Lan T. Pham

February 23, 2011

Senator Chuck Grassley
Ranking Member
United States Senate Judiciary Committee
135 Hart Senate Office Building
Washington, DC 20510

Re: Inquiry into Reprisal Action by the Congressional Budget Office

Dear Ranking Member Grassley:

At the suggestion of Mr. Gary Aguirre, I describe below the circumstances of my discharge by the Congressional Budget Office and request your assistance to the extent you believe there is something appropriate you could do on my behalf.

As the Congress grapples with the economic and budgetary challenges facing the nation, the Congress relies on the Congressional Budget Office (CBO) to provide "objective" and "non-partisan" analyses to inform its policy decisions.[1] This mandate gives the CBO a unique status and confers upon the agency an impression of credibility and authority, as its analyses can alter the course of national policies. The CBO cultivates this image internally and externally, and enjoys the protection of the press.

Yet, my brief time as a senior staffer financial economist at the CBO suggests that there is room for doubt about this perception of an objective and non-partisan CBO. Alternative view points are suppressed or questioned as "pessimistic" by CBO Director Doug Elmendorf. Economic facts inconvenient to the CBO's forecasts of economic growth, recovery and other estimates are omitted or suppressed so the desired message may be delivered. For providing truthful and correct analyses of the issues, I was abruptly fired after 2.5 months at the CBO.

Suppression of Alternative Views

In October 2010, I wrote about the conditions and developments in the banking sector and mortgage markets. The events surrounding the collapse of the housing market triggered what many consider to be the worst economic and financial crisis in 80 years since the Great Depression. The effects from this market with $10 trillion in residential mortgage debt outstanding exposed systemic risks and put into question the solvency of financial institutions worldwide. In addition to the global response, the U.S. government and Federal Reserve have responded with trillions of dollars in extraordinary fiscal and monetary stimulus, the bulk of which was aimed at shoring up the banks and financial institutions.

[1] See CBO website at: http://www.cbo.gov/aboutcbo/policies.cfm.

I was repeatedly pressured by the CBO Assistant Director, Deborah Lucas, in charge of the Financial Analysis Division to not write nor discuss issues in the banking sector and mortgage markets that might suggest weakness in these sectors and their consequences on the economy and households. Assistant Director Deborah Lucas explicitly sought assurances from the Assistant Director in charge of the Macroeconomic Analysis Division that the issues I raised would not lower the CBO's forecasts of economic growth. More broadly, what emerges is a pattern of suppression by the CBO to prevent public writings about the damage brought on by the banking and financial sector and housing collapse. While disregarding *factual* and empirical evidence, the CBO leadership insisted:

- Statements *could not* be made attributing the decline in *property tax revenues* to foreclosures and the decline in home prices, which runs counter to common sense and the findings by the U.S. Senate Joint Economic Committee of the U.S. Congress.
- Foreclosures *had no impact on home prices* (negative externalities, spillover effects). This runs counter to common sense, and a prominent national home price index by CoreLogic in the CBO's key database subscription showing clearly the distressed homes component of the index worsens home price declines.
- The decline in home prices *had no impact* on *household wealth*, which runs counter to common sense and the fact that the home is a significant asset or source of 'wealth' for most households. According to the Federal Reserve, about $7 trillion in home equity evaporated in the housing collapse.
- The emerging foreclosure fraud problems in September 2010 were due to media "*sensationalism*", "*the kind of event of the moment where we should be adding skepticism, not just repeating the hype in the press*" and discussing it "*lacks judgment about what is important*".

Let's take a closer look at the implications of the unknown risks and liabilities of the foreclosure fraud problems unfolding through the legal process, which led the nation's largest banks to suspend foreclosures nationwide. Issues at the heart of the foreclosure problems pertain to securitization (pooling of mortgages that collateralize mortgage-backed securities "MBS") and the Mortgage Electronic Registration System (MERS), which purports to have legal standing on electronic records of ownership on about 65 million or half of all mortgages in the country.

MERS, with Fannie Mae and Bank of America as founding members, facilitated Wall Street's ability to expedite the pooling of subprime mortgages into MBSs by bypassing standard ownership transfer procedures as the housing bubble escalated, the collapse of which devastated the economy and households. The CBO leadership suppressed and minimized concerns about these issues, viewing these concerns in October 2010 as media "*sensationalism*" and "*hype.*" Such statements if made public would raise serious questions about the credibility and objectivity of the CBO, and the kinds of analyses that would be provided to Congress and allowed to be made known to the public. This "hype" has entered the nation's courtrooms:

- On January 7, 2011, the Supreme Court of Massachusetts agreed with a lower court decision that invalidated the foreclosures actions of two of the largest banks on mortgages that were in MBSs; the legal right to foreclose was not proven.
- Courts in Florida have also followed suit.

