Statement by Rep. Michele Bachmann
House Financial Services Committee Hearing
Experts' Perspectives on Systemic Risk and Resolution Issues

September 24, 2009

Thank you, Mr. Chairman.

After months of debate about how to address "systemically risky" or "too big to fail" institutions, I remain unconvinced that moral hazard and perverse market incentives can be avoided under the Obama Administration's financial regulatory overhaul. In fact, those things are innate in the Administration's plan.

Defining large institutions as "Tier 1 Financial Holding Companies" whose creditors will not truly suffer the consequences of company losses will lead to a future filled with careless market discipline and unlimited taxpayer bailouts. Granting financial regulators what the Administration has called "resolution authority" to wind down these "Tier 1" companies in the event of massive failure will only spur investors and lenders to keep making riskier bets than they would have without the cushion of a government guarantee. Congress needs to remember that our regulatory restructuring does not occur in a vacuum. Our decisions create actions and reactions; they have consequences.

If this scenario sounds familiar, it's because it is. We saw this very phenomenon occur with Fannie Mae and Freddie Mac, both of which grew larger and larger as they bought up toxic mortgage-backed securities that eventually went belly up and caused the taxpayers to fork over $200 billion to bail them out. How can we turn our heads from the historical proof we have in Fannie and Freddie? Haven't we learned our lesson?

The Administration's proposal is a codification of the ad hoc approach to bailouts we've experienced over the past two years. It perpetuates this cycle, shielding creditors from taking even the riskiest of risks. In fact, the President of the Minneapolis Federal Reserve Bank, Gary Stern, has said of the Administration's proposal that "there is nothing in the Treasury proposal designed to put creditors of large, systemically important financial institutions at risk of loss."

At the end of the day, I do not see how we can reconcile this problem of moral hazard which got us into the financial crisis in the first place. At yesterday's Financial Services Committee hearing, Treasury Secretary Geithner's response to this question was that more stringent capital requirements and regulatory supervision will be imposed on "Tier 1" institutions. But I'm concerned that that won't be enough to mitigate the tremendous moral hazard here. And even if it did, I strongly question whether it is really the right approach to fixing our financial system, both in principle and in practice.

I thank the witnesses for being here and look forward to today's discussion.

Thank you, Mr. Chairman, and I yield back the balance of my time.