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[Judge Says Fannie Mae Whistleblower's Lawsuit Can Go Forward](#)

By Michael Hudson | February 14, 2011, 11:16 am

As Congress begins to tackle the future of Fannie Mae and Freddie Mac, the government-chartered mortgage giants that have been kept alive with \$150 billion in taxpayer aid, a whistleblower lawsuit has been given the green light to proceed.

Caroline Herron, a former Fannie vice president who returned to the mortgage giant in 2009 as a high-level consultant, claims Fannie Mae executives bungled their key role in the Obama administration's Home Affordable Modification Program (HAMP) foreclosure-prevention campaign, engaging in "mismanagement and gross waste of public funds." A Center for Public Integrity [story](#) in August detailed her allegations that HAMP was marred by delays, missteps and executives preoccupied with their institution's short-term financial interests.

Last Friday, the Treasury Department issued a widely-publicized [report](#) calling for a gradual winding down of Fannie Mae and Freddie Mac.

Unnoticed was Herron's important procedural victory on Thursday when U.S. District Judge Rosemary Collyer rejected Fannie's request to dismiss the whistleblower case.

Fannie had argued that the case should be tossed out because the former executive's allegations of missteps in administering HAMP "are not plausible" and because Herron was dismayed that she could not "leverage her short-term, at-will engagement with Fannie Mae into long-term employment" at the Treasury Department.

The victory allows Herron to proceed with her case, using the legal discovery process to dig into the inner workings of the Fannie Mae and its role as administrator of the mortgage-relief program.

"The nature, scope, and reasons behind plaintiff's termination, and her job expectations at either Fannie Mae or the Department of the Treasury, rely upon disputed facts that only can be distilled and processed after all the facts come to light," Judge Collyer wrote in the Feb. 10 ruling. "The question of whether Fannie Mae is a federal or non-federal entity is a question of law, the application of which can only be understood by discovery of its internal functions, processes, membership of the board, who is in control, and other factors that are used in determining whether an organization is a federal one or not."

The discovery process in the lawsuit will also aim to turn up more about how Fannie handled HAMP, a program to help beleaguered homeowners that has been widely labeled as a failure.

Meanwhile, Treasury's long-awaited report calls for a gradual winding down of the Fannie Mae and Freddie Mac, the two government-chartered mortgage giants.

The report takes the pair to task for their failures and shortcomings. But it also notes that they didn't act as recklessly as did Wall Street firms that sponsored trillions in toxic "private-label" mortgage-backed securities during the real-estate frenzy:

Fannie Mae and Freddie Mac's structural design flaws, combined with failures in management, were the primary cause of their collapse. Although some have suggested affordability goals played a major role, the mistakes that led to the failure of Fannie Mae and Freddie Mac – poor underwriting standards, under pricing risk, and insufficient capital with inadequate regulatory or investor oversight – closely mirrored mistakes in the private-label securities (PLS) market where affordability goals were not a factor. In fact, delinquency rates on many PLS securities and other loans held by banks and other private market institutions were far higher than on the loans held by Fannie Mae and Freddie Mac, including loans qualifying for the affordability goals.

Just how much worse did Wall Street do than Fannie and Freddie?

As the Center [reported](#) last month, mortgages bankrolled by Wall Street from 2001 to 2008 were 4½ times more likely to be seriously delinquent than mortgages backed by Fannie and Freddie.

Those kind of hard numbers may prompt some supporters of a continued role for Fannie and Freddie to ask: Why shut down Fannie and Freddie and depend almost solely on a private mortgage market that has an even worse track record than the two government-sponsored enterprises?