UNDER PRESSURE FOR GLASS-STEAGALL

The U.S. Senate Produces A Sham: 'Too Big To Fail'

by Paul Gallagher

April 29—Pressure on the U.S. Senate for introduction of a bill to restore the Glass-Steagall Act is increasing. Some 17 state legislatures have been stirred up by demands, led by LaRouchePAC, that Congress re-enact Glass-Steagall as the urgent first step to turning around a collapsing economy, and three states have passed such demands. This comes on top of broad demands for Glass-Steagall from constituency groups, economists, and some leading bankers and regulators.

Senators who distinctly advocated restoring Glass-Steagall during their 2012 election campaigns, have hung back. They evidently fear the Obama White House's determination not to allow challenges to the failed Dodd-Frank Act, and the money-power of the big banks; a recent television documentary showed that Wall Street spent a huge $350 million on one election cycle—1997-98—to get Glass-Steagall repealed.

Now some Senators have floated "ersatz" bills, surrounded by much media sound and fury, about "breaking up the too-big-to-fail banks"—but not Glass-Steagall, and not in fact breaking up anything. These are Bernie Sanders' (I-Vt.) S.685, and the "too-big-to-fail" (TBTF) bill, S.798, of Sherrod Brown (D-Ohio) and David Vitter (R-La.), introduced April 24.

This evasion of what's necessary could not come at a worse time. Hit by Obama's killer austerity policy, the U.S. economy is, by all indicators, clearing contracting, except those figures showing new, rapidly inflating bubbles in real estate/mortgage securities, derivatives, and junk bonds. U.S. bank lending fell by another 1.5% in the first quarter, "despite" $85 billion/month in Federal Reserve money printing; commercial banking activities contracted while "trading" and investment banking activities produced the banks' revenues and profits reported in the quarter. The banking system is deranged.

Credit vs. Money

The idea of a national system of credit—credit tied to investments which improve the physical economy's productivity, and bills of credit tied to trade in productive goods—was first fully formulated by Alexander Hamilton, the United States' first Treasury Secretary.

Along with this concept, has gone the uniquely American idea of commercial banks as almost exclusively intermediaries of credit: institutions that convey liquid credit from depositors and lenders (including government lenders) to productive businesses and households; not institutions which trade and speculate in, and bet on, debt. This guideline too comes from the circle of Hamilton, and includes Robert Morris, President Franklin Roosevelt's ancestor Isaac Roosevelt, and others who formed the first commercial banks in the process of forming the Union.

This is radically different from the centuries-long, "financial oligarchy" assumptions of European banking, for the last two centuries called "universal banking." Following the complete collapse of bank lending (other than buying bonds of governments and monarchies) after the 2007-08 financial blowout, brutal austerity policies have been implemented to try to wipe out debt, and have failed disastrously.

Lyndon LaRouche stressed the uniqueness of this idea of a credit system as "the American System," in a full week of discussions with leaders from all over Eurasia, who spoke at the Schiller Institute's April 13-14 Frankfurt conference. And he stressed it again on April 22 in a teleconference discussion with the LaRouchePAC National Policy Committee:

"Now, the key thing that I've emphasized to people here [in Europe], is on just that point: that we have to understand what the Glass-Steagall principle means. It means that when people think that ordinary accounting processes, as Europeans use them, have some relevance, they're nuts! Because it's obvious that it's only by the characteristic of Glass-Steagall that it eliminates the problem, by changing the rules, back to Glass-Steagall, the original U.S. intention. And in Europe, they don't have it. . . .

"The point is, *without Glass-Steagall, we cannot possibly save civilization now*, not by any deliberate action."

'Be Practical'

Thus the uselessness of the two bills claiming to "break up the big banks," and "accomplish the same goal as Glass-Steagall," that are now floating in the Senate: *Neither bill breaks up any banks or bank holding companies, or prevents commercial banks from putting deposit funds into securities and derivatives.* Liberal media are giving wall-to-wall coverage to both, along the lines of "It's what's practical," "might pass," etc.

