

PUBLIC LAW AND POLICY ALERT

EXPLORING SOLUTIONS FOR THE MARKET CRISIS

A Summary of the September 24, 2008, House Financial Services Hearing

MEMBER STATEMENTS – PANEL I

The following House members testified prior to the arrival of Secretary of the Treasury Henry Paulson and Chairman of the Federal Reserve Board Ben Bernanke: Chairman Barney Frank (D-MA), Brad Sherman (D-CA), Jeb Hensarling (R-TX), Melvin Watt (D-NC), Scott Garrett (R-NJ), Dennis Moore (D-KS), Al Green (D-TX), Gresham Barrett (R-SC), Emanuel Cleaver (D-MO), Ron Kind (D-WI), André Carson (D-IN), Lincoln Davis (D-TN), Ed Perlmutter (D-CO), Bill Foster (D-IL) and Joseph Crowley (D-NY).

Member Positions:

- **In general**, members were displeased with the lack of oversight protections in the Department of the Treasury proposal.
- **Representative Sherman** attacked the plan by Secretary of the Treasury, Henry Paulson, for endowing the Treasury with sweeping authority. He recommended a cosigner on all decisions and phased authorization.
- **Representative Hensarling** proposed a temporary suspension of the capital gains tax to inject liquidity into the market. He further suggested suspending mark to market accounting and embraced executive compensation limits.
- **Chairman Frank** noted that the procedures for floor debate on the measure will be bipartisan. He also noted that Congress will be pursuing immediate tax relief for preferred stock holders in Fannie Mae and Freddie Mac.
- Many Democratic members assailed what they perceived to be a lack of executive leadership, calling on President Bush to clearly articulate the consequences of inaction to the American people.
- **Representative Barrett** said that the plan should actively involve private equity and hedge funds in the bidding process for distressed assets.

- **Representative Garrett** made clear his hesitancy to support the proposal outright, stressing the need for viable alternatives to be considered.
- **Representative Crowley** called for active investigations, stating that Wall Street needs “metal bracelets, not golden parachutes.”
- **Representatives Kind, Carson and Foster** specifically called for taxpayer equity provisions.

OPENING STATEMENTS – PANEL II

Chairman Frank declined to give an opening statement.

Ranking Member Spencer Bachus (R-AL) urged the committee not to “kill the messengers.” He further suggested that Congress should stay in session until a solution is reached.

Capital Markets Subcommittee Chairman Paul Kanjorski (D-PA) warned that Congress could only act on the bailout after the president has clearly explained the stakes of the crisis to the American people. He endorsed equity and taxpayer protections, an in-house watchdog, robust Congressional oversight and eventual regulatory reform.

Capital Markets Subcommittee Ranking Member Deborah Pryce (R-OH) cautioned Paulson that the Treasury proposal relied too much on trust, with insufficiently specific explanations of the procedures involved in the bailout. She said the administration is a “far cry” from having people on their side.

WITNESS TESTIMONY – PANEL II

Treasury Secretary Henry Paulson reiterated much of his testimony from yesterday’s Senate Banking Committee hearing. He stressed the potential consequences for Main Street if immediate action is not taken to correct the problems on Wall Street. Moreover, the bailout plan, by Paulson’s description, is an investment program—not a spending program. Paulson ceded some ground on executive compensation, saying that Congress and the administration must find a way to address this in the legislation, but without compromising the program’s overall effectiveness.

Federal Reserve Board Chairman Ben Bernanke, likewise, reiterated many key points from his testimony before the Senate Banking and Joint Economic committees. He gave a brief overview of the market events that created the current crisis, particularly stressing tough components of the AIG bailout designed to prevent “golden parachutes” and a moral hazard situation. As global markets remain under extraordinary stress, Bernanke urged prompt legislative action consistent with the Treasury’s proposal.

KEY ISSUES AND POSITIONS FROM PANEL II Q&A

NOTE: Questioners Included – Chairman Barney Frank (D-MA), Ranking Member Spencer Bachus (R-AL), Paul Kanjorski (D-PA), Deborah Pryce (R-OH), Maxine Waters (D-CA), Peter King (R-NY), Nydia Velasquez (D-NY), Gresham Barrett (R-SC), Carolyn Maloney (D-NY), Steven LaTourette (R-OH), Jeb Hensarling (R-TX), Luis Gutierrez (D-IL), Walter Jones (R-NC), Gary Ackerman (D-NY), Tom Feeney (R-FL), Brad Sherman (D-CA), Ginny Brown-Waite (R-FL), Melvin Watt (D-NC), Edward Royce (R-CA) and Gregory Meeks (D-NY).

Alternatives: Several members offered alternative approaches, including a two-year capital gains tax suspension (Hensarling, Barrett), utilizing bankruptcy courts (Royce) and purchasing preferred stock in distressed banks (Pryce, Maloney). Paulson and Bernanke reiterated the need for a systemic approach.

Executive Compensation: Several members urged the inclusion of provisions that would limit executive compensation. Paulson repeated his earlier concession that the administration is open to a compensation compromise.

Community Banks: Frank expressed concern that community banks holding stock in Fannie Mae and Freddie Mac would be victimized. He further noted his intention to raise the deposit insurance limit next year. Paulson reassured the committee that small banks will be actively involved in the reverse auction process.

Consequences of Inaction: Kanjorski asked what Paulson and Bernanke meant when they said this plan is “better than the alternative.” In one exchange, Representative LaTourette pressed the panel on why they have not said failure to pass the plan would mean “you won’t have a job, you won’t have a car and your kid won’t go to college.” Bernanke responded, “You just said it. We agree with you.”

Credit Rating Agencies: Ackerman asked why credit rating agencies were allowed to rate new and exotic products without any basis for how they would behave in the market. Bernanke responded that this was a contributing factor to the current crisis.

Mark to Market Accounting: Hensarling and Gutierrez proposed changes to the mark to market rule.

Mortgage Relief: Waters urged Paulson and Bernanke to work more with mortgage servicers to ensure more loan modifications.

Oversight: Many members expressed concerns with respect to in-house and Congressional oversight, including procedures for ensuring an efficient transition to the next administration. As he has in past hearings, Paulson welcomed robust oversight and explained that the Treasury’s proposal was intended to be a starting point from which Congress could add supervisory provisions.

Price Tag: Several members expressed concern with approving \$700 billion in one action, preferring instead to pursue a staged authorization. Others expressed concern that purchasing assets at inflated rates would deplete the funds before progress is made. Sherman asked if the Treasury could reinvest profits resulting from the sale of distressed assets. Paulson responded that he did not interpret the proposal to allow such reinvestments.

Private Equity: Barrett encouraged private equity and hedge fund involvement in the bidding process for distressed assets and Royce proposed lifting the 25 percent limit for private equity investment. Bernanke said that regulators are working on providing more flexibility.

Republican Members Signaling Approval: King signaled his likely support of the bailout.

Short Selling: Ackerman proposed reinstating the uptick rule.

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