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The Department of the Treasury's Authority to Regulate GSE Debt: A Legal Analysis

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Summary

Reports have recently surfaced that the Department of the Treasury may soon seek to exercise its approval authority over Fannie Mae's and Freddie Mac's debt issuances in a different manner than it has in the past. While the Department of the Treasury has traditionally used its approval authority merely to coordinate the timing of debt issuances, the Department may soon seek to regulate the amount of debt that Fannie Mae and Freddie Mac may issue. This report analyzes the Department of the Treasury's legal authority over Fannie Mae and Freddie Mac and concludes that a court would likely hold that the Department possesses the power to regulate the amount of debt issued by these two organizations.

Introduction

In the wake of an accounting scandal involving the Federal National Home Loan Corporation (Freddie Mac), various members of Congress have launched efforts to tighten oversight of Freddie Mac and its sister organization, the Federal National Mortgage Association (Fannie Mae).[1] As legislative efforts to increase the oversight of these two entities are still pending,[2] it has been reported that the Department of the Treasury may soon assert that it has the power to regulate Fannie and Freddie's debt issuances much more strongly than it has in the past.[3] According to these reports, the Treasury

[1] For more information on the history and functions of these two organizations, *see* CRS Report RS21748, *Fannie Mae and Freddie Mac: An Overview*, by Nathan Brooks and Barbara Miles.

[2] The 108th Congress has considered a variety of legislative proposals to strengthen oversight of Fannie and Freddie (*See, e.g.*, H.R. 2575 (108th Cong.)), although those efforts appear to have stalled.

[3] The Treasury Department has issued no formal indication that the Department is planning to exercise this power. Reports have recently surfaced, however, indicating that Treasury is considering this action. *See, e.g.*, David S. Hilzenrath, *New Tack in Mortgage Firm Oversight*, (continued...)

Department would trace this authority to language in Fannie and Freddie's charters. The Fannie Mae charter provides Fannie Mae the authority to issue obligations "upon the approval of the Secretary of the Treasury, and have outstanding at any one time obligations having such maturities and bearing such rate or rates of interest as may be determined by [Fannie Mae] with the approval of the Secretary of the Treasury."[4] The Treasury Secretary has the same authority over Freddie Mac's securities issuances.[5]

The Treasury Secretary has traditionally exercised the approval authority with regard to Fannie and Freddie's debt issuances not to prevent them from issuing such debt, but rather to time such issuances so that they do not conflict with the Department of the Treasury's own debt issuances. In other words, the Department of the Treasury has traditionally acted as a "traffic cop" with regard to Fannie and Freddie debt issuances as part of an overall effort to coordinate the federal government's debt issuances. According to officials from Fannie and Freddie, while the Treasury Department has this authority over the *timing* of debt issuances (i.e., asking Fannie or Freddie to change the dates of their offerings), Treasury has never used its power in such a way as to control the amount of debt offered.[6] As mentioned above, however, reports have circulated that the Treasury Department may soon seek to exercise its approval authority not in the usual "traffic cop" manner, but rather to regulate the amount of debt that Fannie and Freddie can issue.[7]

Analysis

The Supreme Court held in *Chevron, Inc. v. Natural Defense Resources Defense Council*[8] that courts should defer to a reasonable agency interpretation of an ambiguous statute that the agency is charged with administering. This *Chevron* deference is only available to interpretations of an agency to which Congress has delegated the authority to make "rules carrying the force of law."[9] Generally, then, *Chevron* deference is warranted for agency interpretations arrived at after formal adjudication or notice-and-comment rulemaking.[10] Actions pursuant to any less formal interpretations are "entitled to respect" under an earlier case, *Skidmore v. Swift Co.*[11] Because it is not clear how — or even if — the Treasury Department plans to issue an interpretation, we will analyze the

[3] (...continued)
Washington Post, April 30, 2004, at E4.

[4] 12 U.S.C. § 1719(b).

[5] 12 U.S.C. § 1455(j).

[6] *See* David S. Hilzenrath, *New Tack in Mortgage Firm Oversight*, Washington Post, April 30, 2004, at E4.

