The Delaware Bay Company LLC

"Let the people know the facts and the country will be safe." – A. Lincoln.

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FANNIEGATE: THE COVER-UP UNRAVELS.

Forced by Court Order, the Government Turns Over Documents Evidencing Perjury and Obstruction of Justice.

OBAMA ADMINISTRATION KNEW THE GSES WERE ON THE VERGE OF RECORDING RECORD PROFITS – BUT DOJ CONTINUES TO TELL THE COURTS THEY WERE IN A PURPORTED "DEATH SPIRAL".

Proof the September '08 takeover wasn't a 'bailout', *it was a stick-up.*

WHEN WILL A JUDGE HAVE THE COURAGE TO SAY: *"ENOUGH!"?*

In our last exciting episode, *"The Case of the Concrete Life Preserver"* (*HINDESight™* Nov. 25, 2016), I related how the Obama Administration was withholding over 11,000 documents from public scrutiny due to "national security" concerns. National security indeed. As it turns out, the documents in question have nothing to do with national security and everything to do with keeping perjury and obstruction of justice by top White House and Treasury Department officials from coming to light.

Last week, some 3500 of those documents were finally produced to the plaintiffs in *Fairholme Funds v. United States* (No. 13-465 Fed. Cl.) under court order (natch). It ain't a pretty picture – and if Mr. Trump and his people really want to drain the swamp, **Treasury** and the **Federal Housing Finance Agency** ("FHFA") are good places to start. In the meantime, the **Inspectors General** of both agencies should open formal investigations.

In courts around the country – including the Fifth, Sixth, Seventh, Eighth, and District of Columbia Circuits – FHFA (Conservator of **Fannie Mae** and **Freddie Mac**) and Treasury continue to assert that the imposition of the unprecedented Net Worth Sweep in August 2012 was necessary because it "*arrested the draws-to-pay-dividends cycle that threatened to erode Treasury's unused funding commitment.*" (U.S. Treasury Brief, 8th Circuit Court of Appeals, June 27, 2017). However, the newly unsealed documents prove that this explanation for the Net Worth Sweep is patently **false**. Furthermore, we now know that both agencies anticipated that the Companies' future profits would **exceed** the 10 percent cash dividend rate that Fannie and Freddie had been required to pay prior to the imposition of

the Net Worth Sweep. And far from imposing the Net Worth Sweep to somehow help or assist the Companies, these documents show that the purpose was to dramatically **increase** the amount of money paid to the government (at a time when Treasury was desperately looking for additional sources of cash to avoid hitting the debt ceiling and triggering a GOP-threatened government shutdown) – and to **prevent** Fannie and Freddie from ever rebuilding capital or exiting conservatorship – a blatant violation of federal law. Indeed, as Treasury and FHFA anticipated, the Net Worth Sweep has enabled Treasury to seize an additional *$130 billion* from these two publicly traded, shareholder-owned companies over and above the 10 percent dividend to which it otherwise would have been entitled.

Obviously, I haven't had time to get through all the documents, but Fairholme's **Dan Schmerin** points out the following highlights:

1. FHFA and Treasury repeatedly acknowledged that the conservator has a legal obligation to preserve and conserve the Companies' assets and restore them to soundness and solvency, but chose to ignore these statutory imperatives by imposing the Net Worth Sweep.

Treasury documents acknowledge that *"FHFA as conservator is required to preserve assets,"* (UST00473629, at 12) and that one of the legal constraints imposed on FHFA is its *"mandate to 'conserve assets.'"* (UST00406435). FHFA similarly recognized it "*has a responsibility to take such actions as may be necessary to put the Enterprises in a sound and solvent condition and to preserve and conserve their assets and property*." (FHFA00105087, at 7). A December 12, 2011 memorandum from **Mary Miller**, assistant secretary for financial markets, to Treasury Secretary **Tim Geithner** emphasized the distinction between conservatorship and receivership: *"Considerations: First, in conservatorship the entities are treated as going concerns, and FHFA as conservator is required to preserve assets. In receivership, the entities would be in wind-down* (i.e., liquidation)*, and FHFA as receiver would be looking to sell the assets for as much money as it could*". Indeed, Ms. Miller was so concerned about liquidating the GSEs (which it has effectively done via the Net Worth Sweep) that she feared Treasury's own preferred stock in the GSEs might be *"wiped out in receivership."* (UST00473640).

2. FHFA forced the Companies to make unjustified loan loss reserve and deferred tax asset accounting decisions that artificially increased the Companies' draws from Treasury, thereby giving the appearance that they required a bailout when they did not.

A key document which the government has fought tooth-and-nail to keep secret is a confidential, in-depth analysis of the GSEs' financial prospects which Treasury had ordered up just a month before **Hank Paulson** showed up on their doorsteps with his bazooka. We now learn that Treasury had been told by the noted investment firm **BlackRock, Inc.** that, for instance, Freddie's *"long-term solvency does not appear endangered – we do not expect Freddie Mac to breach critical capital levels even in stress case*." (FHFA00056237, at 3). But that simply would not do for a Treasury Department which saw in the then-chaotic conditions of the financial crisis an opportunity to nationalize Fannie Mae and Freddie Mac without compensating their owners. So, as I have previously described in *"The Myth of Private Gains and Public Losses"* (HINDESight™ Sept. 6, 2016), once they had control, Treasury and FHFA ordered the GSEs to start booking wildly inflated paper losses. Absent those unjustified, unnecessary, and erroneous accounting entries (virtually all of which had to be reversed four years later), Fannie and Freddie would have needed little or no money from Treasury. It wasn't a bailout, it was a stick-up.

