Witness: Allan Meltzer, Professor of Political Economy and Visiting Scholar at AEI
Hearing: Balancing Monetary Policy with Systemic Risk Regulation
Date: July 9, 2009
Link: http://www.house.gov/apps/list/hearing/financialsvcs_dem/meltzer_testimony.pdf

Summary
Meltzer does not believe that the Fed should have consolidated supervisory authority over systemic risk. He believes that the Fed is not effective at preventing systemic failures and that its decisions regarding systemic failures would be influenced too heavily by Congress, the Administration, or failing firms.

Why Fed Should Not Be a Consolidated Supervisor of Systemic Risk

- Meltzer has not found any instances where Fed has acted preemptively and avoided a crisis.
- There is a conflict between the roles of the Fed and Congress.
- The Fed cannot effectively mitigate of all types of crises.[1]
- The Fed has never announced a lender-of-last resort policy.

An Alternative Proposal

- End "too big to fail" mentality and have larger capital requirements.
- Fed must announce a lender-of-last resort rule and Congress should adopt a rule.
- Realize that regulations are subject to circumvention.
- Incentives must be changed to shift losses onto bankers.
- Apply FDICIA[2] or bankruptcy law to holding companies.
- Close Fannie Mae and Freddie Mac.
- Make compensation systems for financial firms dependent on earnings.

[1] Such as supply shocks or asset market exuberance.
[2] Federal Deposit Insurance Corporation and Improvement Act (1991): intended to lessen losses to the FDIC fund by ensuring that the Fed does not put off the closure of failed banks.