[7] *Id.*

[8] 467 U.S. 837 (1984).

[9] *United States v. Mead Corp.*, 533 U.S. 218, 226-227 (2001).

[10] *See Christensen v. Harris County*, 529 U.S. 576, 587 (2000).

[11] 323 U.S. 134, 140 (1944). For a discussion of the different levels of deference due to agency interpretations, *see* Thomas W. Merrill and Kristin E. Hickman, *Chevron's Domain*, 89 Geo. L.J. 833 (2001).

strength of the Treasury Department's reported proposed interpretation under both *Chevron* and *Skidmore*.

***Chevron* Deference.** *Chevron* analysis requires a two-step inquiry. First, the court must ask if the statute is ambiguous. If not, then the court simply rules according to the clear meaning of the statute. If the statute is ambiguous, though, the court must determine if the agency's interpretation is reasonable. If so, then the court must defer to that interpretation. Here, it would seem that the analysis would end after the first prong. The statute is not ambiguous; it vests approval authority in the Secretary of the Treasury. Here, the language in both statutes clearly gives the Treasury Secretary approval authority over Fannie and Freddie's debt issuances. There is nothing in the statutory language to suggest that this approval authority is limited to the "traffic cop" role through which the Secretary has traditionally exercised this power. The statutory language in both Fannie Mae's and Freddie Mac's charters condition the issuance of debt obligations upon the approval of the Secretary of the Treasury. The power to approve seems to clearly imply the concomitant power to *disapprove*.[12] Indeed, the power to approve would be no power at all if an agency did not have the ability to withhold that approval.

There is one notable Supreme Court case where the Court — faced with clear statutory language — used superceding congressional and agency action to find ambiguity under the first *Chevron* prong. In *FDA v. Brown & Williamson Tobacco Corp.*,[13] the FDA had interpreted its statutory mandate to regulate "drugs" and "devices" to give the agency the power to regulate tobacco. The Supreme Court, however, looked at the FDA's long history of disclaiming authority over tobacco, and the fact that Congress had legislatively addressed tobacco regulation separately six times to find a congressional intent contrary to the agency's proposed interpretation.[14] There is no such history here which would force a reviewing court to look beyond the language of the statute. Congress has passed no legislation evincing a different congressional intent from what the language indicates. Further, Congress has not created a separate regulatory scheme for the regulation of Fannie and Freddie's debt issuances.

Moreover, unlike the FDA in *Brown & Williamson*, the Treasury Department has never disclaimed or receded from its authority to regulate in this area. While the Department has never exercised this authority to stop Fannie and Freddie from issuing debt, the statutory authority to do so is still on the books. Given that the Treasury Department has this authority, then, there appears to be nothing to prevent the Department from exercising it in a different way. As the Supreme Court has held, agencies must be allowed to "adapt their rules and policies to the demands of changing circumstances."[15]

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[12] *See, e.g., State v. Duckett,* 130 S.E. 340 (S.C. 1925) ("Approval implies knowledge and exercise of discretion after knowledge"); *McCarten v. Sanderson,* 109 P.2d 1108 (Mont. 1941).

[13] 529 U.S. 120 (2000).

[14] *Id.* at 137-138.

[15] *Motor Vehicles Mfrs. Assoc. of the United States, Inc., v. State Farm Mutual Automobile Insur. Co.*, 463 U.S. 29, 42 (1983).

While it seems doubtful that a court using the *Chevron* analysis would even get to the second prong of that analysis, the Treasury Department's reported proposed exercise of authority would very likely be legal under *Chevron*'s second prong. Under this highly deferential prong, a court must accept an agency's interpretation so long as that interpretation is reasonable — whether or not the court agrees with it. For the same reasons discussed above, it is hard to imagine bases upon which a court would find the Treasury Department's reported proposed interpretation here to be unreasonable. If Congress wanted to limit the Treasury Department's approval authority, then Congress could have done so. Because Congress chose instead to use broad language in describing Treasury's authority, it follows that a broad interpretation of that authority would likely be judged to be reasonable.

