

Hope rises for real financial reform

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The Goldman Sachs scandal has done the unthinkable: It's made it possible that legislation reining in Wall Street's casino may actually be enacted.

The odds against real reform are still steep. Wall Street remains the most deep-pocketed lobby in the land. And the problem isn't just Republican opposition. "A lot of our members up here just want a bill passed," says one Democratic legislator. "They don't think that people are watching that closely. But this matters immensely to people. This is a which-side-are-you-on moment."

The clearest way for senators to demonstrate that they're not on Wall Street's side would be to support the bill that Arkansas Democrat Blanche Lincoln plans to bring before the Senate Agriculture Committee on Thursday. Going well beyond the bill that the House passed and the legislation that came out of Connecticut Democrat Chris Dodd's Senate Banking Committee, Lincoln's bill aims squarely at the big banks' most highly leveraged, profitable and risky-to-the-rest-of-us business: their trade in derivatives. (The Ag committee has jurisdiction because derivatives historically were used to trade commodities.)

Lincoln's legislation would require the firms that buy and sell derivatives -- 95 percent of such deals in the United States, according to the Comptroller of the Currency, are done by Goldman, Morgan Stanley, J.P. Morgan Chase, Bank of America and Citibank -- to do their trading openly on exchanges and to post some actual money behind their trades. Today, the market is unregulated. But if Lincoln's legislation passes, no longer would deals with the potential to threaten the nation's economic stability be invisible to regulatory agencies; no longer would businesses seeking to buy derivatives have to accept banks' terms with no ability to shop around or even ascertain the going price for such contracts. No longer would trades with foreign entities be exempt from regulation. And no longer would banks that our government backs up with deposit insurance and access to the Federal Reserve's discounted interest rates be able to put taxpayers on the hook for their speculative bets: They could either continue as derivative-trading casinos or as governmentally insured banks, but not both. In fact, Lincoln's bill goes a good deal of the way toward meeting Paul Volcker's proposal to remove banks' proprietary trading from the umbrella of federal protection.

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On Tuesday, leaders of industries that actually need to lock in prices on real commodities -- in particular, oil -- went to the Senate to endorse Lincoln's bill. "In 2008," said James May, president of the Air Transport Association of America, "we burned the same amount of fuel we burned in 2003, but we paid \$42 billion more." The difference,

he said, was the result of the vast increase in oil speculation carried on through derivatives. Over the past half-decade, for instance, the largest holder of home heating oil often has not been an energy company but, rather, Morgan Stanley. Such speculation, estimated Sean Cota of the Petroleum Marketers Association of America, has increased the cost of gas at the pump by about a dollar a gallon.

"We need predictability in prices," Cota said Tuesday. "The banks want volatility. . . . Old-fashioned bonds built Hoover Dam, but they were paid off over many years. The banks are only interested in trades that pay off in the next 30 seconds. . . . They have no concern for the future of the larger economy."

Time was when government regulators at the Commodity Futures Trading Commission could limit the speculation on (and market manipulation of) the basics of life, but the commission lifted limits on oil speculation during the George W. Bush administration. The Dodd legislation would enable the CFTC to impose such limits on currently deregulated markets. The commission's ability to limit speculators from dominating markets, says Chairman Gary Gensler, has gone "from holding up a 'stop' sign to a 'yield' sign to a 'wave when you go by' sign." Lincoln's bill would restore that stop sign.

While White House political operatives now welcome a fight with the banks, it's not clear that Treasury Secretary Tim Geithner feels the same way. Unable, perhaps, to envision an American economy with a Wall Street shrunken to more manageable dimensions, he has not embraced Lincoln's bill, and some senators fear he will craft a bill with Republican assistance that doesn't truly regulate derivatives. I have heard similar misgivings about Obama economic adviser Larry Summers, who as Treasury secretary in the Clinton administration blocked attempts to regulate derivatives. "We could be looking at the same damn Larry Summers move 10 years later," one Democratic legislator frets. The Lincoln bill is a clear test of the Democrats' ability to learn from their mistakes -- and it will make clear which side they are on.