

Federal Housing Finance Agency
Office of Inspector General



Compliance Review of FHFA's Handling of Fannie Mae's Confidential Conservator Requests

Compliance Review • COM-2021-006 • July 21, 2021



COM-2021-006

July 21, 2021

Executive Summary

The Federal Housing Finance Agency (FHFA or Agency) placed Fannie Mae and Freddie Mac (collectively, the Enterprises) in conservatorship in 2008. Pursuant to the Housing and Economic Recovery Act of 2008 (HERA), FHFA is empowered to operate the Enterprises “with all the powers of the shareholders, the directors, and the officers” while they remain in conservatorship.

After placing the Enterprises into conservatorship, FHFA delegated specified general corporate governance authority to each Enterprise’s board of directors (Board) and addressed specific governance matters. In particular, the Agency delegated to the Boards various responsibilities, including but not limited to: (1) developing a succession plan for Board positions, the Chief Executive Officer (CEO), and President, and (2) selecting candidates for those positions when vacant, which are subject to review by FHFA, as conservator. According to FHFA, it has chosen to approve such selections after review. FHFA has retained the responsibility to approve compensation actions for senior executive officers.

Our 2019 evaluation found that a former FHFA Director overrode Agency internal controls for approving conservator requests by reviewing and approving Fannie Mae’s Board Transition Plan by himself, without any staff analysis or recommendation. As a result, the former Director and a Special Advisor were the only FHFA employees aware of the former Director’s approval of the Board Transition Plan, upon which the former Director had imposed specific conditions that were not recorded in the Agency’s conservator Status Tracking and Reporting System (STAR). Because these employees were not aware of the former FHFA Director’s approval conditions, they did not know to track whether any of them had been satisfied. At the time of our 2019 evaluation, the record reflected that two of those conditions had not been met.

We made two recommendations to address these deficiencies, the second of which was to establish a process for maintaining and monitoring sensitive conservator requests in STAR. FHFA agreed with this recommendation. In July 2019, the Agency updated its STAR system user guide to include procedures for managing sensitive, or confidential, information. We closed this recommendation on September 12, 2019, based on those actions.

In January 2021, we initiated this compliance review to determine whether FHFA maintained and monitored confidential conservator requests submitted by Fannie Mae from October 1, 2019, through June 9, 2021 (review period). Based upon our testing, we found that FHFA’s corrective actions, which



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evolved during our review period, complied with our recommendation that it establish a process for maintaining and monitoring sensitive conservator requests in the Agency's STAR system.

This report was prepared by Alisa Davis, Senior Policy Advisor, with assistance from Patrice Wilson, Senior Investigative Evaluator. We appreciate the cooperation of FHFA staff, as well as the assistance of all those who contributed to the preparation of this report.

This report has been distributed to Congress, the Office of Management and Budget, and others and will be posted on our website, www.fhfaoig.gov.

/s/

Brian W. Baker
Deputy Chief Counsel

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ABBREVIATIONS

Agency or FHFA	Federal Housing Finance Agency
Board	Enterprise Board of Directors
CEO	Chief Executive Officer
DOC	FHFA’s Division of Conservatorship
DOR	FHFA’s Division of Resolutions (formerly DOC)
Enterprises	Fannie Mae and Freddie Mac, collectively
Fannie Mae	Federal National Mortgage Association
HERA	Housing and Economic Recovery Act of 2008
LOI	Letters of Instruction
OIG	Federal Housing Finance Agency Office of Inspector General
Review Period	October 1, 2019 – June 9, 2021
STAR	DOR’s Status Tracking and Reporting System

BACKGROUND

As Conservator, FHFA Exercises Sweeping Statutory Powers

HERA charges FHFA with supervision and regulation of the Enterprises and the Federal Home Loan Bank System. HERA authorized FHFA to place the Enterprises into conservatorship, which it did in 2008. As conservator, FHFA may operate the Enterprises “with all the powers of the shareholders, the directors, and the officers.”¹ These powers position FHFA to potentially control every aspect of the Enterprises’ governance and operations.

