

Bad ideas you must fight now

In recent weeks one new idea, one new law, and one existing practice have moved to the forefront. All have the potential to drastically alter the banking industry as we know it.

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The idea – is to nationalize banks. All sorts of people are weighing in on this. Some who should know better, support it.

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Here's a question: If the government failed to recognize, ignored, and to a degree encouraged some of the excesses that have gotten us into this fix, how much sense does it make to have the government take control of, and run, troubled banks?

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The government definitely has to be part of the solution. But nationalization is not the answer.

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Setting up something like the Resolution Trust Company, or closing an insolvent bank, which requires government intervention, are not the same as nationalization. Unfortunately, the widespread confusion over earlier government efforts—especially “TARP”—has paved the way for talk of nationalization. It should be vigorously opposed.

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One key ally here is Federal Reserve Board Chairman Ben Bernanke who has publicly stated that nationalization is neither necessary nor advisable.

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The new law – is the economic stimulus plan, which contains a provision to limit bonuses to the top executives and the top performers at companies that received at least \$500 million from the government under the TARP Capital Purchase Program. This, despite the fact that many healthy banks were encouraged to accept the CPP infusions as a means of leveraging economic growth, which, in fact, has occurred.

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This is a tough issue because, of course, it is already law, but also because of the widespread outrage over overpaid, underachieving execs at a handful of large companies that have had to be bailed out. The outrage in some cases is justified. But the solution shouldn't be a law restricting what private citizens choose to pay other private citizens for services rendered. This is a slippery slope.

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Capitalism does need rules and oversight to counteract excesses resulting from the powerful pull of money. But government-set compensation limits are not the means to use any more than price controls should be used to control inflation. Both create huge back pressures that simply flow elsewhere.

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The rules implementing the compensation provisions have yet to be written. Now is the time to make it clear to the regulators that these provisions are inappropriate and could result in many unintended consequences.

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The existing practice – is mark-to-market (or “fair value”) accounting, the subject of our cover story (p. 18). The misapplication of mark-to-market accounting has greatly exacerbated the current crisis by forcing financial companies to write down certain assets to fire-sale prices even though markets for these assets are not functioning. Banking has been pushing back on this issue for years, but now it is more critical than ever.

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Everyone in the banking industry has their livelihood at stake with these issues. At a recent conference, ABA President Ed Yingling said, “This is the most important and dangerous time in banking in 70 years.” He also told bankers, “We [the ABA] can’t do it all. You have to do it, too. You must make it part of your daily plan to communicate with employees, the media, and Congress” about misguided policy decisions.

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“If you don’t,” he said, “the vacuum will be filled by the wrong message.”

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