***Skidmore* Deference.** While *Chevron* requires a court to defer to an agency interpretation of an ambiguous statute — whether or not the court agrees with that interpretation — so long as it is reasonable, an agency interpretation under *Skidmore* is merely guidance, the weight of which depends on a variety of contextual factors, including the thoroughness evident in the agency's consideration of the interpretation, the validity of its reasoning, its consistency with earlier and later pronouncements, "and all those factors which give it power to persuade, if lacking power to control."[16] In essence, under the *Skidmore* analysis, the court will determine the statute's meaning — merely taking into account the agency's interpretation as one tool among the many statutory interpretation tools used by courts — unless the agency can convince the court that the agency has some special body of knowledge warranting greater deference.[17]

One of the most basic premises of statutory construction is that the statutory language itself should be the initial touchstone for analysis. The Supreme Court has consistently stated that "the meaning of the statute must, in the first instance, be sought in the language in which the act is framed, and if that is plain ... the sole function of the courts is to enforce it according to its terms."[18] As mentioned above, the statutory language at issue here unambiguously grants approval power to the Secretary of the Treasury without any qualifying language limiting the exercise of this power in any way. Further, as the Supreme Court has stated, "legislative history is irrelevant to the interpretation of an unambiguous statute."[19]

While the general rule is that extrinsic aids such as legislative history are only to be used when a statute is unclear and ambiguous, there is no rule which forbids a court from examining legislative history of clear language.[20] Courts have on occasion allowed the admission of legislative history to interpret unambiguous statutes where that history

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[16] 323 U.S. at 140.

[17] *See* Jim Rossi, *Respecting Deference: Conceptualizing Skidmore Within the Architecture of Chevron*, 42 Wm. & Mary L. Rev. 1105, 1131 (April 2001).

[18] *Caminetti v. United States*, 242 U.S. 470, 485 (1917); *see also United Air Lines, Inc., v. McMann*, 434 U.S. 192, (1997).

[19] *United Air Lines, Inc., v. McMann*, 434 U.S. 192, 199 (1997).

[20] 2A Sutherland's Statutory Construction § 48.01 (1992).

clearly expresses a legislative intent contrary to the language.[21] It is important, then, to examine the legislative history and see if it points strongly against the interpretation that the language appears to command.

It was in 1968 that Congress inserted into Fannie Mae's charter the aforementioned language authorizing Fannie Mae to issue debt with the Secretary of the Treasury's approval.[22] The House report that accompanied the legislation stated in clear terms that this language was intended to aid the Treasury Secretary in ensuring that Fannie Mae stays true to its mission:

> The [Treasury] Secretary would have general regulatory powers over FNMA to assure that the purposes of the Charter Act are served. The issuance of all securities or obligations by FNMA would have to receive the prior approval of the Secretary. Through this and other authority, the Secretary would participate in the decision making process at the level of mortgage purchases at various times.[23]

While both the statutory language and the legislative history point to a broad authority vested in the Treasury Secretary to regulate Fannie Mae's debt issuances, the Secretary has traditionally used this power not to disapprove of proposed issuances, but rather to coordinate such issuances so as not to conflict with the Treasury Department's debt issuances.[24] One House Committee clearly had this in mind in 1989, when Congress gave Freddie Mac powers similar to those held by Fannie Mae to issue debt.[25] While the House Report that accompanied that legislation stated that one of the overarching purposes of the statute was to give Freddie Mae powers and authority parallel to those enjoyed by Fannie Mae,[26] Part III of the House Report, submitted by the Committee on Banking, Housing, and Urban Affairs, also offered a very different picture of how the Committee expected the Treasury Secretary to exercise the approval authority:

> The title also grants the Secretary of the Treasury certain approval authorities over [Freddie Mac's] issuance of unsecured debt obligations and mortgage-related securities. Treasury already possesses such powers over [Fannie Mae] ... The Committee intends that the Treasury shall use these powers solely to ensure that [Freddie Mac's] financing activities are conducted in a way that promotes [Freddie Mac's] statutory purpose. *In fulfilling this responsibility, and as is the case with [Fannie Mae], the Committee expects that Treasury will function largely as a "traffic cop" to assure that securities issued or guaranteed by [Freddie Mac] are marketed*

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[21] *See, e.g., Escobar Ruiz v. Immigration and Naturalization Service*, 838 F.2d 1020 (9th Cir. 1988).