FHFA Has Delegated Certain Authorities Back to the Enterprise Boards

After placing the Enterprises into conservatorship in September 2008, FHFA delegated specified general corporate governance authority to each Board and addressed specific governance matters.² In conjunction with these delegations, FHFA issued to the Boards the first Letters of Instruction (LOI) that defined and outlined the scope of delegated and undelegated authorities. FHFA has subsequently revised the LOIs, which delegate to the Boards various responsibilities, including but not limited to: (1) developing a succession plan for Board positions, the CEO, and President; and (2) selecting candidates for those positions when vacant, which are subject to review by FHFA, as conservator. According to FHFA, it has chosen to approve such selections after review. FHFA has retained the responsibility to approve compensation actions for senior executive officers.

FHFA’s Division of Resolutions (DOR)³ evaluates the Enterprises’ requests for conservatorship approval and facilitates FHFA’s review of – and decisions regarding – such requests. To those ends, STAR is DOR’s internal tracking and reporting system for conservator decisions. In addition to STAR, DOR has used an electronic shared drive to store information related to the Enterprises’ submissions.

A Former FHFA Director Overrode DOR’s Conservator Decision-Making Controls

FHFA has established internal controls for DOR’s processing, tracking, and monitoring of Enterprise requests for conservator approval. We found that a former FHFA Director

¹ See 12 U.S.C. § 4617(b)(2)(B)(i), (D)(ii).

² Conservatorship Order No. 2008-006 issued November 24, 2008. For a general discussion of the authorities delegated by FHFA to the Boards under its different orders and LOIs, see OIG, *FHFA Letters of Instruction to the Enterprises* (July 23, 2018) (WPR-2018-004) (online at www.fhfaig.gov/sites/default/files/WPR-2018-004.pdf).

³ DOR was formerly named the Division of Conservatorship (DOC). This report refers to the division by its current label, DOR.

overrode those controls by reviewing and approving Fannie Mae’s Board Transition Plan by himself, without any staff analysis or recommendation.⁴ As a result, the former Director and a Special Advisor were the only FHFA employees aware of the former Director’s approval of the Board Transition Plan, upon which the former Director had imposed specific conditions that were not recorded in STAR. Because DOR employees were not aware of the former FHFA Director’s approval conditions, they did not know to track whether any of them had been satisfied. At the time of our 2019 evaluation, the record reflected that two of those conditions had not been met.

We made two recommendations to address these deficiencies, the second of which was to establish a process for maintaining and monitoring sensitive conservator requests in DOR’s STAR system. FHFA agreed with this recommendation.

We Closed Our Recommendation After FHFA Revised its STAR Procedures

DOR updated its STAR system user guide to include procedures for managing sensitive, or confidential, information.⁵ According to FHFA, the revised procedures would allow administrators to assign a STAR record to a confidential Enterprise request and use a generic title within STAR to further maintain the submission’s confidential nature. DOR staff would also save related information submitted by the Enterprises and FHFA’s internal analysis to DOR’s electronic shared drive for record-keeping purposes, with restricted access as appropriate. Based on FHFA’s revised STAR system user guide, we closed the recommendation on September 12, 2019.

⁴ In 2015, FHFA awarded annual target compensation of \$4 million to each Enterprise CEO to “promote CEO retention, allow reliable succession planning, and ensure the continuity, efficiency and stability of enterprise operations.” Congress then suspended those awards and capped each Enterprise CEO’s compensation at \$600,000. In June 2018, Fannie Mae’s Board Chair, on behalf of the Board, submitted the Board Transition Plan to FHFA for approval. In this Plan, the Board recommended a change to Fannie Mae’s management structure by filling the positions of President and CEO with separate individuals; previously, the two positions had been held by a single person. Also, some responsibilities previously executed by the CEO and President would be assigned to the President, and annual compensation would be no less than for Fannie Mae’s most highly compensated Fannie Mae officer, which was then \$3.25 million. The former FHFA Director approved the Board Transition Plan in July 2018. We found that FHFA’s approval of the Board Transition Plan acted to circumvent the Congressionally mandated cap of \$600,000 on CEO compensation. By authorizing Fannie Mae to fill the positions of CEO and President with two separate individuals and transfer substantial responsibilities from the CEO and President to the President position alone, FHFA permitted Fannie Mae to compensate its President at a level more than five times greater than the statutory cap. See *OIG, FHFA’s Approval of Senior Executive Succession Planning at Fannie Mae Acted to Circumvent the Congressionally Mandated Cap on CEO Compensation* (March 26, 2019) (EVL-2019-001), online at https://www.fhfa.gov/Content/Files/EVL-2019-001_0.pdf.

