An Insider's View of the Historic Fight for a Glass-Steagall Standard

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Jeffrey Steinberg interviewed her on Jan. 8. This is an abridged transcript.

EIR: You've written a widely circulated critique of the Volcker Rule,[1] which is unique, in that you've clearly read the entire 800-plus pages of the rule and the many exemptions. You've spent years on Wall Street, worked at some of the big financial houses, and have a unique insider's insight into the goings-on within the major financial institutions. Could you highlight for us your own experiences?

Prins: Well, I start out on Wall Street in the late '80s at Chase, and then spent over a decade with a variety of banks, ending up at Goldman Sachs in the early part of the last decade; I left in 2002.

During that time, the evolution of banking, and particularly investment banking, was moving in an accelerated fashion towards more esoteric types of securities, combined securities, synthetic securities—ways in which to combine the positions that banks had, or took on their own books, and rejigger them in such a way as to distribute them to end-buyers. This has been investment banking for decades before that, but particularly in the time before I left, it was accelerating.

For example, I would be sitting in trading and sales meetings during which a trader would come in and say, "Hey, I've got this position in this kind of junky bond or junky security"—they might not use the term "junky," but "a double B," or "something of inferior value"—"I need to move it. Can you figure out a way, a story, a means to get it out the door?" With a larger, more complex security, the idea was to create a more generous spread or profit for the bank, and move that risk to the buyer. That's obviously manifested in the large blowup in 2008, and also in 2001-02, with Enron and Worldcom, and will continue to manifest itself through different types of crises going forward.

EIR: Does the Volcker Rule, in any meaningful way, address any of these problems?

Prins: It doesn't. And the reason is that, the position of a trading desk, in the minor example I gave, isn't necessarily just proprietary trade for an investment bank, which is the only thing that the Volcker Rule sort of gets at. The idea of trading, of market making, of all the terms that are used by banks to identify their activities as speculators, by saying they're "customer-driven" or "client-driven," are not stopped or delimited in any way by the Volcker Rule.

What the Volcker Rule does, is specifically look at *one* aspect of one kind of speculative trading that an investment bank or a commercial bank might be engaged in: the proprietary desk. But the nature of creating securities, complex derivatives, of distributing these through their "market-making" capabilities, through their insurance arms, through their advisory arms, through all sorts of different entities within the banking arena, within the one umbrella of a bank holding company—these are *explicitly exempted* from being touched by the Volcker Rule in its current format.

1. "Volcker Rule Made Meaningless by Abundant Exemptions," Truthdig, Dec. 18, 2013.


White House Photo/Pete Souza

Paul Volcker meets with the President, Jan. 21, 2010. The "Volcker Rule" specifically exempts most of the speculative trading that led to the 2007-08 crisis, and will do nothing to prevent another one.

Not a 'Rule,' But a Set of Exemptions

EIR: I gather from your recent article, that there are about 51 pages of the Volcker Rule that define the limits, and then hundreds and hundreds and hundreds of pages, itemizing all of the exemptions, and pretty much giving a roadmap for how to drive a Mack truck through the holes in the rule.

Prins: Yes. A sheer visual interpretation of the 892-page Volcker Rule would show you a very small percentage of "rule" and a very, very large percentage of exemptions to the rule. It's been massaged and lobbied for in all sorts of different ways, to ensure that *there's no way to misinterpret the ineffectiveness of the Volcker Rule, vis-à-vis the large banking institutions.*

So basically, after 55 pages of talking about what the rule *is* going to do with respect to proprietary trading and limiting those activities, it then goes into *all* of the ways that banks don't have to curtail their trading-related activities, such as trading securities, trading government securities, such as their insurance-related activities, such as their asset-management-related activities, such as all of the things that are under that one umbrella in the bank holding company, into which trading and speculative activities go, and will continue to fester.

EIR: The largest U.S. banks are actually much larger today, by about 40%, than they were at the time of the 2007-08 crisis. What do you see as the level of risk or danger in the U.S. and European banking systems now? Do you see a threat of another major banking crisis looming in the near term?

