STATEMENT OF THE HONORABLE WM. LACY CLAY
Before
The Subcommittee on Capital Markets, Insurance, and Government Sponsored Enterprises
"A Review of the Federal Home Loan Bank System"
September 7, 2006

Good morning Mr. Chairman, Ranking Member Kanjorski, Member of the committee, and Chairman Rosenfeld.

Thank you for holding this hearing, Mr. Chairman.

The Finance Board's rule proposal to require FHL Banks to meet a fixed formula retained earnings requirement should be reconsidered because of its [potential adverse impact on the availability and cost of mortgage credit. As FHLBanks are forced to retain earnings, no matter what their individual business plans or risk profiles look like, over $2 billion will be retained and not distributed through FHLBank member institutions to the borrowing public. In addition, as FHLBank adjust their business operations to take into account that some of their large members may leave because FHLBank membership is no longer financially attractive, the cost of FHLBank advances to remaining members will increase and members will in turn pass on those increased costs to working class families seeking home mortgages. The Finance Board must consider these serious consequences before proceeding any further with its rule proposal.

If FHLBank members leave, another potential adverse effect of the rule proposal is that earnings of FHLBanks may decr5ease, thereby decreasing the amount of funds available for FHLBanks Housing Programs. Each year, FHLBanks contribute 10% of their earnings as seed capital to Affordable Housing Programs sponsored by local community groups and backed financially by FHLBank members. Since 1990, FHLBanks have provided over $2 billion in Affordable Housing Program funds. This public-private partnership is vital to providing decent housing opportunities for working class families, and the Finance Board must not inadvertently restrict the ability of FHLBanks to meet their Affordable Housing Responsibilities.

Another area of concern is the Finance Board's refusal to appoint public interest directors to the boards of directors of the FHLBanks. This self-imposed, two year old moratorium, in clear violation of the Federal Home Loan Bank Act requirement that the Finance Board appoint at least six directors to each FHLBank board, will cause a corporate governance crisis at FHLBanks by the end of this year, when virtually no appointed directors will remain. This is not some forgotten statutory provision--- the House passed GSE reform bill specifically retains this appointive system. The Finance Board should meet its statutory responsibilities and fill all of the appointed director positions at the FHLBanks.

Mr. Chairman I ask unanimous consent to submit my statement to the record.