[22] P.L. 90-448, § 804(a).

[23] H.R. Rep. No. 90-1585 (1968), *reprinted in* 1968 U.S.C.C.A.N. 2873, 2946.

[24] *See* David S. Hilzenrath, *New Tack in Mortgage Firm Oversight*, Washington Post, April 30, 2004, at E4 ("Freddie Mac spokeswoman Sharon McHale said the Treasury Department has never used that clause to control the amount of debt the company has issued or the interest rates on the debt. Instead, the Treasury has asked the company to change the dates of some offerings so they would not interfere with the government's sale of Treasury securities, McHale said").

[25] P.L. 101-73, § 731(i).

[26] H.R. Rep. No. 101-54(III) (1989), *reprinted in* 1989 U.S.C.C.A.N. 86, 385.

> *in an orderly way in appropriate coordination with the financing activities of the Treasury and other government-sponsored enterprises (GSEs)*[27] [Emphasis added].

At first glance, then, it appears possible that Congress had a different intent in mind when it granted this approval authority to the Secretary of the Treasury. Put simply, while the statutory language regarding the Treasury Secretary's authority here is clear, one could argue that Congress's understanding of that authority may have changed in between the time it was granted over Fannie Mae and when it was granted to Freddie Mac, due to the way that the Treasury Department had traditionally chosen to exercise this authority.

For a variety of reasons, however, the above-quoted report language from 1989 would not likely be enough to convince a court that the Secretary of the Treasury's power is limited here. First and foremost, the language represents the opinion of one committee, not the entire Congress. The Supreme Court has made it clear that a committee's direction cannot be equated with a statute passed by Congress.[28] Under the Constitution, federal statutes must pass both Houses of Congress and be signed by the President to have legal effect. As the Supreme Court has stated, "unenacted approvals, beliefs, and desires are not laws."[29] This is not to suggest that Committee reports are not important interpretive tools. On the contrary, such reports are among courts' favorite sources of interpretation. Such sources, however, cannot be divorced from the statutory language. In other words, "Courts have no authority to enforce [a] principle gleaned solely from legislative history that has no statutory reference point."[30] In this case, Congress could have chosen to enact language explicitly limiting the Treasury Secretary's authority to the "traffic cop" function described above. Congress chose not to do so, however.

Even if the report language were to be given greater weight, however, the language itself does not evince an intent to completely constrain the Treasury Secretary's authority. The language describes an expectation that — with regard to securities and debt issuances — the Department would function "*largely* as a 'traffic cop.'" This use of the word "*largely*" as opposed to "*only*," suggests that there are other, unenumerated ways in which Treasury could exercise that authority.

Lastly, the legislative history does not provide a clear Congressional intent that courts should depart from the clear statutory language. At best, the scant legislative history available on this question provides a confusing conflict between two committee reports. In addition to the clear language, as mentioned above, a reviewing court using the *Skidmore* analysis would weigh the opinion of the Treasury Department. The likely final result under the *Skidmore* analysis, then, appears to be the same as that under *Chevron* deference.

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[27] H.R. Rep. No. 101-54(III) (1989), *reprinted in* 1989 U.S.C.C.A.N. 86, 386.

[28] *See TVA v. Hill*, 437 U.S. 153, 191 (1969).

[29] *Puerto Rico Dept. of Consumer Affairs v. Isla Petroleum Corp.*, 485 U.S. 495, 501 (1998).

[30] *Shannon v. United States*, 512 U.S. 573, 581 (1994) (quoting *International Brotherhood of Elec. Workers v. National Labor Relations Board*, 814 F. 2d 697, 712 (D.C. Cir. 1987).