YET MORE HOUSE FINANCE HEARING GEITHNER LIVEBLOG, PART TWO

First liveblog thread here.

Castle: I want to address what you didn't address. Collins, stability management council. Unanimous agreement we need to do something. Fed has certain authority now, I worry about conflicts there. I would hope that careful thought is given to being inclusive. To have some of the entities being regulated at table. I don't want iron fisted hand making all these decisions.

[Can we put labor at the table, Mr. Castle??]

TG: Three different issues. Division of labor. Checks and balances. As is now case under FDIC. Can't vest authority within one entity. Another set of issues, cooperation across regulator authorities. Much more integration. Not vested in one place. Third, who should be responsible. We have to make sure the people who are responsible are competent to regulate. Not Treasury. In a fire, the fire station needs to understand the neighborhood, don't want to convene committee. Pragmatic case, authority for crisis management matched with systemic risk.

[Again, why did you send someone–Steven Rattner–who knows nothing about the auto industry to resolve it??]

Grayson: How difficult the decisions we make today. Balance sheet earlier this month. AIG had an exposure to the yield curve of $500B, five times greater than it ever had in equity. Why didn't anyone stop from accumulating that risk.

TG: AIG was allowed to build up through complex structures huge amounts of risk. No competent authority. No choice but to come in and unwind.

Grayson: Last 10Q. Fannie Mae accumulated over $250B in derivatives.

TG: Not something I could respond to as carefully. Fannie and Freddie, large set of risks they have to hedge. More powerful supervisor. Not infer from looking at one piece of 10K.

Grayson: It's all exposure, in June over 1.5 trillion. If that contributed to failure, what point should have someone said enough is enough.

TG: You can't measure risk and exposure by looking at that.

Grayson: Substantive rules to prevent this kind of risk.

TG: Capital capital capital. Greater cushion. Best solution these things. Not something market's gonna provide on its own.

Grayson: If AIG subject to margin calls, never have gotten here.

TG: Margin regime, AIG hold more capital in regards to risk. Derivatives, much more conservative.

Grayson: Rules you see being put in place.

TG: If an entity were to rise to a level, it could pose systemic risk. Brought within framework similar to large regulated institutions.

Grayson: Someone will say enough is enough.

TG: constrain risks.

Royce: Wind down power. You'd be able to take over any large firm. Permanent TARP authority. How would you have handled creditors?

TG: Two types of authorities. Intervene. Wind down. Figure out best way to absorb losses. In event default would cause systemic consequences to put in capital guarantee liabilities. Has to be made high threshold. Demonstrate consequences would be systemic.

Royce: All borrowing presumed in market. Moral hazard. GE. They won NBC. Consequences over at treasury. How do you handle these decisions.

TG: [doesn’t answer NBC question] blatherblatherblahter

Royce: My presumption is guarantee large firms borrow at lower price. In text of bill, FDIC appropriate over insurance.

Minnick: Ag committee, systemic regulator, is this consistent?

TG: Take a careful look and get back to you?

Minnick: WRT new mechanism for creating liquidity [public private]. Concerned, need for capital, that this regime not underprice these assets. Under regulatory scheme, if initial auctions produce prices that are at low end of fair market value, additional leverage into system to increase bid prices to point where solution doesn’t exacerbate.

TG: More leverage would help. Relative to alternatives. Better than what we have today. Absence of financing.

[Then why are BoA and Citi buying these up?]

Minnick: All want taxpayer to be treated fairly. TO extent that financial institutions getting less than fair price.

TG: You’ve got tradeoffs right.

Paul: Excess leverage, pyramiding of debt. Look at easy money from Fed and aritifically low interest rates. Everybody knows I’m a proponent of free market. Not free markets got us into this trouble. In other areas we never automatically resort to regulation. Press, it would be prior restraint. Innocent until proven guilty. If there were a reasonable respect for rule of law, taxpayer, burden of proof on govt. Prove that someone broke these regulations.