Prins: First of all, yes. The big six banks are somewhere between 37% and 40% greater in terms of their assets than they had been before the 2008 crisis, largely by design, and partially because of smaller banks going belly-up and their businesses going over to the big six banks. And by design, things like Bear Sterns being taken over by JPMorgan Chase, with government backing; Bank of America taking over Merrill Lynch, with government support, and so forth—all those things have definitely made these banks bigger.

In terms of risk, the top six banks are responsible for 93-94% of the trading activities in the country: That is a substantial risk. They're also very interdependent. They're no less interdependent than they had been before the 2008 crisis. By that I mean, they're often involved in co-managing a particular derivative, and different components of that complex security, or other activities that combine to create a particular transaction. Sometimes they do transactions individually, but because they incorporate so much of the trading activity in the market, and because they are so connected to each other in terms of jointly operating in a lot of that trading activity, or being exposed to the same sorts of risks through the different institutions, in that type of trading activity, the risk in the system continues to exist.

In terms of derivatives themselves, these big six banks are responsible for 96-97% of all of the derivative-related risk of all the U.S. banks. These big six banks not only own the largest set of deposits and assets historically, but they are also historically large in terms of the risk that that size represents, by virtue of the trading activities and derivatives activities in which they engage.

Therefore, it is highly probable that another crisis—maybe not related to mortgages, maybe not related to particular sectors of the corporate world, like it was back in beginning of the 2000s—but most certainly the risk is there, and most certainly there will be another crisis, because the structure of the banking industry has not been altered, to mitigate the possibility of a crisis. The banks have not gotten smaller; the banks have not reduced their risk in any meaningful way; the banks have not been prohibited from creating complex securities, or acting in ways that are difficult to decipher, that create risks that can't even be calculated or represented properly. And so, there is no reason to assume there won't be another major crisis looming.

Glass-Steagall

EIR: You're a longstanding advocate of a return to Glass-Steagall. As you know, there are now two Glass-Steagall bills in the Senate and two in the House. I'm sure you support these efforts. How do you see the prospects of passage of Glass-Steagall, in the current session?

I should note that the vice chairman of the FDIC, Thomas Hoenig, who's also a very strong advocate of Glass-Steagall, has testified before Congress, the House Financial Services Committee on July 26 last year, that he believes that Glass-Steagall must be reinstated before the next big banking crisis, because in the panic that will ensue, the impulse to bail out the too-big-to-fail banks will be almost impossible to overcome.

So how do you see the efforts to pass Glass-Steagall in a timely fashion?

Prins: First, I absolutely agree with Mr. Hoenig. When I left the banking industry and wrote my first book, *Other People's Money*, which came out in 2004, I ended the book by saying that if we do not bring back Glass-Steagall, if we do not restructure the banking system in such a way as to separate deposits and commercial banking from other types of investment banking or speculative activities, we *will* have another crisis. The crisis at the time was over the corporate and banking interests regarding Enron and Worldcom in those sectors. The next crisis was regarding the mortgage sector. But I was very explicit in saying that there *will be*—and there was—another crisis, because banks were not separated.

I believe that, going forward, the conclusion remains the same. Hoenig's conclusion remains the same: The bills that have been proposed by Senators Warren and McCain, and Cantwell and King, in the form of the 21st-Century Glass-Steagall Act, and also by Tierney for the House version of that Act, are absolutely imperative.

The good thing about the language of the Warren-McCain bill is that it doesn't just look at proprietary trading, like the Volcker Rule does; it examines *all* of the ways in which the Glass-Steagall Act has been weakened over the decades since it was passed in 1933. It talks about ensuring that these banking conglomerates shouldn't be able to have deposits, and have government deposit insurance, plus be involved in insurance, plus be involved in other types of investment banking activities as well. The Warren-McCain bill looks at the whole gamut of problems of having this financial services industry in control of *so many* different types of businesses, and therefore, forms of inherent risk in the system.

So they're very good bills. And it would be very important for the financial security of the citizens of this country and the nation itself, to ensure that they are passed.

However, the likelihood of them being passed, unfortunately, at this point, seems very slim. If we could not get the Dodd-Frank Act—and the inclusion of this Volcker Rule, which took five years to basically be represented as something that's effectively meaningless—to be passed in such a way as to restructure the banking system back to a Glass-Steagall format, in wake of the crisis of 2008, in the more lackadaisical atmosphere today, where many people, including in Washington, believe that the crisis has passed, and everything is merry and stable right now, it is more unlikely that these acts will get passed.