⁵ DOR uses the term “confidential” instead of “sensitive” to refer to such matters. For this report’s purposes, we use DOR’s term “confidential.”

FHFA's Updated STAR Process

During this compliance review, DOR informed us that it had updated the STAR system and part of its process to further address confidential Enterprise submissions. According to DOR, as of September 2020, a “confidential” identifier or label would be applied to each newly received Enterprise confidential submission when a DOR staffer entered that submission into the STAR system. Previously, DOR could only designate an Enterprise submission as being confidential using an identifier applied within its dedicated conservator email inbox, but not within STAR itself.

DOR also told us the STAR system was modified in September 2020 to restrict access to confidential submissions to certain users only.⁶ Because this restriction limits the users who may view confidential information, DOR staff told us that as of September 2020, they no longer save on the electronic shared drive any related information submitted by the Enterprises. Therefore, Enterprise information related to confidential submissions that had previously been saved on the electronic shared drive now resides within the STAR system, with restricted access to that confidential information.

DOR also stated that it revised its process for handling confidential Enterprise submissions again in February 2021, because it had confirmed that the STAR confidential identifier implemented in September 2020 was working properly. As a result, DOR states that it discontinued the following processes:

- DOR no longer uses a generic title for confidential Enterprise conservator submissions in order to limit their visibility within the STAR system. Instead, DOR uses the title provided by the Enterprise for its request.
- DOR also discontinued using a second restrictive identifier in STAR (in addition to the “confidential” identifier) to limit those able to view confidential Enterprise submissions. As of February 2021, DOR relies solely on the system’s “confidential” identifier to appropriately restrict access to Enterprise confidential submissions within STAR.

⁶ As of the time of our fieldwork, we found that there were five users with access to the confidential submissions. Three of the users are DOR personnel who input entries into STAR. The other two users are in FHFA’s Information Technology department.

FINDINGS

We initiated this compliance review in January 2021 to determine whether DOR complied with its STAR user guide in maintaining and monitoring in STAR those confidential conservator requests submitted by Fannie Mae from October 1, 2019, through June 9, 2021 (review period). DOR informed us that Fannie Mae submitted seven confidential submissions to DOR during our review period. DOR received one of these submissions before the September 2020 STAR system update, two were received after September 2020, and four were received in or after February 2021. As noted above, DOR modified its corrective actions during our review period. Therefore, our testing procedures varied depending on the date of each confidential submission to DOR.

1. DOR Applied its Procedures for Fannie Mae’s Confidential Submission Received Prior to September 2020.

DOR received the first confidential submission from Fannie Mae during our review period on March 25, 2020. For the one confidential submission received before September 2020, we assessed whether DOR complied with the following two provisions in its STAR user guide:

1. DOR was required to use a generic title to label confidential submissions in STAR, such that the submission’s exact details are not identifiable by the title to those outside of DOR. We observed that the submission had a generic title that did not identify the subject individual’s name in the STAR system, which met this requirement.
2. DOR was required to save Enterprise attachments that accompanied the submission or other documents and analysis pertinent to the confidential submission within DOR’s electronic shared drive only, not in the STAR system. We found that DOR did not save Enterprise attachments to its electronic shared drive but only within the STAR system. However, because an external organization publicly announced the substance of this confidential submission on March 16, 2020, the submission was no longer confidential and the requirements to protect confidential information were rendered moot once the announcement had been made.

