Congress of the United States
Washington, DC 20515

September 17, 2008

The Honorable Henry Paulson
Department of the Treasury
1500 Pennsylvania Avenue
Washington, DC 20220

The Honorable Ben Bernanke
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

Dear Secretary Paulson and Chairman Bernanke:

We write to express our deep concerns over the increasing propensity, size, and frequency of government interventions to prop up failing private sector companies. These bailouts have set a dangerous and unmistakable precedent for the federal government both to be looked to and indeed relied upon to save private sector companies from the consequences of their poor economic decisions.

We have little doubt that in many cases the motivation of regulators has been a fervent desire to preserve market stability and avoid tumultuous disruptions and systemic risk. To that end, such motives are commendable. Yet the fact remains that these massive federal bailouts have exposed taxpayers to literally tens of billions of dollars of new risk, diluted the incentive for the private sector to make the difficult but necessary decisions to address its fiscal problems, and created a sizable moral hazard where companies are absolved, not punished, for excessive risk taking.

While there are likely many causes that contributed to this economic turmoil we are now facing, it is clear that at least some part of it has been furthered by the moral hazard created by the potential for government intervention. For decades and more acutely in recent years, we witnessed how the formerly implicit, now explicit, government guarantee behind the GSEs Fannie Mae and Freddie Mac allowed them to swell to stratospheric and ultimately unsustainable financial heights. Regrettably, the GSE precedent and the March Bear Stearns bailout might have spurred other companies likewise to conclude that they, too, were "too big to fail" and prevented them from acknowledging the true gravity of their financial situations.

As tempting as it is to resort to federal intervention as a bailout for fiscal problems, the blunt truth is that the federal government cannot afford to be the automatic savior for every company facing financial peril. Look at the facts: in 2008, the federal government through its various agencies has taken on $9 billion of losses from the collapse of IndyMac, $29 billion of risk from the Bear Stearns bailout, $85 billion of risk from the AIG bailout, and at least $200 billion and potentially trillions of dollars of risk from the Fannie Mae/Freddie Mac bailouts. Those figures do not even include the $300 billion of exposure to expand the FHA to refinance problem mortgages or a reported $25 billion loan being considered for big Detroit automakers.

All of these financial commitments come on top of a projected budget deficit of $407 billion in FY08, a national debt of $9.6 trillion, and over $640 billion in proposed tax increases passed by the House of Representatives this Congress. Add to that record energy prices, increased labor costs, the assault on private pools of capital and foreign investment, trade agreements long ignored, and a host of new government mandates on everything from cars to light bulbs. These conditions have lumped together to create a perfect storm of financial uncertainty for nearly every segment of our economy and a resulting scarcity of liquid capital and available credit.

Even if we could financially afford to continue bailing out troubled private sector companies, there is a very real question as to whether we should. These bailouts raise serious public policy questions. We believe that even if some Americans might support intervention, many would be shocked to learn that the federal government could now end up as the majority owner of private sector businesses like depository institutions, investment banks, secondary mortgage lenders, and insurance companies. We are not suggesting that such acquisitions done in an effort to offset taxpayer risk are inherently ill-advised, but federal investment in such large amounts of private company stock has the appearance of a socialist and not a free market approach to managing our economy.

It is evident that no one wants to be the one who says no to a fiscal rescue when there is so much at stake. But the reality is that actions like federal bailouts taken to delay short-term financial pain often end up producing long-term damage to our entire economy. One need only look to Japan and the banking crisis that led to its 'Lost Decade' of recession and stagnant economic growth from which it has still failed to recover. The IMF has called those economic problems "a failure to deal proactively with the impact of the collapse in asset prices" that has led to real GDP growth only averaging 1 percent a year over the past decade.

Instead of actions to insulate our economy, we believe that regulators ought to pursue a path that acknowledges the realities of our current financial problems without delay and implements reforms based on free market principles to restore certainty to our markets. These principles include encouraging more—not less—competition among market participants, rewarding innovation, creating incentives for responsible risk management, and re-establishing the market discipline that comes from the potential of failure. Such principles will be key to developing a more responsive and reliable 21st century financial framework when Congress examines regulatory regimes as we believe it must.

Experience has shown that the best antidote for market turmoil is regulatory certainty and economic growth. Since any legislative response is unlikely in the waning weeks of the 110th Congress, we urge you in the strongest terms possible to refrain from conducting any additional government-financed bailouts for large financial firms. Regardless of the precautions taken, the risk to taxpayers and to the long-term future health of our economy remain just too great to justify.

Sincerely,

J. Hensarling

Michele Bachmann

Virginia Foxx

Tom Feeney

Bill Sali

Marsha Blackburn

Mary Fallin

Trent Franks

Zach Wamp

David Davis

Barbara Cubin

Dan Burton

John J. Duncan Jr.

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Connie Mack

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Jim Jordan

Sam Johnson

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