Testimony of Elizabeth Warren
Congressional Oversight Panel
Senate Banking Committee
Hearing on "Emergency Economic Stabilization Act: One Year Later"
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Chairman Dodd, Ranking Member Shelby, and members of the Committee, thank you for the opportunity to testify today about the Troubled Asset Relief Program (TARP) and the work of the Congressional Oversight Panel.

I should begin by noting that, although I am the Chair of the Panel, the views I express today are my own, as I cannot speak on behalf of all of the other Panel members.

As we examine the year since the passage of the Emergency Economic Stabilization Act (EESA), it makes sense to consider where we were 12 months ago. By last October, major financial institutions that had stood strong for decades were wiped out of existence in a wave of acquisitions and bankruptcies. Others had been bailed out by the government or were teetering on the brink of collapse. The stability of the American financial system was in serious question. The Secretary of the Treasury said that business credit was frozen.

Americans were deeply concerned. Home values were dropping, sending shock waves throughout the economy. Families had seen their savings evaporate, their home equity disappear, and their retirement account values plunge as the Dow continued to fall. The fear was compounded by uncertainty: confusion as to what had just happened, what would happen next, and how policymakers would respond.

TARP was offered as a centerpiece of the government response: a $700 billion program, proposed by then-Secretary of the Treasury Henry Paulson, to stabilize the financial system. For a short while Treasury aimed to use TARP to purchase mortgage-backed securities and loans – which many came to call "toxic assets" – from major financial institutions. Before Treasury completed a single purchase, however, its strategy shifted to buying a wide range of financial instruments through at least 10 different subprograms. Using TARP funds, Treasury has now made significant investments in several hundred financial institutions, bought significant stakes in Chrysler and GM, and provided incentives for home loan modifications, reinvigoration of the market for asset-backed securities, and purchases of loans and real-estate based securities from banks.

From the outset, it was clear that such an enormous program would require enormous oversight. In the year since TARP began, the scope of oversight has only grown. Each of Treasury's new initiatives may serve a role in helping to restore financial stability, but each also raises questions about its design, its effectiveness, the clarity of its goals, and its mix of public costs and benefits.

The Congressional Oversight Panel, along with SIGTARP and GAO, was your creation to provide that oversight. You charged our Panel to "review the current state of the financial markets and the financial regulatory system" and to report to Congress every 30 days.

The Panel works closely with GAO and the Special Inspector General to ensure that our efforts complement rather than duplicate one another. We all want to ensure that the whole of our work is greater than the sum of its parts. The unique contributions of the Congressional Oversight Panel are that we are the only one of the three oversight bodies authorized to hold hearings, we submit monthly reports, and we are responsible for taking a big-picture view of the markets and the financial system. So far we have released 10 monthly oversight reports and two special reports on regulatory reform and on farm credit, as required by law. We have held 11 hearings so far, including six field hearings that have taken us to areas of the country hit hard by the financial crisis. As I testify to you today, other members of the Panel are continuing this work at a twelfth hearing in Philadelphia, where they are exploring the effectiveness of current foreclosure mitigation efforts at helping homeowners stay in their homes.

Of all the questions that TARP raises, one that I am frequently asked as the Chair of the Panel is straightforward: “Has TARP worked?” It may be a simple question, but it has no simple answer. Partly this is because there is no single way to measure the health of our economy. EESA listed five specific objectives for TARP: to restore financial stability, protect home values and family savings, promote jobs and economic growth, maximize returns to taxpayers, and provide public accountability.

If a TARP program advances all five of these objectives at once, then no one would hesitate to call it a success. But what if a program advances only some of these goals, or even advances certain goals at the expense of others? How should we gauge a program that achieves greater financial stability by taking money from taxpayers? Should we consider a program successful if it stabilizes the financial markets but produces no measurable gains in the broader economy?

The experience of the last year has demonstrated that these are not merely hypothetical questions. For example, on February 6, 2009, the day after my last appearance before this Committee, the Panel released a report evaluating Treasury’s largest acquisitions of bank equity and warrants under TARP at that time. Despite the assurances of Secretary Paulson that the initial purchases of stock and warrants of the banks were made at full value, our analysis of the numbers showed that Treasury paid substantially more for these assets than they were worth. In fact, for every $100 spent by Treasury, it received assets then valued, on average, at only $66.

These capital purchases very likely helped to stabilize the financial markets, thereby achieving one of the key goals of TARP. But Treasury paid substantially more for the assets than their market value, subsidizing the banks at the direct expense of the taxpayer. Any discussion of success requires balancing these sometimes contradictory effects.