2. DOR Followed its Revised Process for Fannie Mae’s Confidential Submissions Received from September 2020 through January 2021.

DOR received two confidential submissions from Fannie Mae on October 28, 2020, and December 7, 2020. We assessed whether DOR complied with the following three provisions in the revised process for handling confidential submissions:

1. DOR was required to use a generic title to label confidential submissions in STAR, such that the exact details of the submission are not identifiable by the title to those outside of DOR. Our testing found that DOR used generic titles for these two submissions in the STAR system, which did not identify the subject individual’s name, in compliance with the requirement.
2. DOR was required to designate each entry as confidential within STAR. Our testing found that DOR marked the items as confidential within STAR.
3. DOR was required to use restricted access roles to limit users’ view of the confidential matters within STAR. Our testing found restricted user access roles in place.

3. DOR Followed its Revised Process for Fannie Mae’s Confidential Submissions Received In or After February 2021.

DOR received four confidential submissions from Fannie Mae in or after February 2021: three submissions were received on February 6, 2021, and the final submission was received on April 19, 2021. We tested whether DOR designated each of the four entries as confidential within the STAR system, as required by its revised process. We found compliance with this requirement.

CONCLUSION.....

Based upon our testing, we found that FHFA’s corrective actions, which evolved during our review period, complied with our recommendation that it establish a process for maintaining and monitoring sensitive conservator requests in DOR’s STAR system.

OBJECTIVE, SCOPE, AND METHODOLOGY.....

We initiated this compliance review in January 2021 to determine whether DOR maintained and monitored confidential conservator requests submitted by Fannie Mae.

To accomplish our objective, we reviewed all seven of Fannie Mae’s confidential conservator requests submitted from October 1, 2019, through June 9, 2021, as identified by DOR. We reviewed STAR system documentation for all seven confidential submissions in our population. The procedures for testing compliance, however, varied based on the confidential submission date.

- For the one confidential Enterprise submission dated before September 2020, we obtained system documentation to assess if STAR entry titles did not include identifying information and that there were no attachments in STAR associated with the entries. We also viewed via video conference the shared drive location of the documents related to the confidential STAR requests.
- For the two confidential Enterprise submissions dated from September 2020 through January 2021, we reviewed system documentation to assess if the STAR entry titles did not include identifying information and the confidential identifier was applied to those entries within STAR.
- For the four confidential Enterprise submissions dated in or after February 2021, we examined system documentation to evaluate if the confidential identifier was applied to those entries within STAR.
- Finally, we reviewed user access documentation to verify restricted access to confidential records in STAR.

We also interviewed Agency officials and reviewed publicly available information.

We conducted our compliance review from January 2021 through June 2021 under the authority of the Inspector General Act of 1978, as amended, and in accordance with the *Quality Standards for Inspection and Evaluation* (January 2012), which were promulgated by the Council of the Inspectors General on Integrity and Efficiency.

We provided a draft of this report to FHFA for its review and comment.

APPENDIX: FHFA MANAGEMENT RESPONSE.....



Federal Housing Finance Agency

MEMORANDUM

TO: Brian Baker, Deputy Chief Counsel, Office of Inspector General

FROM: Jason Cave, Deputy Director, Division of Resolutions Cave, Jason Digitally signed by Cave, Jason
Date: 2021.07.19 11:25:59 -04'00'

SUBJECT: Draft Report: *Compliance Review of FHFA's Handling of Fannie Mae's Confidential Conservator Requests.*

DATE: July 19, 2021

Thank you for the opportunity to respond to the Office of Inspector General's (OIG) draft report referenced above (Report). The Report presents the results of the OIG's compliance review to determine whether the Federal Housing Finance Agency (FHFA) maintained and monitored confidential conservator requests submitted by Fannie Mae.

I am pleased that the OIG concluded that the Division of Resolutions (DOR) established a process for maintaining and monitoring sensitive conservator requests in DOR's STAR system that addressed the OIG's previous recommendation.

I would like to acknowledge the dedicated OIG staff that worked with FHFA during the compliance review.

If you have any questions relating to our response, please do not hesitate to contact me.

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