Opening Statement of Ranking Member Spencer Bachus, Hearing Entitled, "Municipal Bond Turmoil: Impact on Cities, Towns, and States"

March 12, 2008

Thank you, Mr. Chairman, for holding today’s hearing on the ongoing turmoil in the bond markets and the problems local cities and counties are facing in trying to issue, refinance, or price their municipal debt.

This is the Committee’s first hearing on the $2.6 trillion municipal securities market. Unfortunately, it comes at a time when that market – which traditionally has been known for its safety, security and rate of return – is under severe stress.

Constituents in my district are being hit particularly hard by this crisis. In my home area of Jefferson County, Alabama, the breakdown of the secondary bond markets has forced the county’s interest rate payments on local sewer bonds to skyrocket from 3.06% to 10% -- a more than triple increase. These higher costs will come out of the pockets of local taxpayers in my district in the form of reduced services or higher fees and taxes. We need to act swiftly and responsibly to ensure that our markets get back on track before too much more damage is done.

Local governments across the country are facing a hostile environment in which to raise funds, with new issues plummeting and many municipalities forced to pay significantly higher interest rates to attract investors. The downgrading of bond insurers and the constriction of the credit markets as a result of the subprime mortgage problems have forced banks and hedge funds to dramatically reduce their municipal debt risk exposure. The resulting collapse of the secondary bond markets has further impaired the ability of local governments to manage their debt exposure.

Until the recent crisis, the secondary bond markets had ample liquidity, but auctions have been failing since the end of last year as the investment markets pulled back. On March 5, Bloomberg reported 536 unsuccessful auctions in the market for floating-rate securities, a failure rate of 68 percent of all auctions. According to the Bank of America, the rate of failures reached 87 percent on February 14 and has since ranged from 61 to 69 percent. These are sobering statistics.

Fortunately, the Committee has solutions available to better protect both local governments and investors. SEC Chairman Cox presented a vision last year for increasing integrity, transparency, and accountability in the municipal securities market. Chairman Cox’s initiative would require meaningful public disclosures that are current and understandable, with a full accounting of all material information at the time of a new municipal bond issuance. Chairman Frank has agreed to invite Chairman Cox to appear before the Committee later this year to formally consider his proposal.

In addition to considering Chairman Cox’s constructive proposal for greater disclosure and transparency, the Committee will also need to further examine the dual credit rating scale used by the rating agencies that appears to arbitrarily assign municipalities a higher risk rating than other debt issuers. This creation of risk perception has forced many municipalities to purchase insurance that may not have been otherwise necessary. More business is created for the rating agencies who analyze the bond insurers’ offerings, but it’s the local taxpayers who end up with the increased costs. Not surprisingly, it has been the non-municipal debt that the rating agencies severely under-assessed for risk, with investors and secondary markets absorbing huge losses as the result of a fundamentally flawed system of risk analysis.

The municipal bond markets finance the development of roads, bridges, sewer and water systems, hospitals, universities, and other critical infrastructure that local residents rely upon. Efficient and liquid municipal finance markets are critical to keeping our economy moving forward and must be restored to working order as promptly as possible.

That is why I appreciate your holding this hearing, Mr. Chairman, and I thank our witnesses for joining us today to improve our understanding of the turmoil in the bond markets.