



Financial Regulatory Reform

Treasury Secretary Tim Geithner's Opening Statement before the U.S. Senate Banking Committee

As Prepared for Delivery

Chairman Dodd, Ranking Member Shelby, members of the Banking Committee. I'm pleased to be here today to testify about the Administration's plan for financial regulatory reform.

Over the past two years, our nation has faced the most severe financial crisis since the Great Depression. Our financial system failed to perform as it should have – by distributing and reducing risk.

Instead, the system magnified risk. Some of the world's largest institutions failed. The resulting damage on Wall Street hit Main Streets across the country, affecting virtually every American.

Millions have lost their jobs, families have lost their homes, small businesses have shut down, students have deferred college, and seniors have shelved retirement plans.

American families are making essential changes in response to this crisis. It is our responsibility to do the same – to make our government work better.

That is why yesterday President Obama unveiled a sweeping set of regulatory reforms to lay the foundation for a safer, more stable financial system; one that can deliver the benefits of market-driven financial innovation even as it guards against the dangers of market-driven excess.

Every financial crisis of the last generation has sparked some effort at reform. But past efforts have begun too late, after the will to act has subsided.

We cannot let that happen this time. We may disagree about the details, and we will have to work through those issues. But ordinary Americans have suffered too much; trust in our financial system has been too shaken; our economy has been brought too close to the brink for us to let this moment pass.

In crafting our plan, the Administration sought input from all sources. We consulted extensively with Members of Congress, regulators, consumer advocates, business leaders, academics and the broader public.

We considered a full range of options and decided that now is the time to pursue the essential reforms, those that address the core causes of the current crisis; and that will help to prevent or contain future crises.

Let me be clear, our plan does not address every problem in our financial system. That is not our intent. It does not propose reforms that, while desirable, would not move us towards achieving those core objectives and creating a more stable system.

By now, the details of our proposals are widely available so I would like to spend a few minutes explaining the priorities that guided us.

If this crisis has taught us anything, it is that risk to our financial system can come from almost any quarter, so we must be able to look in every corner and across the horizon for dangers.

Clearly, our current regulatory structure was not able to do that.

While many of the firms and markets at the center of the crisis were under some form of federal regulation, that supervision didn't prevent the emergence of large concentrations of risk.

A patchwork of supervisory responsibility; loopholes that allowed some institutions to shop for the weakest regulator; and the rise of new financial institutions and instruments that were almost entirely outside the government's supervisory framework left regulators largely blind to emerging dangers.

And regulators were ill-equipped to spot system-wide threats because each was assigned to protect the safety and soundness of the individual institutions under their watch. None was assigned to look out for the system as a whole.

That is why we propose establishing a Financial Services Oversight Council to bring together the heads of all of the major federal financial regulatory agencies. This Council will fill gaps in the regulatory structure where they exist. It will improve coordination of policy and resolution of disputes. And, most importantly, it will have the power to gather information from any firm or market to help identify emerging risks.

The Council does not have the responsibility for supervising the largest, most complex and interconnected institutions. The reason is simple: that is a specialized task, which requires tremendous institutional capacity and organizational accountability.

Nor would the council be an appropriate first responder in a financial emergency. You don't convene a committee to put out a fire.

The Federal Reserve is best positioned to play that role. It already supervises and regulates bank holding companies, including all major U.S. commercial and investment banks. Our plan gives a modest amount of additional authority - and accountability - to the Fed to carry out that mission. But it also takes some authority away.

Specifically, we propose removing from the Federal Reserve and other regulators, oversight responsibility for consumers. Historically, in those agencies, consumer interests were often perceived to be in conflict with the safety and soundness of institutions.

That brings me to our second key priority -- consolidating protection for consumers and ensuring they can understand the risks and rewards associated with products sold directly to them.

Before this crisis many federal and state regulators had authority to protect consumers, but few viewed it as their primary charge. As abusive practices spread, particularly in the market for subprime and nontraditional mortgages, our regulatory framework proved inadequate.

This lack of oversight led millions of Americans to make bad financial decisions that emerged at the heart of our current crisis. Consumer protection is not just about individuals but also about safeguarding the system as a whole.

Congress, the Administration, and regulators have already taken steps to address consumer problems in two key markets, those for credit cards and mortgages. But here too we need comprehensive reform.

Our proposed Consumer Financial Protection Agency will serve as the primary federal agency looking out for the interests of consumers of credit, savings, payment and other financial products.

This agency will be able to write rules that promote transparency, simplicity and fairness, including defining standards for "plain vanilla" products that have straightforward pricing.

Our third priority was making sure that reform, while discouraging abuse, encourages financial innovation.

The United States is the world's most vibrant and flexible economy, in large measure because our financial markets and our institutions create a continuous flow of new products, services and capital. That makes it easier to turn a new idea into the next big company.

Our core challenge is to design a system that has a proper balance between innovation and efficiency on the one hand, and stability and protection on the other.

We did not get that balance right. That requires reform.

We think that the best way to keep the system safe for innovation is to have stronger protections against risk with stronger capital buffers, greater disclosure so investors and consumers can make more informed financial decisions, and a system that is better able to evolve as innovation advances and the structure of the financial system changes.

I know that some suggest we should ban or prohibit specific types of financial instruments as too dangerous. And we are proposing to strengthen consumer protections and enforcement by, among other things, prohibiting practices such as paying brokers for pushing consumers into higher-priced loans or penalties for early repayment of mortgages.

However in general, we do not believe that you can build a system based on banning individual products because the risks will simply emerge in new forms.

Our approach is to let new products develop, but to bring them into a regulatory framework with the necessary safeguards.

America's tradition of innovation has been central to our prosperity. These reforms are designed to strengthen our markets by restoring confidence and accountability.

A fourth priority was addressing the basic vulnerabilities in our capacity to manage future crises.

The United States came into the current crisis without an adequate set of tools to confront the potential failure of large, interconnected financial institutions. That left the government with extremely limited choices when faced with the failure of the largest insurance company in the world and one of the largest US investment banks.

That is why, in addition to addressing the root causes of our current crisis, we must also act preemptively to provide the government better tools to manage future crises.

We propose a new resolution authority, modeled on the existing authority of the FDIC to handle weak or failing banks, that will give the government more options.

That authority will reduce moral hazard by allowing the government to resolve failing institutions in ways that impose the costs on owners, creditors and counterparties, making them more vigilant and prudent.

We must also minimize the moral hazard of institutions considered too big or too interconnected. No one should assume that the government will step in to bail them out if their firm fails.

We do this by making sure financial firms follow the example of families across the country that are already saving more money as a precaution against bad times. We require all firms to keep more capital and liquid assets on hand as a greater cushion against losses. And the bigger, most interconnected firms will be required to keep even bigger cushions.

The critical test of our reforms will be whether we make this system strong enough to withstand the stress of future recessions and the failure of large institutions.

That's our basic objective; we want to make it safe for failure.

We cannot afford inaction. We cannot afford a situation where we leave in place vulnerabilities that will sow the seeds for future crises. And in the weeks and months ahead I look forward to working with this Committee to build a new foundation for a stronger American economy.

Thank you