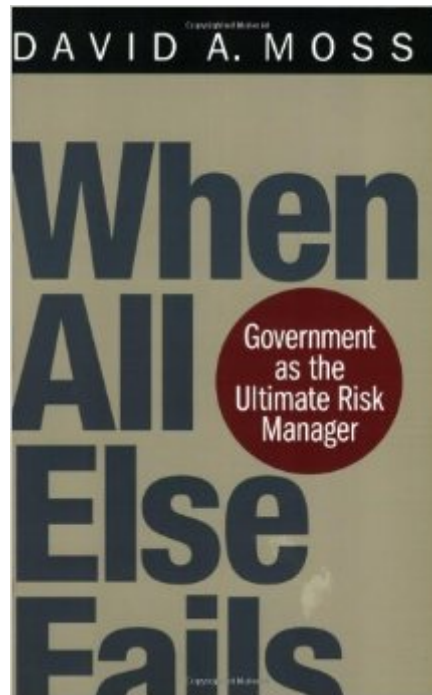


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# When All Else Fails: Government As The Ultimate Risk Manager



## Synopsis

One of the most important functions of government--risk management--is one of the least well understood. Moving beyond the most familiar public functions--spending, taxation, and regulation--*When All Else Fails* spotlights the government's pivotal role as a risk manager. It reveals, as never before, the nature and extent of this governmental function, which touches almost every aspect of economic life. In policies as diverse as limited liability, deposit insurance, Social Security, and federal disaster relief, American lawmakers have managed a wide array of private-sector risks, transforming both the government and countless private actors into insurers of last resort. Drawing on history and economic theory, David Moss investigates these risk-management policies, focusing in particular on the original logic of their enactment. The nation's lawmakers, he finds, have long believed that pervasive imperfections in private markets for risk necessitate a substantial government role. It remains puzzling, though, why such a large number of the resulting policies have proven so popular in a country famous for its anti-statism. Moss suggests that the answer may lie in the nature of the policies themselves, since publicly mandated risk shifting often requires little in the way of invasive bureaucracy. Well suited to a society suspicious of government activism, public risk management has emerged as a critical form of government intervention in the United States.

## Book Information

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## Customer Reviews

I bought this book on the strength of a review in *The Economist* and was not disappointed. With

policies as varied as limited liability, central banking, deposit insurance, and Social Security, American legislators transformed government into an insurer of last resort. Sometimes they shift risk from prospective victims to those better able to afford the loss (product liability); at other times they spread catastrophic risks over the whole tax base (flood insurance). The book charts the expansion of government in the United States from the late 19th century to its zenith in the late 1970s. The author answers the objections of the Chicago and Austrian schools - Becker, Hayek, Mises, and the others - in convincing fashion thanks to its moderate tone and extensive research. The prose is clear, surprising for a book dealing with such complex subject matter. The chapter on the emergence of limited liability corporations is particularly strong. Unfortunately, the chapter on product liability could have used a bit more skepticism. Few readers will share the author's view that tort lawyers are an unalloyed blessing. The author sidesteps many of the problems we now face with exploding damage awards and wide discrepancies in the awards handed down in various jurisdictions. Nor does he grapple with the consequences these problems impose for medical research and the US insurance industry.

This author has a lot to say about the topic, reviewing governmental trials, errors and developments in several settings: corporate limited liability, money, bankruptcy law, workers' insurance, social security, and product liability, among others. Each area is well-researched and crisply explained. The author moves at a good pace: the book is informative without bogging down, and is well-edited. My knowledge in these areas is significantly deepened, particularly in their legal dimensions, and I see debates and rationales of various players, private and governmental, weaving through the narratives, which I had been unaware of. For example, bankruptcy at an early stage (in a few colonies) appears to have been intended as an orderly and fair means for creditors to get at assets, and less in its modern form of a device more oriented to relief of debtors. Many such facets of the topic are set forth here, as they unfolded through time. This book came out around 2002, so sadly, I am left to apply its (clear and well-laid-out) ideas to the massive risk management events that have happened lately. But this book gives me a platform from which to consider such things as the Dodd-frank legislation and PPACA. I am grateful to the author for staying in a disciplined way on the topics, and not overstaying or getting lost in digressions. In my quest to learn a historical background to risk management, I previously read "Freaks of Fortune," which started with sea voyage insurance and walked through slavery and other 19th century institutions which are (arguably) risk management attempts. I like these sorts of books, which take a broad view of what arrangements in society may be considered "risk management," from family arrangements to various customs, to

major legislation, and go in a scholarly and methodical way through the pertinent history.

"Too Big to Fail""A risk to the economy"We see these phrases in the media now more and more. What they imply is the mutualization of all risk i.e. the risks that individual managers take of "too large to fail" institutions will be borne by the government, and therefore all of us.If JPM or C rolled over today - would the US government let it happen? Would the IMF? Would the BIS? Of course not. We are all implicitly short a load of puts on collective market risk. This incentivizes individual managers to make riskier bets (and actually forces them to do so, if they want to remain competitive). This therefore raises the strike of these puts higher and higher i.e. things can go very badly much sooner, and individual institutions are LESS insulated from market volatility than they were 30-40 years ago.Sub-prime moral hazard is playing itself out now (q1 '08). Credit creation through innovation unlocks equity and allows for economic expansion. This is a reasonable policy goal. However, Moss' claim is that this innovation (unlike in Silicon Valley), comes with a built in safety net that encourages excessive risk taking.

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