White House to Banks: “Lend More Money”

"What we’re trying to do is get banks to do what they are supposed to do, which is support the system that we have in America. And banks exist to lend money," said Perino. "So we think that one of the things that we have to do is help recapitalize them so that they have a capital base, so that they are willing to lend money." Along with touting the government largesse, Perino added a caveat: “They [government regulators] will be watching very closely, and they’re working with the banks.”

The French Press Agency AFP reported Perino’s explanation that, while the government cannot force the banks to lend money, they "are regulated by the Treasury Department … [and] they have every incentive to move forward and start using this money."

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At the same time, Treasury Department officials were meeting with banking-industry representatives to remove an impediment that has prevented about 6,000 of the nation’s 8,500 banks from applying for the government program. The program specifies that Treasury will purchase up to $250 billion of senior preferred shares in “qualifying” financial institutions. However, 6,000 of the nation’s banks don’t have publicly traded shares of stock and, therefore, do not meet Treasury’s current qualifications. Treasury’s statement of October 14 noted that, as of that date: “Nine large financial institutions already have agreed to participate in this program.” The nine banks are Citigroup, JPMorgan Chase, Bank of America, Goldman Sachs, Morgan Stanley, Wells Fargo, Bank of New York Mellon, State Street, and Merrill Lynch, soon to be taken over by Bank of America.

According to the Associated Press, Treasury officials have assured banking-industry representatives that they will change the application forms so that privately held financial institutions, as well as banks with publicly traded stock, will qualify for the program. If necessary, officials said, they will extend the November 14 deadline for applying for the government program.

Acting Treasury Under Secretary Anthony Ryan told the annual meeting of the Securities Industry and Financial Markets Association: “As these banks and institutions are reinforced and supported with taxpayer funds, they must meet their responsibility to lend, and support the American people and the U.S. economy. It is in a strengthened institution’s best financial interest to increase lending once it has received government funding."

In correspondence sent to Treasury Secretary Henry M. Paulson, Jr. during the week of October 19, several members of Congress demanded that banks receiving federal bailouts use the funds to increase their lending to previous levels. Excerpts from the correspondence were reported by AFP:

• "This plan will only be effective if these funds are used to increase lending by banks, and it is Treasury's obligation to ensure that," wrote Senator Charles Schummer (D-N.Y.). "The last thing these banks should be doing is stuffing this money under the proverbial mattress."

• Senator Robert Menendez (D-N.J.) stated in the same letter: "Banks must understand that these funds aren't a gift — people and businesses on Main Street are counting on them to use this capital to free up lending, prevent foreclosures and stimulate the economy."

• Representative Barney Frank (D-Mass.), chairman of the House Financial Services Committee, wrote: "Any use of the these funds for any purpose other than lending — for bonuses, for severance pay, for dividends, for acquisitions of other institutions, etc. — is a violation of the terms of the act."

• And House Minority Leader John A. Boehner (R-Ohio) wrote in the letter to Paulson: "Funds made available under the economic rescue package should not be used to pay for bank acquisitions, raises, and executive bonuses."

The Treasury Department statement explaining the bank recapitalization plan lists several standards that qualifying banks must meet, including:

> (1) ensuring that incentive compensation for senior executives does not encourage unnecessary and excessive risks that threaten the value of the financial institution;
>
> (2) required clawback [monies or benefits that are taken back due to specially arising circumstance] of any bonus or incentive compensation paid to a senior executive based on statements of earnings, gains or other criteria that are later proven to be materially inaccurate;
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> (3) prohibition on the financial institution from making any golden parachute payment to a senior executive based on the Internal Revenue Code provision; and
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> (4) agreement not to deduct for tax purposes executive compensation in excess of $500,000 for each senior executive. Treasury has issued interim final rules for these executive compensation standards.

Thus far, there have been no responses from major banking executives to the statements emanating from the White House and Treasury Department concerning the banks' loan policies. The examples quoted in this report are so elementary that it is possible that top banking officers with advanced degrees in finance and years of business experience considered them to be condescending and, therefore, not worth commenting on. Or perhaps, since they received a fresh reminder that they "are regulated by the Treasury Department," it was considered prudent not to annoy the regulators.

Several principles at work in this scenario are worthy of comment. First, it is a tried-and-true principle that government regulates what it subsidizes, so bankers who accept aid from the federal government can hardly be surprised at calls from Washington telling them they should use their bailout money.

Second, bankers already know that making loans is essential to their solvency since money is their product, and no business can survive unless it continues to sell its product. Leading banking executives must recognize the statements emanating from the White House and Treasury Department — redundancies as far as bankers are concerned — for what they are: political statements made for the benefit of the general public.

Third, loans issued at artificially low interest rates or to risky borrowers will lead to more malinvestment and bad loans. So long as the government persists in trying jump start the economy through more money creation, more spending and more borrowing, it will only make matters worse.

Only savings and living within our means will get the economy going again.

And, finally, in an age when few people pay much attention to the Constitution, it must be pointed out that no authority to provide public money to rescue private business is found in the Constitution, much less authority to fund such exercises with fiat, printing-press currency. The powers delegated to Congress by the Constitution in the area of economics are limited to a few specific areas: “lay and collect taxes, duties, imposts, and excises, to pay the debts” of the United States and “to coin money, regulate the value thereof, and of foreign coin, and fix the standard of weights and measures,” and “to provide for the punishment of counterfeiting the securities and current coin of the United States.”

Bankers may have been unwise in violating the laws of economics, but expecting Congress to repeal the laws of economics to bail them out is not only unwise, it is impossible.