

All County Auditors

Through: Carol Mahaffey, Deputy Tax Commissioner for Real Property  
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RE: Fannie Mae, Freddie Mac, and Ohio's Real Property Conveyance Fees  
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### Introduction

Questions continue to arise concerning whether the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac) are federal instrumentalities and, as a result, exempt from the real property conveyance fees under R.C. § 319.54(G)(3)(a), which exempts the transfer of real property "to or from the United States, this state, or any instrumentality, agency, or political subdivision of the United States or this state." This information release updates our research in this area.

### Conclusion

Fannie Mae and Freddie Mac are **not** federal instrumentalities for purposes of the real property conveyance fee exemption in R.C. § 319.54(G)(3)(a).

### Analysis

#### Introduction

'Instrumentality jurisprudence has never been characterized by particular clarity.' . . . But where an entity claims federal instrumentality immunity from state regulation, a court must answer two fundamental questions. First, the court must determine whether that entity qualifies as a federal instrumentality for the purpose at issue. Then, if the answer is 'yes,' the court must determine whether that entity's status as a federal instrumentality immunizes it against the particular local state exaction it seeks to avoid.

James v. Fed. Reserve Bank, 471 F. Supp. 226, 238 (E.D.N.Y. 2007) (citations omitted).

Consequently, a government-sponsored and chartered corporation may be an instrumentality of the U.S. for some purposes and may not be such an instrumentality for other purposes. The following analysis will focus on the first question, whether Fannie Mae and Freddie Mac are instrumentalities of the U.S. for purposes of applying the Ohio conveyance fees on transfers of real property to or from Fannie Mae and Freddie Mac, since the second question is already answered. To wit, if Fannie Mae and Freddie Mac are instrumentalities of the U.S., real property transfers to or from them are exempt from Ohio's conveyance fees by R.C. § 319.54(G)(3)(a).

Note, two Ohio conveyance fees exist: the mandatory charge (R.C. § 319.54(G)(3)), which is called a "real property transfer fee," and the permissive charge (RC § 322.02), which is called a "real property transfer tax." Collectively, they are known as the "conveyance fees."

## Discussion

### *Not Instrumentalities for these Purposes*

The U.S. Code does not call Fannie Mae and Freddie Mac instrumentalities of the federal government. As the case law repeatedly mentions, after the split of the original Fannie Mae in 1968, part of the original Fannie Mae became a private, for-profit corporation and kept the name Fannie Mae, referred to as the Corporation in the U.S. Code, and the other part, Ginnie Mae, referred to as the Association in the U.S. Code, remained in the Government as part of HUD, making it clearly an instrumentality of the U.S. Correspondingly, with the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Freddie Mac was overhauled and restructured, placing the operational control in the hands of the voting common shareholders, resulting in Freddie Mac also becoming a private, for-profit corporation.

Most significantly for this discussion, the U.S. Court of Appeals for the 6th Circuit, whose jurisdiction includes Ohio, held that Fannie Mae is **not** an instrumentality for purposes of applying **due process** under the 5th and 14th amendments of the U. S. Constitution to mortgage foreclosure proceedings. Northrip v. Fed. Nat'l Mortgage Ass'n, 527 F.2d 23 (6<sup>th</sup> Cir. 1975). In this activity, Fannie Mae is not fulfilling a governmental objective: it is not a state actor. Other circuits follow this opinion.

The U.S. Court of Appeals for the 9th Circuit, in a Freddie Mac opinion, cites Northrip with approval. American Bankers Mortgage Corp. v. Fed. Home Loan Mortgage Corp., d/b/a Freddie Mac, 75 F.3d 1401 (9<sup>th</sup> Cir. 1996). The 9<sup>th</sup> Circuit cited the two-part test created by the U.S. Supreme Court in Lebron v. Nat'l R.R. Passenger Corp., 513 U.S. 374 (1995), as the standard to use when determining whether a federally chartered corporation is an instrumentality of the Government for constitutional purposes, which test would apply to Fannie Mae and Freddie Mac.

For a federally chartered corporation to be considered an instrumentality of the U.S. for constitutional purposes it must meet two conditions: (1) the Government created the corporation by special law for the furtherance of governmental objectives and (2) the Government retains for itself the permanent authority to appoint a majority of the directors of that corporation. Lebron, 513 U.S. at 400; American Bankers Mortgage Corp., 75 F.3d at 1406.