I hope they do, I think they should. I think it's a battle that I think we all need to be involved in, because all of our financial securities are at stake.

The Roosevelt Years

EIR: I'll just mention, that through our own activities, there are resolutions either before or already passed in 25 state legislatures, that call for reinstatement of Glass-Steagall. And Senator Warren has put herself in the position of becoming the point-person on Capitol Hill, with a significant amount of media attention.

One of the obstacles that obviously makes for a profound difference between 1933 and 2014, is that President Roosevelt was clearly on board with the original Glass-Steagall. It was an integral part of the agenda of his First Hundred Days. But President Obama, not surprisingly, with Timoty Geithner and Larry Summers and similar people as key advisors during his Presidency, is openly opposed to the reinstatement of Glass-Steagall.

Prins: Yes, back in 1933, and even in 1932, under President Hoover, when the Glass-Steagall Act was originally brought into Congressional debate, and when

President Roosevelt after the signing of the Glass-Steagall Act, June 16, 1933. With him are Sen. Carter Glass (far left) and Rep. Henry Steagall (right), and members of the Admministration.

the Pecora Commission was begun as a different form of investigation of what the banks had done egregiously wrong during the 1929 Crash and going into that period, FDR had not only the intent, and saw through on it, to pass the Glass-Steagall Act. Both Houses of Congress, because of that and because of his political abilities, overwhelmingly voted in a bipartisan fashion to pass Glass-Steagall. And in addition to that, something we do not have today, is that *two of the three main banks at the time,* were very much in the camp of passing a Glass-Steagall Act which would separate the two components of their business, to such an extent that they *publicly advocated* the passage, and they even preempted the passage by announcing that *they* would separate their own institutions; *they* would reduce the size of their own reach, in order to ensure the effective implementation of the Glass-Steagall Act.

So FDR was able to politically organize members of Congress, invoke the public will, *and* get bankers to promote his agenda, in order to pass Glass-Steagall. There was an overwhelmingly positive approach to reforming banking, and it served to not just reform banking, but to stabilize the fears that were still running through the country in the beginning and middle of the Great Depression.

What we have today is a President whose closest advisors, on the one hand, are members of the team that obliterated the Glass-Steagall Act, under Clinton, in 1999. And also the White House and the Federal Reserve, because they are so involved in the bailouts and want to act as if these were the successful ameliorant for creating stability, rather than reforming the banks in a meaningful way, are very positive about something as weak as the Volcker Rule, so they can act as if something has been done, that is reformative. When the Dodd-Frank Act was passed, Geithner and Obama both said this was the most sweeping form of legislation since FDR—and it most certainly is not.

So, the will politically at the very top echelons of Washington is aligned against Glass-Steagall being reinstated. The will of Senator Warren, of all of the supporters who know that it is necessary for stability in the system, is going to be fighting that battle.

The Pecora Commission

EIR: You mentioned the Pecora Commission, which certainly did a critical thing in spotlighting the criminal misconduct of certain key Wall Street players and creating a public groundswell, that President Roosevelt certainly understood quite well how to use. It's notable to me, that we have a contrary situation now, namely that the Wall Street top financiers have been more or less given a permanent "stay out of jail" card. There's actually even something referred to as the Holder Memorandum, which says that sending top bankers to jail would create significant secondary effects, instability in the banking system, and therefore we don't dare do that.

How do you see the issue of criminal prosecutions? The case of JPMorgan Chase comes up prominently this week, with clear indications that at least some top executives were aware of and did nothing to stop the Bernie Madoff Ponzi scheme, which was a blip on the radar screen compared to things like the Libor scandal.

The climate of "too big to jail" seems to be one of the important differences between then and now.

Prins: Well, what happened then was not only did the Pecora Commission showcase the criminal activities of the main bankers, but the main bankers stepped aside and new ones stepped into place. So before, when I referred to bankers supporting Glass-Steagall and working together with FDR, these bankers were his friends. These bankers stepped into running Chase and what was National City Bank at the time, now Citigroup, to commandeer a more stable environment even after the reforms were passed, and they continued to support FDR in that capacity.