The Panel can contribute to this discussion by assembling the data and making recommendations. We can press Treasury for greater clarity, transparency, and accountability, but ultimately, the American people will decide if the right balance has been struck.

I would like to briefly expand upon these broad themes by describing each of the Panel’s reports since my last appearance here, as they have explored a wide range of important topics.

In March, the Panel examined the causes of the foreclosure crisis and developed a checklist that provides a roadmap for foreclosure mitigation program success. Among the questions on our checklist: Will the plan result in modifications that create affordable monthly payments? Does the plan deal with negative equity? Does the plan address junior mortgages? And will the plan have widespread participation by lenders and servicers? The Panel plans to release an update to this report in October, using these metrics to examine how well the program has performed.

In April, the Panel looked back on the first six months of Treasury's TARP efforts and offered a comparative analysis of previous efforts to combat banking crises in the past. We found that the successful resolution of past financial crises involved four critical elements: transparency of bank accounting, particularly with respect to the value of bank assets; assertiveness, including taking early aggressive action to improve salvageable banks and shut down insolvent institutions; accountability, including willingness to replace failed management; and clarity in the government response. Without those elements, a financial crisis is likely to create long-term economic problems.

In May, we surveyed the state of lending for small businesses and families and examined the Term Asset-Backed Securities Loan Facility (TALF). The report raised concerns about whether TALF was well-designed to help market participants meet the credit needs of households and small businesses. It also raised serious doubts about whether the program would have a significant impact on access to credit.

In June, we examined how effectively Treasury and the Federal Reserve conducted the stress tests of America's 19 largest banks. The Panel found that, on the whole, the stress tests were based on a solidly designed working model, but that serious concerns remained, including the possibility that economic conditions could deteriorate beyond the worst-case scenario considered in the tests. The Panel recommended that, if the economy continued to worsen, stress testing should be repeated. I should note that the 2009 average unemployment rate now appears likely to exceed the stress test's worst-case scenario, but so far Treasury has declined to call for a repeat of the stress tests. In light of the impact of unemployment on bank losses and the possibility of future large losses from commercial real estate, repeated stress tests may yet be necessary.

In July, the Panel examined the repayment of TARP funds and the repurchase of stock warrants. At that time, 11 banks had repurchased their warrants from Treasury. Once again, our analysis of the numbers indicated that the taxpayer had received only 66 percent of the Panel's best estimate of the value of the warrants. In order to ensure that taxpayers would receive the maximum value as banks exited TARP, the Panel urged Treasury to make its process, reasoning, methodology, and exit strategy absolutely transparent. We are pleased to note that since our July report was published, an additional nine large institutions have repurchased their warrants, generating receipts to Treasury of $2.9 billion, representing more than 94 percent of the Panel's best estimate of their values.

In August, we reported that substantial troubled assets backed by residential mortgages remained on banks' balance sheets and presented a potentially serious obstacle to economic stability. The risk to the health of small- and mid-sized banks was especially high. The Panel recommended that Treasury and the bank supervisors carefully monitor the condition of the troubled assets held

by financial institutions and that Treasury should move forward with one or more initiatives aimed at removing troubled whole loans from bank balance sheets.

This month, the Panel examined the use of TARP funds in support and reorganization of the domestic automotive industry. We recommended that Treasury provide a legal analysis justifying the use of TARP funds in the auto industry. We further recommended that, in order to limit the impact of conflicts of interest and to facilitate an effective exit strategy from ownership, Treasury should consider placing its Chrysler and GM shares in an independent trust.

Since EESA was enacted one year ago, the apprehension that pervaded this country has turned into something else: frustration and anger. Taxpayers have committed over $531 billion through TARP, and although there is no doubt that the financial system has begun to stabilize, families are still feeling the pain of rising unemployment, rampant foreclosures, higher bank fees, and limited access to credit.

Today's fragile stability has come at an enormous cost to the American people. Taxpayers have a right to expect full clarity, full transparency, and full accountability in Treasury's use of their money. They also have a right to know what has fundamentally changed to prevent this crisis from ever happening again. It is time for our focus, which has been fixed upon avoiding short-term disaster, to expand to include this long-term thinking. We should explore ways to change the rules of the financial system to make certain that this economic crisis is not repeated—a topic that the Panel first considered in our special report on regulatory reform.

Thank you again for the opportunity to explain the work of the Congressional Oversight Panel. I look forward to answering your questions.