OPENING STATEMENT OF CHAIRMAN PAUL E. KANJORSKI

SUBCOMMITTEE ON CAPITAL MARKETS, INSURANCE, AND GOVERNMENT SPONSORED ENTERPRISES

HEARING ON PERSPECTIVES ON SYSTEMIC RISK

MARCH 5, 2009

We meet today to discuss the issue of systemic risk. The bailout of American International Group, the bankruptcy of Lehman Brothers, and the takeover of Bear Stearns each demonstrate that systemic risk is not just confined to the banking sector. We therefore will focus our examinations at this hearing on insurance, securities, and capital markets issues.

The ongoing turmoil in our financial markets has led us to a crossroads. Because our current regulatory regime has failed, we must now design a robust, effective supervisory system for the future. In doing so, we must move expeditiously in order to help restore confidence in our markets and to get our economy moving again.

We must, however, also move carefully and take the time to do it right. We should not rush to judgment on developing a new systemic risk overseer. We must also put aside our partisan differences and aim at the onset to reach a genuine consensus. Perhaps most importantly, we must start at the beginning and ask some basic questions.

First, we must define systemic risk. Does a financial services company pose a systemic risk if it is too big to fail, too interconnected to fail, or too leveraged to fail? Could the independent actions of many small players compound to create a systemic risk? Do only financial services providers pose a risk? For example, could the technology used in our financial markets pose a risk to the broader economy?

Moreover, are there certain financial products, business activities, or industry segments more likely to cause risk than others? How can we distinguish which is which? Today's witnesses will help us to start answering these complex questions and to begin defining more concretely the amorphous concept of systemic risk.

Second, we need to ask ourselves how the government can work to diminish systemic risk. Should we create an umbrella overseer? If so, how should such an entity operate? Alternatively, could existing regulators undertake this objective? If so, how should we address the products and parties that operate in the shadows of our financial system and outside of regulatory oversight?

Third, and arguably most important, how can the government prevent an institution from becoming too important to fail going forward? Should we impose a systemic risk test as part of governmental reviews of mergers? Moreover, could the financial innovations of one company or one sector contribute to systemic risk?

Today we will spend much time studying insurance issues. Our panel has examined insurance regulation many times, but this debate is different. This debate is about recognizing that insurance is a part of an integrated financial services system.

Insurance companies and their affiliates, in some instances, could pose risk to the broader system. American International Group is a perfect, and severe, example of this reality. In other instances, insurers could be negatively impacted by ratings downgrades, capital impairments resulting from external events, and the application of accounting standards.

We will also learn more about credit default swaps, a product that sometimes operates as an insurance contract and sometimes as a securities product. Credit default swaps have generally fallen through the cracks of our fragmented regulatory system. Therefore, Congressman Bachus joined me in asking the Government Accountability Office to study credit default swaps, and an expert will share GAO's findings today.

Hedge funds, too, are largely unregulated. After the government-organized rescue of Long Term Capital Management in 1998, the President's Working Group made legislative recommendations for preventing future systemic risk by hedge funds. I subsequently joined with then-Capital Markets Chairman Richard Baker in proposing the Hedge Fund Disclosure Act and moving it through a Subcommittee markup.

Even though our bill did not become law, I welcome Mr. Baker back to Congress today in his new role as the leader of the Managed Funds Association. This time he and I have another chance to ensure that hedge funds are appropriately regulated and our economy better protected from systemic risk. This time we will hopefully succeed.

In closing, the work ahead of us is important and necessary. I look forward to the testimony of our witnesses and to engaging in a productive debate on these matters.