Senator Sanders' S.685 calls for the biggest banks to be broken up by decision of Obama's Treasury Secretary (that would be Citigroup veteran Jacob Lew), without suggesting how this would be done—in fact, only the bill's title has been filed, with no legislative text; the description of requiring decisions by Lew, comes from a Sanders press release. This is apparently more of a protest resolution than a bill.

For the Brown-Vitter "too-big-to-fail" bill, S.798, a detailed draft legislative text was leaked April 11, and circulated by some Senators, which makes clear that it does not break up any financial institutions. The full text does not yet appear on the Library of Congress website thomas.gov.

Brown-Vitter will be a bank capital requirements bill, to which will be added a number of elements of the Glass-Steagall Act, for verisimilitude, but *without the two central elements: separating commercial banking from securities broker-dealing, etc.; and preventing commercial banks from dealing in securities, derivatives, and insurance.*

Judging from the circulating draft, Brown-Vitter would:

a) require five years for its basic provisions to take full effect (!), compared to one year for the Kaptur-Jones HR 129 bill in the House which does restore Glass-Steagall (see http://larouchepac.com/glass-steagall);

b) require all banks to have a 10% capital ratio of tangible equity/tangible assets including "fair value" of all derivatives and off-balance-sheet entities;

c) require banks with more than $400 billion in assets (changed to $500 billion in the bill introduced April 24) to have a capital ratio on a sliding scale, greater than 10%, but less than 15% tangible equity/tangible assets;

d) withdraw U.S. banks from the Basel III agreement on capital standards; *but,* paradoxically,

e) allow U.S. regulators to design their own "risk-weighted capital standard"—exactly what is most objectionable about Basel III, because it favors the biggest bank holding companies, which use computer risk-models and derivatives trades to make their assets go away for capital purposes;

f) prohibit bank holding companies from making transfers of securities between investment affiliates and the commercial bank (a Glass-Steagall-like provision);

g) prohibit bank holding companies or commercial bank units from making loans, purchases of securities, repo agreements, or derivatives contracts with non-bank affiliates (a strongly Glass-Steagall-like element).

h) prohibit government assistance/insurance to non-banks (another strongly Glass-Steagall-like element);

i) will specifically permit commercial banks and their holding companies to operate insurance affiliates.

Admitting the Obvious

In interviews April 24 with Bloomberg News and the *Cleveland Plain Dealer*, both Vitter and Brown "acknowledged the bill will not break up any of the large banks." It does nothing, in fact, to change the incredible complexity of the largest bank holding companies, which now average 3,900 subsidiaries *each*, almost all of them dealing in securities, according to studies cited on the Senate floor by Brown.

Brown, in fact, said, at an American Banker forum April 23, that "maybe later" he would join with Sen. Jeff Merkeley (D-Ore.) to introduce a bill to "really" shrink the biggest banks—with Glass-Steagall remaining a bridge too far even then. The tragedy of this is that Brown supports Glass-Steagall and knows it should be restored.

There were no other initiating sponsors announced for this TBTF Act; Vitter's office staff, contacted April 24, did not know of any, nor of a companion bill in the House.

The summary released by Brown April 24 indicated a few changes from the text which leaked on April 11. It remains predominantly a bill to raise bank capital requirements: on the six banks with more than $500 billion in assets, to 15% tangible equity; on other banks with over $50 billion in assets, to 8-9%; and on community banks, to a level to be determined by regulators. Vitter, in a seven-minute Bloomberg interview April 24, spoke of nothing *but* capital requirements relative to bank assets. Whether those assets must still include derivatives and off-balance-sheet structures, as in the April 11 draft, is not yet clear.

Brown's provision to prohibit FDIC insurance or Federal Reserve discount-window borrowing to non-commercial bank units, remains in the bill, along with restrictions on transfer of assets from uninsured to insured commercial units. These provisions alone hearken to the still-certain trumpet of Glass-Steagall.

While Wall Street toadies will put up a show of opposing the TBTF sham, there is no question but that it's a part of their game, to divert from the necessary immediate action which will cut off government support for their ill-gotten gambling game. It's the constitutional *function* of the banking system that must be restored, and FDR's Glass-Steagall is the only way that can be done.