The men who had been at the helms of those banks actually were not jailed. One was fined for tax evasion, and one was very embarrassed and abdicated his position. So there is a sense historically that bankers of the main institutions don't get jailed; but the difference back then, was they specifically *did* step aside, and they specifically were prosecuted in some capacity.

Now, today, that hasn't happened, in terms of the bankers who have had the tightest relationships with Washington. You mentioned Chase: Jamie Dimon certainly has a very tight relationship with Washington. And Timothy Geithner spent a lot of time with Jamie Dimon when Dimon was a Class A director at the New York Federal Reserve, and Geithner was running it even before all the bailouts started happening after the 2008 crisis. And everything else that's developed has been the situation where Chase, through Dimon, can say, "Oh this was an element, this was a problem, we can settle on this." And billions of dollars of the settlements have been ways to avoid any criminal implications or punishments, but just sort of passing the buck—literally!

The Department of Justice has really stepped away from prosecuting any of the major banks, particularly the ones with the strongest lines to Washington. That's what we are dealing with right now: that settlements and fines just work to pave over enormous problems and bad practices. And punishments that are really meaningful, the same way actual reform could be meaningful, are not used.

EIR: I was at a briefing given by Sen. Carl Levin last year, the day before the Senate Permanent Investigations Subcommittee released their report on HSBC bank, and found that they were deeply involved in facilitating drug-money laundering on a pretty massive scale, from Mexico; that they were violating all kinds of international sanctions involving both terrorist networks in the Middle East and the Iranian government.

The other thing that comes to mind, is that we're still waiting to see what will be the outcome of the investigations into the Libor scandal, which seems to have been a major market-rigging, and had a significant impact on municipalities and counties around the U.S., which were buying interest-rate swaps as a way of hedging against rate hikes.

It seems that the level of sophistication of some of the criminality that's going unpunished, is probably beyond what was in play in the 1920s and '30s.

Prins: I think on the one hand, yes, it is beyond; things are more complex. On the other hand, I think there's an acceptance, at the higher echelons in Washington, at the Department of Justice, that this complex system that we have right now is sort of too difficult to prosecute. Not necessarily that it is, but the *perception* that it is, so that this amounts to the same lack of prosecution.

It's not that complicated to understand, that if you rig interest rates collectively, and based on that, as you mentioned, municipalities lose money, or investors or clients are purchasing things at the wrong levels, and these banks, in turn, profit from those activities, that that is *fraud*, that is embezzlement, that is all sorts of felonies. And yet, there's this willingness to ignore that, to not try to make the case.

And I think that's the problem that we have today: Yes, maybe things are more complex, but we should be more knowledgeable. This just didn't happen in an instant. And if you're in charge of monitoring or regulating or running a system, or of having the jurisdiction of law over that system, you should step up to the plate. You should learn a bit about what you're dealing with!

And I think there's been a complete reluctance to do that. It's a political reluctance; it's perhaps a knowledge reluctance, but whatever the reasons, it's been an effective means to *not* prosecute, and therefore not agree to fully reform the system.

The simplicity versus the complexity of 1933 compared to 2014 is really not the issue. It's a convenient excuse.

The Dodd-Frank 'Bail-In'

EIR: I absolutely agree.

Recently Federal Reserve Chairman Ben Bernanke, who leaves office in a few days, and Treasury Secretary Jack Lew, have claimed that any new systemic banking crisis of the too-big-to-fail banks will be resolved without another Federal bailout, through various provisions of Dodd-Frank, and specifically, Section 2 of Dodd-Frank, which established a "bail-in" resolution authority, like the bail-in process that we saw last year in Cyprus.

How do you assess the Bernanke and Lew claims that the system is now insulated against another major too-big-to-fail crisis, because of alternatives to a taxpayer bailout, which, most everybody seems to agree, is going to be an *extremely* hard sell at this point?