- On February 14, 2011, U.S. Bankruptcy Judge Robert E. Grossman in Central Islip, New York rendered the MERS system invalid. In rendering his decision, Judge Grossman acknowledged that his decision would have "significant impact."
- On February 16, 2011, MERS released a statement, an excerpt which reads: *"The proposed amendment will require Members to not foreclose in MERS' name...During this period we request that Members do not commence foreclosures in MERS' name."*

The implications have profound financial and economic consequences that would be of compelling interest to Congress and the public, but the CBO sought to silence a discussion of such risks, that in reality, have been materializing. These risks put into question the ability of investors or bondholders to make claims on the collateral (the homes) that underlies trillions of dollars in MBSs, the bulk of which are now guaranteed by the government-sponsored enterprises ("GSEs" Fannie Mae and Freddie Mac). This affects $10 trillion in residential mortgage debt outstanding, of which $7 trillion in mortgage-backed *securities* (MBSs) are backed by about 65 million homes, and roughly $3 trillion is in the form of mortgage *loans* on bank balance sheets.

The $7 Trillion MBS Problem –Foreclosure Problems and Buy Backs

Banks, Private Label MBSs. About $1.5 trillion MBSs are bank-issued, private label MBSs that were collateralized by primarily subprime mortgages, $330 billion of which is delinquent. Banks have publicly acknowledged these risks by recently increasing reserves against repurchase of bad mortgages from investors and litigation costs. As of third quarter 2010, the nation's largest four banks – Bank of America, JP Morgan Chase, Citigroup, and Wells Fargo – have reserved about $10 billion for potential mortgage buy back demands,[1] a "miniscule" amount given the $330 billion in delinquent mortgages. The combined net worth of the largest four banks is about $700 billion.

The foreclosure problems may put even greater pressure on banks as some state courts and legislation have made dents into the legal foundation of MERS. The implication is that investors may be holding trillions in MBSs that are unsecured, which places even greater pressure on banks for mortgage buy-backs. Banks may also face greater losses in not having the legal authority under MERS to foreclose and liquidate the collateral. These issues (among others) are concentrated among a handful of the largest banks that hold about three quarters of the nation's banking assets, a concentration that has been deemed a systemic risk to the nation's economic and financial system. The CBO dismissing such issues prevents an analysis of the risks, so that the public may be forced again to shoulder the consequences for which they have not been a given a voice or a choice.

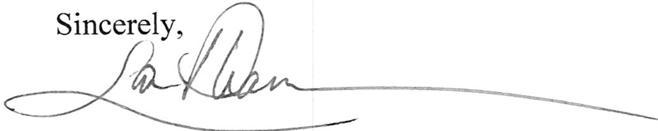
GSEs, Agency MBSs. The other $5.5 trillion MBSs are issued or guaranteed by Fannie Mae and Freddie Mac, whose fate is currently being debated by policy makers. During the first nine months of 2010, Fannie Mae repurchased about $195 billion in delinquent loans from its MBSs;[2] Freddie Mac faced $5.6 billion in buy back demands.[3] The amount of these repurchases in less than one year alone would wipe out Bank of America, the largest bank in the country. The GSEs hold $266 billion in bank-issued private label MBSs, which have experienced the highest rates of default. Recently, Bank of America paid $2.8 billion to the GSEs to settle $7 billion in mortgage buy-back requests, a private transfer of loss to the public that remains unbeknownst to the public.

A discussion of these and other issues were not acceptable to the CBO leadership, but unrealistic assumptions are encouraged and significant facts inconsistent with their predetermined views are overlooked in providing economic analyses and estimates to Congress. For instance, the CBO leadership appeared panic-stricken when I suggested that interest rates were likely to rise in early November 2010 despite the Federal Reserve's quantitative easing programs, and what that may mean for example, to an already weakened housing market. Indeed, interest rates have risen sharply since then from 4.3% to 5.0% on the 30 year fixed-rate mortgage "FRM" (as of 2/17/11). Providing a correct assessment did not seem to matter.

For presenting a truthful and correct assessment of where things stood, I was fired. I know other economists who have been pressured to fall in line with the leadership, but are afraid to voice their concerns for fear that it could endanger their careers. I am prepared to identify them, but only with your assurance that their identities will be remain confidential at this time.

I deeply appreciate your taking the time to consider the information I have placed before you.

Sincerely,



Lan T. Pham, Ph.D.

Attachments

New York Times Article
Time Line
Mortgage Forecast Memo
Banking Forecast Memo
Banking Forecast Memo: Revision of Key Points

[1] Morgenson, Gretchen. (2011). "$2.6 Billion to Cover Bad Loans: It's a Start The New," *New York Times,* January 8. http://www.nytimes.com/2011/01/09/business/09gret.html

[2] Fannie Mae Third Quarter 2010 Results. November 5, 2010 Release, Number 5214a. http://www.fanniemae.com/media/pdf/newsreleases/q32010_release.pdf (page 2).

[3] Timiraos, Nick. (2010). "Freddie Mac Reports $2.5 Billion Loss, Warns of Weak Housing Market," *Wall Street Journal*, November 3, 2010. http://online.wsj.com/article/SB10001424052748703506904575592051567709086.html