The secondary market for mortgage loans as it exists today is almost entirely the product of federal laws and regulation. The National Housing Act, in addition to boosting the construction industry, was also designed to encourage liquidity in the mortgage market. Lack of liquidity was a major reason for the high foreclosure rate during the Depression. When banks refused to refinance homeowners’ short-term loans, widespread foreclosures were inevitable.

The FHA’s new twenty-year mortgages also risked creating a liquidity problem, because they would tie up lenders’ capital for much longer, a risk lenders would be reluctant to take. So, by creating a secondary market for FHA-insured loans, lending institutions would be able to sell the loans to someone else, receive their capital back, and recycle it into new loans. An essential step in reaching this goal was creating what eventually became known as the “government sponsored entities” or GSEs—most prominently Fannie Mae and Freddie Mac.

The National Housing Act promoted liquidity by authorizing the establishment of “national mortgage associations.” These were intended to be private institutions that would buy and sell credit instruments secured by home mortgages. This would be the first time institutions would trade in mortgages as commodities on a national scale. But the concept was a complete flop. Nobody wanted to create one.

After several years of unsuccessful tinkering and making changes to entice investors, President Roosevelt asked the federal Reconstruction Finance Corporation (RFC, another Depression-era agency) to form one. The first and only association established under the Act was the National Mortgage Association of Washington, chartered in 1938 as a subsidiary of the RFC. It was renamed two months later as the Federal National Mortgage Association and nicknamed Fannie Mae. Initially Fannie Mae was an agency of the federal government that exclusively purchased, sold, and held FHA-insured loans, a role later expanded to loans guaranteed by the Veterans Administration (VA). In doing so, it created a secondary market for these loans, enabling lenders to make more loans. This role is now served by the Government National Mortgage Association (nicknamed Ginnie Mae).

In 1954 the Federal National Mortgage Association Charter Act converted Fannie Mae from a government agency into a “public-private, mixed ownership corporation.” In 1968 the Housing and Urban Development Act of 1968 (HUD Act) split Fannie Mae into two entities. One retained the Fannie Mae name and was converted into a for-profit, shareholder-owned corporation under the supervision of the newly created Department of Housing and Urban Development (HUD). HUD retained direct control of the other entity, which became known as Ginnie Mae.

The privatized Fannie Mae was responsible for buying and selling conventional loans. Ginnie Mae was given Fannie Mae’s responsibility for FHA, VA, and other government insured or guaranteed mortgages. Ginnie Mae began as, and remains, a government-owned corporation within HUD.

Two years later, in 1970, Congress adopted additional laws that changed mortgage lending as radically as the statutes of the Great Depression. By 1970 mortgage credit had become painfully tight. Up until this time, bank deposits had been one of the largest sources of mortgage capital. But inflation, shifting demographics, and other factors led depositors to move their money elsewhere. This reduced the capital available and made it increasingly difficult for home buyers to find mortgages.

To address this problem, in 1970 Congress chartered the Federal Home Loan Mortgage Corporation (nicknamed Freddie Mac) by passing the Emergency Home Finance Act. Created as a private company, owned by the Federal Home Loan Bank system and their thrift members, Freddie Mac was designed to provide a secondary market for conventional mortgages originated by thrifts (savings and loan institutions). The Act also authorized Fannie Mae to begin trading in other conventional mortgages. From this point onward Wall Street increasingly became the primary source of mortgage capital.

One of the ways the Emergency Home Finance Act laid the groundwork for the commoditization of home mortgages was by catalyzing the development of the uniform mortgage instruments used in the majority of mortgage transactions today. Before the Act was passed, it was clear that mortgage documents would need to be standardized before they could be traded as commodities. At that time, the text of promissory notes and security instruments used in mortgage transactions varied widely across the country. While VA and FHA lending had produced some standardization for those loans and various trade associations had promulgated their own model forms, conventional mortgage loans lacked the standardization necessary to satisfy investors in a secondary market. Accordingly, after the Emergency Home Finance Act became law, Fannie Mae and Freddie Mac established a task force of attorneys and lenders to develop standard loan documents.
Ostensibly a matter involving private companies, Congress and consumer advocates nevertheless recognized the impact of the standardization process and demanded input. At the urging of Ralph Nader and the Public Interest Research Group, the proposed forms were published in the *Federal Register* and were the subject of public meetings and testimony on Capitol Hill in April 1971. After extensive debate, two final versions (one for each entity) were published in 1972 and merged into one by 1975. The “uniform instruments,” as they are known, have since been updated, but without public input.

The following year Freddie Mac issued the first securities backed by conventional loans. In 1989 Freddie Mac joined Fannie Mae as a publicly traded corporation under HUD’s supervision.

**Footnotes**


63 [63] See § 1.2.2.3 [2], supra.


There are several other less well-known GSEs involved in the mortgage market. They are discussed in § 1.4.12 [1], infra. Technically “government sponsored enterprise” is a generic term. But in the mortgage world, the term is widely assumed to refer to Fannie Mae and Freddie Mac. One definition of GSE (in the generic sense) can be found at 2 U.S.C. § 622(8). For more background on government sponsored enterprises in general, see Kevin Kosar, Congressional Research Service, *Government-Sponsored Enterprises (GSEs): An Institutional Overview* (Apr. 23, 2007).


67 [67] Id. at 27.

68 [68] Id.


70 [70] Id.


84 [84] See § 2.4 [6], *infra* (describing different types of mortgages).
1.2.3.1 Rise of the Government Sponsored Entities

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92 [92] Id. at 397.


96 [96] The websites for Fannie Mae and Freddie Mac’s uniform instruments are listed in Appendix O [7], infra.


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