Prins: I think that's the same wishful thinking/negligent thinking that is behind considering the Dodd-Frank Act to be a sweeping reform; or the Volcker Rule to be a sweeping reform. It's different parts of the same willful misinterpretation of what we're dealing with. The Section 2 of Dodd-Frank specifically calls for banks, particularly the biggest banks, to submit a resolution[2] strategy to the FDIC, and they had done so; that the date to submit a final version was Oct. 30 of last year, whereby they would discuss how they would act in the event of an emergency. I looked at these documents as well: They tend to be about 30 pages, from places like Goldman Sachs and JPMorgan Chase, with about one page of resolution, and 29 pages of explaining what they do for a living.

But in that one page, it basically says things like, "we will adhere to Section 2," that the FDIC will be the authority that, after the banks have exhausted *all other measures*, have exhausted basically trying to find other buyers to get rid of their bad securities, trying to do whatever else they can do—and mind you, this could be in a situation where they're *all* facing the same problems, and they're all interdependent, as they were in 2008, and still are! But they will somehow first try and reduce their size, sell their bad securities, or whatever the problem is. When that doesn't work, the FDIC will effectively take them over, and the FDIC will try to do the same thing.

But the idea that in a crisis situation, where some securities or sector in which all of these six banks are operating, goes belly-up, as we just saw in the 2008 mortgage-related part of this crisis, it is impossible to assume that the FDIC can really take on the risk and the resolution of all the big banks! They are just too big!

Yes, the FDIC can, and has, resolved issues with smaller banks; when IndyMac went belly-up, basically, the FDIC took it over and rejiggered it and sold it to private equity firms. But with JPMorgan Chase, it's very unlikely. And it's *more* unlikely that this would happen if there is a systemic crisis among the six banks—the FDIC just doesn't have the capacity, or the funds, to deal with this!

But the reason the banks only spent a page talking about how they would adhere to Dodd-Frank, and 29 pages of BS about what they do, is because it doesn't matter! Because in the event of a truly large, systemic crisis, with these big six banks being as big and as interdependent and as complex as they are, the FDIC will not be able to resolve the situation by itself.

And so, all the verbiage involved in this, and all of the accolades about the verbiage, is kind of irrelevant if there's actually a crisis.

EIR: One of the other dimensions of this, that I think only came out because of certain limited Congressional demands on further Fed disclosure—Bernie Sanders and even Ron Paul come to mind—is that a certain amount of the bailout in 2008 went to European banks that happen to have operations in the United States, but it was primarily because of the interaction between the big six U.S. banks, and counterparty banks in Europe, like Deutsche Bank, Barclays, UBS, and others. It's not even conceivable that such a crisis would remain strictly within the borders of the U.S. banking system.

Prins: Correct. We can talk about jurisdiction and regulatory authority from the standpoint of justice in the U.S. banking system, just as the big six banks are interdependent and connected in the United States, they're also interdependent and connected on an international basis, which is why the *idea* of this resolution agreement is not something that is effective. Although it is something that the Administration and others seem to want to point to as being effective.

All in the Family

EIR: I understand that in April, you'll be coming out with a new book, *All the Presidents' Bankers*, which takes up this question of the incestuous relationship between Wall Street and our political institutions. Could you give us a preview of the book, and what you hope to stir up with this?

Prins: Well, the book was something that I worked on by going to all of the Presidential archives across the country, to examine what the relationships were between the Democrats, Republicans, and the key bankers of that time, who happen to have been related to a similar set of families—blood relationships, protégé-mentorship relationships—that have run the country over the past more than a century. I examined how those relationships impacted policies over different events: economic panics, like the Panic of 1907, the Crash of 1929, what happened in the wake of the Crash and the Great Depression, how

2. "Resolution" is what the FDIC does when a bank it insures fails: a form of bankruptcy proceeding. The bank is shut down and its assets are transferred to a new entity controlled by the FDIC. From the Financial Times Lexicon.

banks were involved during World War I and World War II, Vietnam, and so forth, up through today's relationship between bankers and Presidents. And some of the same people that have really been components of our history, the same institutions, the same families, continue to be involved in aspects of policy in ways that are not voted on by the public.

It was very fascinating in terms of the research, because I wasn't just focused on economic events, but also on social events to some extent, and military events, and how all those things interrelated to the same set of "recycling" families and people.