[in which Geithner tries to show patience with Paul.]

TG: I've never been a regulator. We need to be very skeptical that regulators can fix these problems. Banks vulnerable to runs. Have to impose limits.

Paul: How can we make it like criminal govt proves guilty of crime. Innocent until proven guilty.

TG: I'm not sure I can give adequate answer.

Kanjorski: Oppty to answer Royce's question. Gaps, not an announcement until April 20, when you'll come back. What covered institutions. Insurance. Proposed legislation. Suggestion is that it won't significantly change from what the present status is. State v. federal jurisdiction. If you have oppty answer Royce.

TG: Change regulatory treatment of insurance companies?

Kanjorski: Federal treatment of insurance companies.

TG: Come back soon in more detailed proposals. Good case for optional federal charter. I'd welcome a chance to talk about in as much detail as you'd like.

Frank: If you think any difference to deal with life insurance and property and casulty.

Biggert: "Legacy loans."

TG: 5 asset managers. security side. On loan side, entity that FDIC now uses on resolution process. Auction process for investors to come in and take equity stake.

Biggert: Competition? Ability to successfully manage legacy loan?

TG: Complicated set of questions. Best thing to come before you and walk you through it.

Biggert: So much of our problem, regulators didn't catch it. Failure of communication. Homeland security, katrina. Seems to me, when we asked questions of Greenspan, he didn't answer and he said he didn't know.

TG: Can’t let the regulated be part of their regulation. Can’t put in body which is designed to put regulation in place. You need these regulatory agencies working together. There’s a very strong case to make for coordination.

Frank: If anybody suffers from absence of communication from regulators.

Waters: I want to ask about the products on the market. Why not talk about elimination of various products. We regulate. Why don’t we talk about AltA, why are CDS good products? Not allowing certain products on the market?

TG: People always innovate around what govt prohibits. More effective way to regulate. Make sure institutions are strong enough and protected from predatory behavior. Need to have clearer standards regulated more effectively. If you do it by banning certain things, just be chasing next innovation.

Waters: Scrutiny before they come on the market. Asset management. 5 firms indicated in plan. Women-owned and minority owned businesses. Dumping a lot of money into the economy. Want everyone to participate. Why can’t we look at this a little bit closer. Figure out how we get more women and small firms rather than begging the five.

TG: I’ll look at it more carefully.

Waters: How the dollars have been put out there. FDIC. Banks doing their own underwriting. Small firms to get a crack at?

TG: A lot I don’t understand. Will pass onto Bair.

Waters: Why can’t we eliminate CDS.

TG: I don’t think it’d help. It’d deprive people of a tool to make things safer. Put on exchanges, provide much more transparency. If you just ban them, something else would evolve like that.

Waters; I wish that in the thinking that goes on about these markets. Some deeper thought about not allowing things to come on market. It’s better that you look at that than let something get out there.

Manzullo: Fed, individual applicant.

TG: Important powers.

Manzullo: Very powerful federal agency could have curbed subprime abuse. Teaser and cheater mortgages. Did not act. Reason I bring that up. You want to start yet another powerful agency. Example where federal agency did not act.

TG: You’re right.

Manzullo: Super regulatory system. How many entities can you envision having to be at position where they coudl be seized? 100, 1000, 10,000?

TG: Congress would have to provide standards. Those largest institutions. Grave risks.

Manzullo: Company by company on whether they can be seized.

TG: We have to do better. System does not work.

Manzullo: How many companies, how intimate?

TG: Broad principles.

Manzullo: Do you realize how radical this is?

TG: Prudent, carefully designed.

Manzullo: If it’s prudent and carefully designed, you’d have answers to my questions. Guideline and framework.

Frank: THere will be no law passed that will regulate insurance rates.

Cleaver: No legislation. As specifically as you can can you let me know PPIF process of pricing assets and whether or not bid process can be conducted in way that is auditable. How do we handle settlement.

TG: Best to have FDIC to walk you through that.

Cleaver: Let’s go to lunch.