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Before the
United States Senate
Committee on Banking, Housing, and Urban Affairs

“Proposals for Improving the Regulation of the
Housing Government Sponsored Enterprises”

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Chairman Shelby, Ranking Member Sarbanes and members of the Committee, I am William Longbrake, Chairman of The Financial Services Roundtable's Housing Policy Council. It is my pleasure to appear before the Committee on behalf of the Roundtable and the Housing Policy Council in support of strong, effective GSE regulatory reform legislation.

The Roundtable's member companies formed the Housing Policy Council in 2003 because of the importance of housing and mortgage finance to consumers, the economy and the business of our members. The members of the Roundtable and the Housing Policy Council are directly involved in providing mortgage credit to Americans seeking to achieve the dream of homeownership. We estimate that the nineteen member companies of the Housing Policy Council originate over 62% of the mortgages in the nation. Our members originate, service and insure mortgages for Americans across the nation every day. We lend the money and create the mortgages that are ultimately purchased by the GSEs. We are business partners of Fannie Mae, Freddie Mac, and members of the Federal Home Loan Banks. We recognize the important role they play in the housing finance system. We want them to continue to play the role Congress intended in supporting the housing finance system. The task before us is to ensure their safety and soundness and their proper operation in the secondary market. To do that it is essential that these entities have a world class regulator with the full array of tools to effectively regulate them.

The Financial Services Roundtable and its Housing Policy Council urge the enactment of effective GSE reform legislation this year. We have identified a number of key provisions that are essential to this legislation:

- o **New, Independent Agency** -- Transfer supervisory authority over Fannie Mae, Freddie Mac, and the regional Federal Home Loan Banks to a new, independent agency.
- o **Funding** -- The new agency should be funded by assessments on the GSEs, which are not subject to the Congressional appropriation process.
- o **Supervisory Authority** -- Ensure that the new agency has full supervisory powers comparable to federal banking agencies, including authority to establish and adjust risk-based and minimum capital requirements and to establish other prudential operating standards. In addition, provide receivership authority comparable to the federal banking regulators.
- o **Activities** -- Give the new, independent agency the authority to review and approve activities of Fannie Mae and Freddie Mac in a manner comparable to the authority of the Office of the Comptroller of the Currency (OCC).
- o **Market Disclosure** -- To improve transparency, Fannie Mae, Freddie Mac, and the Federal Home Loan Banks should be required to register with the SEC and be

subject to disclosure standards similar to those applicable to other companies with publicly traded stock. However, provisions should be adopted that recognize the cooperative governance structure of the Federal Home Loan Banks.

- o **Strengthen Affordable Housing Goals** -- Strengthen the affordable housing goals applicable to Fannie Mae and Freddie Mac by making the definitions of low and moderate-income applicable to those goals consistent with the definitions used in other federal housing programs and the Community Reinvestment Act (e.g., make moderate-income equal to 80% of area median income, not 100%, and make low-income equal to 50% of area median income, not 80%). Clarify the duty to serve underserved markets to ensure that this duty cannot be interpreted to authorize direct lending by the GSEs.

Mr. Chairman, S. 190, sponsored by Senators Hagel, Sununu, and Dole effectively addresses most of these key issues and would serve as an excellent basis for the Committee's action. This legislation builds on the excellent start provided by the Committee's action last year. We want to thank the sponsors of the legislation for their leadership. In addition, we greatly appreciate the Chairman's commitment to strengthening GSE regulation. The Administration has also stated that regulatory reform of the GSEs is one of its top priorities and Federal Reserve Chairman Alan Greenspan has consistently outlined the economic importance of improved regulation of the GSEs.

I will briefly expand on the key provisions I outlined above.

Independence: A new independent agency with a Director possessing full regulatory authority is the foundation for effective GSE reform. S. 190 would create the position of Director for the new agency with a six year term. The Director would be assisted by three deputies, one to oversee the safety and soundness of Fannie Mae and Freddie Mac, another to oversee the housing mission of Fannie and Freddie, and a third to oversee the Federal Home Loan Banks. This is a sound model which would assure that the key functions of the GSEs are given proper attention and that the differences in governance structure between Fannie Mae and Freddie Mac and the Federal Home Loan Bank System are recognized. This meets the priority our member companies have identified for an improved regulatory structure for the GSEs.