Since more than two-thirds (13/18) of the directors of Freddie Mac are elected by the shareholders and less than one-third (5/18) are appointed by the Government, the 9<sup>th</sup> Circuit concluded that Freddie Mac is **not** an instrumentality for 5th Amendment **due process purposes**. The 9<sup>th</sup> Circuit cites Northrip and Roberts v. Cameron-Brown Co., 556 F.2d 356 (5<sup>th</sup> Cir. 1977), when they held that Fannie Mae was not an instrumentality for due process purposes citing several attributes of Fannie Mae, one of which is the appointment of the board of directors. Since only five of the eighteen directors of Fannie Mae are appointed by the President, and the other thirteen are elected by the shareholders, Fannie Mae also fails the second prong of the Lebron two-part test and, as a result, Fannie Mae is **not** an instrumentality of the U.S. for **constitutional purposes**.

Fannie Mae and Freddie Mac are not instrumentalities of the U.S. for other purposes, as well. Fannie Mae is **not** an instrumentality for purposes of **original federal jurisdiction** and for **removal** of a case in State court to a federal court. Knuckles v. Global Mortgage Group, Inc., 481 F. Supp.2d 559 (S.D. W.Va. 2007). Note: this decision does not apply to Freddie Mac because original federal jurisdiction and removal to federal court have been granted by specific statutory authority. 12 U.S.C. § 1452(f).

Fannie Mae and Freddie Mac are **not** instrumentalities for purposes of **sovereign immunity** because they are private, for-profit entities. See Fed. Nat'l Mortgage Ass'n v. U.S., 379 F.3d 1303, 1305 (Fed. Cir. 2004); Williams v. Fed. Nat'l Mortgage Ass'n, Civ. No. 05-1483 (JDB), (D.D.C. 2006).

Fannie Mae and Freddie Mac are **not** instrumentalities for purposes of the **federal tort claims act** because of the control of the board of directors by the shareholders. See Mendrala v. Crown Mortgage Co., 955 F.2d 1132 (7<sup>th</sup> Cir. 1992).

#### *Instrumentalities for these Purposes*

Fannie Mae and Freddie Mac are instrumentalities for purposes of the **federal preemption** under the supremacy clause. See Rust v. Johnson, 597 F.2d 174 (9<sup>th</sup> Cir. 1979); see also 12 U.S.C. § 1723a(c)(2) (real property of Fannie Mae is subject to State and local taxation), 12 U.S.C. § 1452(e) (real property of Freddie Mac is subject to State and local taxation).

Fannie Mae and Freddie Mac are instrumentalities for purposes of being exempt from **punitive damages**. See Alam v. Fannie Mae, Civ. No. H-02-4478 (S.D. Tex. 2007).

Fannie Mae and Freddie Mac are instrumentalities for purposes of **estoppel**. See Mendrala v. Crown Mortgage Co., 955 F.2d 1132 (7<sup>th</sup> Cir. 1992) (the enterprise is free from liability for the unauthorized acts of its sellers/servicers).

#### *Summation*

The 6<sup>th</sup> Circuit Court of Appeals in Northrip, which is controlling in Ohio, ruled that Fannie Mae is not a federal instrumentality for due process purposes relating to foreclosure proceedings. Given that transfers to or from Fannie Mae usually occur in connection with a foreclosure, the Northrip line of cases present the most compelling argument against instrumentality status for Fannie Mae for conveyance fee purposes. Since Fannie Mae and Freddie Mac have similar underpinnings and the 9<sup>th</sup> Circuit Court of Appeals in a Freddie Mac decision cites Northrip with approval, both Fannie Mae and Freddie Mac should be similarly treated.

Even if we ignore the second prong of the Lebron test (governmental control), and apply only the first prong (governmental objective), as the courts did to find that Fannie Mae and Freddie Mac are instrumentalities of the U.S. for the three purposes mentioned above, by foreclosing on, and taking title to, real property, Fannie Mae and Freddie Mac are not fulfilling their mission of providing a secondary market for home mortgages. They are not acting in a governmental capacity or serving any governmental objective, they are simply foreclosing on, and taking title to, real property, as any other private entity would. Accordingly, transfers of real property to or from Fannie Mae and Freddie Mac should be subject to the conveyance fees.

Moreover, the recent so-called take-over of Fannie Mae and Freddie Mac is simply a management tool, called a conservatorship, likened to a corporation being reorganized in bankruptcy. Fannie Mae and Freddie Mac are still referred to as for-profit, private companies. The Federal Housing Finance Agency, which is regulating Fannie Mae and Freddie Mac, has not taken-over the two companies in the Lebron sense, since it has not replaced the board of directors and appointed a majority of them. Consequently, Fannie Mae and Freddie Mac are still for-profit, private companies and should not be considered as instrumentalities of the federal government for purposes of transferring real property. As a result, Fannie Mae and Freddie Mac are not eligible for the real property conveyance fee exemption provided in R.C. § 319.54(G)(3)(a).