mortgage securities and currently owns them.

Fannie Mae's acquisition of the securities backed by the [redacted] mortgages qualifies as a "mortgage purchase" for its secondary market operations, and its continuing ownership interest in the securities backed by the [redacted] mortgages qualifies as a beneficial ownership interest in the mortgages that is sufficient to authorize the associated REO services. Accordingly, Fannie Mae does not have to terminate these [redacted] agreements to the extent that Fannie Mae performs post-foreclosure REO services on mortgages owned by [redacted] and for which Fannie Mae continues to own the related securities.

The [redacted] agreements also provide for certain REO services that are not authorized. The [redacted] agreement provides for Fannie Mae to continue to perform, and to be compensated for, REO services even if it sells its securities backed by [redacted] mortgages. Moreover, both the [redacted] agreement and the [redacted] agreement provide that, upon referral to Fannie Mae by [redacted] Fannie Mae will conduct REO disposition services for properties that secured mortgages that Fannie Mae does not own. Because the [redacted] agreements contemplate that Fannie Mae can provide REO services in connection with mortgages that Fannie Mae does not own and mortgages collateralizing securities that Fannie Mae does not own (i.e. Fannie Mae holds no beneficial ownership interest in the mortgages) at the time it performs the REO services, Fannie Mae must discontinue these REO disposition services immediately.

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To verify completion of these actions, Fannie Mae must notify the Department in writing when all unauthorized agreements and services described herein have been terminated or otherwise discontinued. If Fannie Mae has entered into any third-party REO agreements subsequent to the information submitted to the Department on April 27, 2005, and Fannie Mae does not hold a legal or beneficial ownership interest in the mortgages at the time it performs the REO services, then these agreements must also be terminated.

Should you have any questions about the Department's determinations described herein, please do not hesitate to contact either Sandra L. Fostek, Director, Office of Government Sponsored Enterprises Oversight or me.

Sincerely,

A handwritten signature in black ink, appearing to read "B. Montgomery", written over a horizontal line.

Brian D. Montgomery
Assistant Secretary for Housing-
Federal Housing Commissioner

cc:

Anthony F. Marra
Senior Vice President and
Deputy General Counsel
Fannie Mae