Funding: S. 190 incorporates what all observers of this issue recognize: an effective financial services regulator requires independent funding that is not subject to the annual Congressional appropriations process. A regulator cannot effectively oversee large, complex financial enterprises if it is uncertain whether it will be able to fund the necessary examiners, accountants, and financial experts needed to oversee organizations with trillion dollar balance sheets and complex derivative-based transactions. This point should no longer be subject to debate.

Supervisory Authority: This is at the heart of the task the Committee faces. To effectively regulate the GSEs, the new regulator must have clear, strong, and broad

regulatory authority. Such authority is possessed by the federal banking regulators and they have used it to effectively regulate the national banking and thrift system and to ensure that problems are discovered and addressed in a timely manner. The regulation of Fannie Mae and Freddie Mac must catch up to their size and complexity. They are much larger in size with more complex business transactions than they were when the Office of Federal Housing Enterprise Oversight (OFHEO) was created in 1992. OFHEO has done a good job with the limited resources and authority it has. However, there have been repeated instances where the GSEs disputed aspects of OFHEO's oversight authority. That does not occur with the Federal banking regulators and this new legislation will provide clear authority to the new regulator. This authority should include cease and desist powers, the authority to set both risk-based and minimum capital and receivership authority. With these provisions and effective regulation, receivership authority should never have to be used, but nonetheless it is an essential power and is one that bank regulators possess. We believe the employees of OFHEO and the Federal Housing Finance Board are dedicated to their mission and serve the public well. They will have the resources and authority to do even better under a new regulatory structure.

Activities: The authority to review current and proposed business activities is a fundamental part of the tools of any effective regulator. The OCC, the Federal Reserve, the Office of Thrift Supervision and the Federal Housing Finance Board review and approve the activities of their regulated entities. OFHEO does not possess that authority and HUD has testified to the Committee that its authority in this area is inadequate. We believe that providing the regulator with authority over programs and activities will assure that Fannie Mae and Freddie Mac meet their statutory housing mission, will benefit the housing market and will help ensure the safe and sound operation of the GSEs.

Market Disclosure: An important part of this regulatory reform initiative is improved transparency for the regulators and the public. The housing GSEs are exempt from the requirements of the 1933 and 1934 federal securities laws. Fannie Mae and Freddie Mac are publicly traded companies and should be subject to the same disclosures as other public companies. The Federal Home Loan Banks are already moving to register their capital stock with the SEC. However, SEC disclosure requirements for Federal Home Loan Banks should recognize the cooperative governance structure of the banks.

Commitment to Affordable Housing: Fannie Mae and Freddie Mac should be given additional guidance and requirements to improve their focus on providing secondary market support for lending to truly low and moderate income borrowers. A first step that can be taken is to make the definitions of low and moderate-income applicable to Fannie Mae and Freddie Mac consistent with the definitions used in other federal housing programs and the Community Reinvestment Act (e.g., make moderate-income equal to 80% of area median income, not 100%, and make low-income equal to 50% of area median income, not 80%). This will provide a clearer understanding of how much of the GSEs business is devoted to purchasing mortgages to borrowers most in need. There are a number of other suggestions that have been circulated on the topic of affordable housing, including requiring the GSEs to purchase CRA-qualified loans. We

believe this is a worthwhile proposal. The key for the Committee in assessing these ideas is to ensure they help support loans to those in need and do not permit the GSEs to expand their role beyond the secondary market.

FARM CREDIT SYSTEM

One final GSE issue that has not received as much attention - but deserves serious study and consideration - is the appropriate regulation of the Farm Credit System. The Farm Credit System is the Nation's first Government Sponsored Enterprise (GSE). The Roundtable believes that the role of all GSEs must be reviewed carefully to ensure they have a strong, independent regulator, are meeting their original mission and not expanding into areas served by the private sector. We recognize that addressing the issues associated with the Farm Credit System may take more time, but we hope Congress will undertake this effort.

CONCLUSION

Mr. Chairman, the work this Committee has already done in airing the issues needed for improved regulation of the Government Sponsored Enterprises together with the legislation sponsored by Senators Hagel, Sununu and Dole provide an excellent framework for strengthening the regulation of Fannie Mae, Freddie Mac and the Federal Home Loan Bank System.

The Financial Services Roundtable and its Housing Policy Council believe that the time is now to achieve these needed reforms. If enacted, the proposed reforms will help preserve the strength of the housing finance market, preserve Fannie Mae and Freddie Mac in the important secondary market role they serve well, and most of all benefit consumers and protect the taxpayers.

We look forward to working with the Chairman, Senator Sarbanes and the members of the Committee to pass effective legislation as soon as possible. Thank you for considering our views.