3. Contrary to their public statements, the Obama White House and Treasury knew that the Net Worth Sweep would result in a windfall for the federal government.

An email from a Treasury official dated July 20, 2012, recognized the possibility that restructuring the dividend would lead to "*a better outcome*" for Treasury in light of projections about the Companies'

future profitability. (UST00555247). A question-and-answer document circulated among Treasury officials on July 20, 2012, stated that Treasury would be *"in a better position*" after the Net Worth Sweep because "*the GSEs would be making a binding contractual commitment to turn over profits to taxpayers, as opposed to the current discretionary dividend*." (UST00061432). And on August 13, 2012, **Jim Parrott** – the White House official who worked most closely with Treasury in concocting the Net Worth Sweep – wrote in an email that *"we are making sure that each of these entities pays the taxpayer back every dollar of profit they make, not just a 10% dividend"* and that *"the taxpayer will thus ultimately collect more money* with the changes." (UST00061143)

These previously withheld internal agency communications directly contradict the sworn declaration of former Treasury and FHFA official **Mario Ugoletti**, who stated on December 17, 2013, under penalty of perjury that: *"These changes in structure did not change the underlying economics of the PSPAs … Treasury would receive as much from the Enterprises under the Second Amendment as it would under the Third Amendment. Thus, the intention of the Third Amendment was not to increase compensation to Treasury – the Amendment would not do that – but to protect the Enterprises from the erosion of the Treasury commitment that was threatened by the fixed dividend"* (i.e., the "death spiral" excuse).[1] (D.D.C. Case 1:13-cv-01025-RLW Document 27-2 Filed 12/17/13)

Presciently, a Treasury official named **Benson Roberts** observed in an August 13, 2012 email that the "death spiral" explanation that both agencies trumpeted when announcing the Net Worth Sweep (and which the Trump DOJ repeated in a court filing less than a month ago) **"doesn't hold water."** (UST00406517, at 13).

4. The Net Worth Sweep was purposely timed to coincide with the Companies' return to sustained profitability so as to achieve Treasury's extralegal policy objective of eliminating both Companies.

An email from **Brian Deese** at the White House on July 22, 2012, to Treasury officials reveals Treasury's desire to impose the Net Worth Sweep swiftly: *"Gene and I are concerned about timing … if you* [Treasury] *guys are landing on moving out fast we should discuss*." (UST00517876). An internal Treasury document prepared on July 30, 2012, stated that the Net Worth Sweep should be announced shortly after August 7, when *the "GSEs will report very strong earnings . . . that will be in-excess of the 10% dividend to be paid to Treasury*," (UST00533618) and on August 1, 2012, a Treasury official emphasized that the Net Worth Sweep should be announced in mid-August *because Fannie and Freddie's "earnings will be in excess of current 10% dividend paid to Treasury*." (UST00385572). A Treasury official observed on August 13, 2012, that the imposition of the Net Worth Sweep was *"really a mechanical means to broader policy objectives,"* and questioned *"How can we argue that* (government) *ownership/control is temporary if we will be sweeping their* (entire) *net worth? Doesn't that ensure the GSEs will have no exit from conservatorship*?" (UST00406521). Finally, a Q&A document prepared by Treasury on August 13, 2012, revealed the motivation to promptly impose the Net Worth Sweep: "*Given their improvement in operating performance and our intention to wind them down, we think the current steps being taken are appropriate*." (UST00406521)

'May' versus 'shall'

Alas, only one federal judge has disagreed with Treasury and FHFA's position that under the law, no court can review their decisions when it comes to the GSEs – but that one was in a vigorous dissenting opinion. All others have piggybacked off Judge **Royce C. Lamberth**'s September 2014 Opinion dismissing Fairholme's lawsuit, a decision which was upheld 2-1 at the **U.S. Court of Appeals for the District of Columbia Circuit**. But as dissenting Judge **Janice Rogers Brown** pointed out, the majority's logic makes no sense. It cited the portion of the law which says

[1] You can't make this stuff up: Mr. Ugoletti left the government in September 2015 and is reportedly living in Ecuador – which is said to have an enviably loopholed extradition treaty with the United States. http://www.valuewalk.com/2016/04/unsealed-gse-litigation-documents-show-government-claims-filings-questionable-best/.

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that as conservator, FHFA *"may take such actions as may be necessary to put the Enterprises in a sound and solvent condition and to preserve and conserve their assets and property*." According to the Court of Appeals, because the statute uses the word "*may*" instead of "*shall*", FHFA's duty is not obligatory, but merely optional[2] – and its director has unfettered leeway to do whatever he wishes with Fannie and Freddie's assets (including, if he deems it in their or his agency's best interest, selling said assets to his brother-in-law). Of course, this position is simply preposterous and it is, frankly, shameful that Senior Judge **Douglas Ginsburg** decided to go along with Judge **Patricia Millet**'s patently outlandish logic. Admittedly, neither had the benefit of the documents which have only now been made public – nor, for that matter, have any of the other judges. And while the D.C. Circuit's decision is not binding on any of the other circuits, at least three have appeals pending and have yet to weigh in. You can be sure that they will shortly be provided with the newly-released evidence which proves beyond a doubt that the government has been lying all along and that, indeed, the very act of trying to keep those documents secret and hide them under a cockamamie theory that allowing the public to see what is in them would create panic and cause another major financial crisis, is (in my opinion, at least), a clear act of obstructing justice.

The evidence of what happened here is overwhelming – and gets stronger and stronger with each turn of the page. Nonetheless, shareholders await one brave jurist who has the courage, the decency, the honesty, the moral outrage to say: *enough*!".

[2] Really? See item 1 above.