Financial Services

The financial near-collapse of 2008 had many causes, some of them extremely complex. Causes ranged from misguided government housing policies to the global savings glut to the failure of banks to adequately manage lending decisions. The crisis caused the largest federal government intervention in the private markets in history, complete with the de facto nationalization of some companies. Now, the Obama Administration and many in Congress are attempting to micromanage everything from consumer products to pay levels through increased regulation. This is completely the wrong approach. First, they need to develop and implement a strategy to responsibly end government interference and sell off assets purchased through the emergency programs. Then, Congress should focus on improving existing regulation, and not on creating new agencies and piling more regulations on top of existing ones.

RECOMMENDATIONS

1. Get the government out of the financial industry. The 2008 crisis saw the government effectively nationalize some financial institutions, give billions of taxpayer dollars to others, and create huge new programs to buy or subsidize financial markets. These new programs need to be shut down in a way that returns control of financial services to the private sector without undermining confidence in financial institutions. A first step would be to continue to allow well-capitalized banks to repay taxpayer money that went to them, and to prohibit future bailouts. Then, the several programs to prop up lending and asset sales need to be closed down. This will take time, but it is an essential precondition to the recovery of the industry.

2. Oppose the creation of a Consumer Financial Protection Agency (CFPA). Treasury Secretary Tim Geithner has proposed an unnecessary regulatory agency, the CFPA, to oversee the consumer financial product market. However, creating the CFPA would be a huge mistake that would involve ambiguous grants of almost unlimited power, poorly considered policies, and attempts to micromanage financial

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products. It would end up hurting consumers far more than it helped them. A CFPA would raise costs to consumers, reduce the number and kind of products available to them, increase the micromanagement of financial services firms, and greatly increase the confusion caused by differing and conflicting consumer laws in the different states.

3. Modernize the federal financial industry regulatory structure. The current federal financial regulatory structure reflects the financial services industry of 70 years ago, not that of today. There are too many different agencies with overlapping missions. Many of these agencies should be combined, and some of them, such as the Office of Thrift Supervision (OTS), can be eliminated. Next, agencies should be asked to use their existing powers to ensure that financial institutions understand and control the risk of their products and investments to reduce the chance that they will need a taxpayer bailout. Finally, bankruptcy laws must be modified in order to ensure that any future financial institution failures are handled in the courts, instead of necessitating a government bailout. This step will also help to reduce risky behavior within the financial industry.

FACTS AND FIGURES

- According to *The New York Times*, the largest recipients of TARP funds are: A.I.G. ($70 billion), Bank of America ($45 billion), and Citigroup ($45 billion). Treasury officials acknowledged that it would take years for the government to get its money back from A.I.G. or many of the more troubled banks they have helped.

- Besides the $700 billion TARP bailout program, the government has created an array of other programs to address to the struggling financial system. Through April 30, the government had made commitments of about $12.2 trillion and spent $2.5 trillion—but also had collected more than $10 billion in dividends and fees.

- Under the Administration's proposed CFPA model, national firms could face up to 51 separate consumer regulatory regimes. Financial services providers would be forced to create multiple variations of their product that meet various state requirements. This cost would be passed on to the consumer in the form of higher fees.

ADDITIONAL RESOURCES

David C. John, "The Obama Financial Regulatory Reform Plan: Poor Policy and Missed Opportunities," Heritage Foundation *WebMemo* No. 2545, July 15, 2009, at *http://www.heritage.org/Research/Regulation/wm2545.cfm*

David C. John, "Republicans' Financial Regulatory Reform Plan a Good Start," Heritage Foundation *WebMemo* No. 2484, June 15, 2009, at *http://www.heritage.org/Research/Regulation/wm2484.cfm*

David C. John, "How to Protect Consumers in the Marketplace: An Alternate Approach," Heritage Foundation *Backgrounder* No. 2314, September 8, 2009, at *http://www.heritage.org/Research/Regulation/bg2314.cfm*

Stuart M. Butler, Alison Acosta Fraser, and James L. Gattuso, "What Should Be Done About the Financial Markets?" Heritage Foundation *WebMemo* No. 2070, September 19, 2008, at *http://www.heritage.org/Research/Economy/wm2070.cfm*

"Adding Up the Government's Total Bailout Tab," at *http://www.nytimes.com/interactive/2009/02/04/business/20090205-bailout-totals-graphic.html*

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