OPENING STATEMENT OF CHAIRMAN PAUL E. KANJORSKI

SUBCOMMITTEE ON CAPITAL MARKETS, INSURANCE, AND GOVERNMENT SPONSORED ENTERPRISES

HEARING ON RECENT INNOVATIONS IN SECURITIZATION

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We meet this afternoon to examine recent innovations in our securities markets, especially those related to life insurance settlements. While the life settlement industry is now well established and quickly growing, the securitization of life settlements remains in its infancy. Investors, however, have already gained access to other securities products like life settlement funds, mortality indexes, and derivatives linked to life settlements.

Today's hearing offers us an incredible opportunity to employ the lessons that I hope we all have now learned – even though we paid too dear a price to learn them – about issuing toxic securities. By asking some fundamental questions about this industry, we can prevent trouble using foresight rather than later undoing disaster in hindsight.

Specifically, we should ask how one would securitize life settlements, what is needed to properly securitize these products, and whether or not we should securitize them. We should also explore how we can protect those who invest in these products and better safeguard those who sell their life insurance policies. Perhaps most importantly, we must examine whether or not securities products based on life settlements actually contribute to economic growth or merely prolong the casino culture on Wall Street that got us into our current economic mess.

Generally, I see enormous value in securitization. Pooling assets together to create new products can effectively allocate limited economic resources. Securitization has mobilized trillions of dollars of capital from around the world to enable Americans to purchase cars and homes, obtain a college education, and start new businesses. Through securitization, we have also created new sources of liquidity and helped investors to diversify their portfolios.

In short, the securitization of home mortgages and other assets still has the potential to produce enormous societal benefits. That said, we must remember that securitization is only an engine and not an end in itself. Like other engines, for it to run as intended, securitization needs strong, reliable inputs, responsible operators, and clear rules of the road.

In the case of the subprime crisis, we failed on all three fronts. Wall Street's insatiable demand for subprime mortgages fueled a Frankenstein-like engine that allowed originators to hit full throttle and bundle tens of thousands of toxic mortgages without regard to the consequences. At the same time, regulators ineptly monitored these activities, underwriters dangerously relaxed standards, and far too many investors failed to fully understand the purchases they made.

Perhaps most troubling, the gatekeepers to our markets – credit rating agencies – negligently, if not recklessly, stamped nearly everything with a triple "A." Their wildly inappropriate investment grades nearly drove our economy off of a cliff.

Before life settlements have the chance to give securitization another black eye, we ought to consider the need for additional safeguards. Today's hearing will therefore focus on whether or not life settlements are an appropriate input for the securitization engine, and whether or not its operators can appropriately drive this vehicle.

Life settlements can provide retirees with a source of liquidity to fund unexpected expenses or to sell an asset that they no longer need at a better price. But this industry also has the potential for substantial abuse. Presently, states inconsistently regulate life settlements. Many states have also failed to require the registration of life settlement brokers.

Moreover, because of the opaqueness of life expectancy estimates, some investors in life settlement funds have already lost money on inaccurate predictions. The financial gains made by a select few middlemen from the transaction costs related to life settlements are also estimated to be four times that associated with the sale of masterpiece paintings.

In sum, we face many problems with this budding industry. The improper securitization of life settlements could ultimately leave countless seniors penniless and innumerable investors broke. The idea of institutional investors profiting from a person's death also seems, to say the least, unsettling and immoral. It leads us down a slippery slope that might eventually result in indexes based on divorce rates and swaps tied to gambling losses.

We are hopefully now emerging from the worst recession of our time. This committee is also working diligently to strengthen the regulation of our financial system to withstand future crises. It is in this spirit of reform that we should examine the life settlement industry and its connection to our securities markets. By doing so today and before we face another crisis, we may also decide that the best policy is to keep this Pandora's box shut.