EIR: It very much reminds me that one of the fairly recent biographies of Franklin Roosevelt was called *Traitor to His Class.*

Prins: Yes. And what I found very interesting about FDR is that—he was obviously President for quite a number of years—and there were times in which he and his class were very, very much allied, and that included during the beginning of his Presidency, during the passage of Glass-Steagall, at the beginning of the Great Depression. Where that diverged was in the period between the Great Depression's height and World War II. There were some people who actually thought, okay, you've done your regulation, you've done your New Deal: All right, back off! Whereas before that, they were actually aligned with him. However, when they went into the war, they were back, aligned with him, again.

And so it's very interesting to see how his class, and people he hung out with, he grew up with, really supported him, at one point, then diverged, and then resupported him.

It's a very interesting way, to me anyway, of looking at that whole period, as not simply black and white, "supporter" or "traitor," but with a lot of nuances in between.

EIR: One of the studies I was engaged in myself was the process by which Glass-Steagall was repealed, starting back in 1984, when Alan Greenspan was a director at JPMorgan, and they produced a paper called "Rethinking Glass-Steagall." You've probably seen that. It's striking how certain personalities recur. The guy who worked under Greenspan on that project was William Dudley

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Library of Congress

Bankers and Presidents: FDR's friend Jack Morgan, Jr. (left), the only one of the Big Three bankers who opposed Glass-Steagall when it was passed; and Jamie Dimon of Chase (now JPMorgan Chase), who has close ties to Washington and opposes the reinstatement of Glass-Steagall today.

Prins: Who is now the head of the New York Fed.

Dudley and I passed a couple times when we were both at Goldman, and he's actually a really nice guy, but he's in a position where he has to do what he has to do.

What's interesting, is that even in that study, I do mention it; they get a lot wrong. You'll see in the book. At the time, Morgan was obviously against Glass-Steagall. That was the bank that was against it, whereas the other two banks were for it, but they still saw it as a way to sort of decrease their competition; and then once the war started, everyone was on the same side.

But FDR himself was very close to Jack Morgan and Tom Lamont, at the time. He gave them his house when he was assistant Navy Secretary in World War I, and they were going to Harvard, and they had a very longstanding relationship. Some of the letters that I found between them, and actually a third guy at Morgan, [Russell Cornell] Leffingwell, who became head of Morgan later, was very close to FDR, in such a way that he really could tell FDR what he thought was wrong with what FDR was doing, and FDR really responded to him. It was the kind of thinking on those matters that a lot of us haven't seen publicly.

They have self-interested reasons, but so did the people on the other side. But it's very interesting to note that the bankers were always self-serving. That's the nature of capitalism. But you can do it in such a way that you take into account the greater picture. And they don't do that today.

EIR: I find it ironic that you've got Sandy Weill, now, who's come out and said it's time to reinstate Glass-Steagall, and John Reed, also from Citibank. And the *Financial Times*, last year, published three or four editorials in which they said explicitly that the Vickers Commission and the ring-fencing idea, all of these things, are inadequate. And that ultimately we're going to have to have a full-scale separation, Glass-Steagall. So there are obviously some people who are worried that it's not good for the banking sector to—

Prins: Exactly. And that's what happened then [in the 1930s]. The head of Chase at the time, the complement to Jamie Dimon, Winthrop Aldrich [of Chase National Bank], a friend of FDR, was for Glass-Steagall. His predecessor, Albert Wiggin, was a very staunch *dis*-advocate of Glass-Steagall.

Aldrich was in and out of Washington, and he became a fierce advocate of making Glass-Steagall stronger, when, in 1935, the bankers tried to bury it the first time. He was pissed off. And FDR made him his guy, inside Congress. Can you imagine Jamie Dimon being Obama's guy, in favor of regulation? It's not even feasible.

EIR: We're trying to explore some of the fault lines among the Big Six, on the one side, and some of the regional and community banks, on the other. And we're had two or three head-to-head confrontations with the American Bankers Association on these state resolutions.

Prins: Because they don't want it! And they never did, all throughout the history. Obviously, the more they can operate on a national level, the more power they have. They don't like things at the state level—not insurance, not banking, not electricity—because then you have to deal with another set of people who can get in your way.

And the Fed is easy. It's the New York Fed or whatever. Or the White House. That's easy.