Break Up the Giant, Insolvent Banks Using America's 100-Year Old Anti-Trust Laws

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I have previously pointed out that we can (and should) break up the giant, insolvent banks under a number of different laws.

Indeed, the government could break up the "systemically dangerous institutions" under 100-year old antitrust laws.

The Sherman Act

The two primary U.S. antitrust laws are the Sherman and the Clayton Acts. I'll give a very brief overview of the two acts.

The Sherman Act (15 U.S.C. Sections 1-7) – enacted in 1890 – makes trusts and cartels illegal.

Section 1 of the Sherman Act is basically violated if there is:

1. An agreement
2. which unreasonably restrains competition
3. and which affects interstate commerce.

Section 2 of the Sherman Act is basically violated if there is:

1. The possession of monopoly power in the relevant market and
2. the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident.

The Clayton Act

The Clayton Act (15 U.S.C. Sections 12-27 and 29 U.S.C. Sections 52-53) – passed in 1914 – makes it illegal to use price discrimination, exclusive dealings, "tying", mergers and acquisitions which substantially lessen competition, or to perform certain other anti-competitive acts.

Have the Giant Banks Violated the Anti-Trust Laws?

The big banks have gotten bigger and bigger.

Noted economist Mark Zandi says we have an oligopoly of banks, and that "the oligopoly has tightened". Oligopolies and cartels are closely interrelated, in that cartels (e.g. agreements to fix prices) arise when there is an oligopoly (i.e. when a few firms control a market).

Indeed, William K. Black – senior regulator during the S&L crisis, professor of Economics and Law, and an expert on white collar financial crime – says that banks intentionally grew themselves by using fraudulent loan practices. As I explained last month:

> Black explained that fraud by a financial company usually involves the company:
>
> > 1) Growing like crazy
> >
> > 2) Making loans to people who are uncreditworthy, because they'll agree they'll pay you more, and that's how you grow rapidly. You can grow really fast if you loan to people who can't you pay you back
> >
> > and
> >
> > 3) The use of extreme leverage.
>
> This combination guarantees stratospheric initial profits during the expansion phase of the bubble.
>
> But it guarantees a catastrophic subsequent failure when the bubble loses steam.
>
> And collectively – if a lot of companies are playing this game – it produces extraordinary losses (more than all other forms of property crime combined), and a crash.
>
> In other words, the companies intentionally make loans to people who will not be able to repay them, because – during an expanding bubble phase – they'll make huge sums of money. The top executives of these companies will make massive salaries and bonuses during the bubble (enough to live like kings even even if the companies go belly up after the bubble phase).

As the New York Times noted in May:

> President Obama's top antitrust official this week plans to restore an aggressive enforcement policy against corporations that use their market dominance to elbow out competitors or to keep them from gaining market share.

Fortune pointed out in February that the only reason that smaller banks haven't been able to expand and thrive is that the too-big-to-fails have decreased competition:

> Growth for the nation's smaller banks represents a reversal of trends from the last twenty years, when the biggest banks got much bigger and many of the smallest players were gobbled up or driven under…
>
> As big banks struggle to find a way forward and rising loan losses threaten to punish poorly run banks of all sizes, smaller but well capitalized institutions have a long-awaited chance to expand.

Read more at: http://www.huffingtonpost.com/2009/05/11/justice-department-plans-_n_201409.html

In other words, the "tightened oligopoly" described by Zandi has precluded small and mid-size banks from competing with the too-big-to-fails.

In addition, Nobel prize winning economist Joseph Stiglitz noted this week that giants like Goldman are using their size to manipulate the market:

> "The main problem that Goldman raises is a question of size: 'too big to fail.' In some markets, they have a significant fraction of trades. Why is that important? They trade both on their proprietary desk and on behalf of customers. When you do that and you have a significant fraction of all trades, you have a lot of information."
>
> Further, he says, "That raises the potential of conflicts of interest, problems of front-running, using that inside information for your proprietary desk. And that's why the Volcker report came out and said that we need to restrict the kinds of activity that these large institutions have. If you're going to trade on behalf of others, if you're going to be a commercial bank, you can't engage in certain kinds of risk-taking behavior."

The giants (especially Goldman Sachs) have also used high-frequency program trading which not only distorted the markets – making up more than 70% of stock trades – but which also let the program trading giants take a sneak peak at what the real (aka "human") traders are buying and selling, and then trade on the insider information. See this, this, this and this. (This is frontrunning, which is illegal; but it is a lot bigger than garden variety frontrunning, because the program traders are not only trading based on inside knowledge of what their own clients are doing, they are also trading based on knowledge of what all other traders are doing).

Goldman also admitted that its proprietary trading program can "manipulate the markets in unfair ways".

And JP Morgan Chase, Bank of America, Goldman Sachs, Citigroup, and Morgan Stanley together hold 80% of the country's derivatives risk, and 96% of the exposure to credit derivatives.

Federal investigators are currently looking into whether illegal, collusive actions took place with regards to derivatives by the giant banks and others (mainly in regard to credit default swaps).

The giant banks have also allegedly used their Counterparty Risk Management Policy Group (CRMPG) to exchange secret information and formulate coordinated mutually beneficial actions, all with the government's blessings.

Indeed, good lawyers could prove numerous antitrust violations by the giant, insolvent banks.

As one of the world's leading economic historians – Niall Ferguson – recently wrote:

> What's needed is a serious application of antitrust law to the financial-services sector and a speedy end to institutions that are "too big to fail."

As Former chief IMF economist Simon Johnson wrote in June:

> [People are] thinking about the wrong Roosevelt (FDR). In order to get to the point where you can reform like FDR, you first have to break the political power of the big banks, and that requires substantially reducing their economic power – the moment calls more for Teddy Roosevelt-type trustbusting…

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