

bailout, Secretary Paulson actually said that this might discourage participation. It can't be that big a financial crisis if execs would rather forfeit the aid than give back a chunk of excessive compensation.

3. Help homeowners stay in their homes.

4. Rebuild the real economy. It should be obvious that you can't run a consumer economy on debt and low wages. We need a second economic stimulus package that extends unemployment benefits, provides aid to cities and states, and creates good jobs by rebuilding crumbling schools, roads, bridges and water systems. In the medium term (next year!), we should enact the Employee Free Choice Act, so that more workers can join unions and bargain for their fair share of the wealth they create.

5. Re-regulate our financial sector, so we don't end up right back where we started.

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## Ending Casino Capitalism

by ROBERT POLLIN

Wall Street is begging for government life support. Unfortunately, we need to acquiesce to avoid another 1930s-style Depression. But Wall Street has to accept in return a revived regulatory system that would promote financial stability and the well-being of the majority. Here are four observations and proposals, intended to apply to all US financial markets and institutions, whether banks, holding companies, hedge funds or variations thereof:

1. The bailout doesn't have to cost taxpayers \$700 billion. The most cost-effective way to finance the bailout is for the Federal Reserve, not the Treasury, to buy the bad debt from distressed financial institutions. If the Fed, as opposed to the Treasury, buys the bad debt, the funds don't come out of taxpayers' pockets but from the Fed's power to create money. This may seem like alchemy. But in fact it is simply a variation on what the Fed does normally—in conducting day-to-day monetary policy and in managing financial crises. Last year the Fed bought \$840 billion in government bonds outright from US banks. As recently as September 19, the Fed announced plans to purchase short-term debt obligations issued by Fannie Mae, Freddie Mac and the federal home loan banks as a way to “further support market functioning.” The Fed can later resell the bad debt to private dealers, albeit at distress-level, cut-rate prices. In any case, the funds to transact these operations will not have to come from taxpayers.

2. Tax speculators. A small sales tax on all securities transactions—stocks, bonds, derivatives, mortgage-backed securities, short sales and all new schemes—would raise the costs of speculative trading and therefore discourage casino capitalism. At the same time, the tax will not discourage investors who intend to hold securities for a longer period since unlike the speculators they will be trading infrequently. This tax could generate, conservatively, \$100 billion per year in government revenue—enough to cover, for example, a green investment program that could create 2 million new jobs.

3. Impose asset-based reserve requirements. These force financial institutions to maintain cash reserve funds in proportion to the riskier assets in their portfolios. They can discourage firms from holding excessive amounts of risky assets and serve as a cash cushion to draw on when market downturns occur. The same principle guides the margin requirements that apply to stocks purchased with borrowed funds. During the late 1990s, Federal Reserve chair Alan Greenspan acknowledged that he could have dampened the stock market bubble by raising margin requirements, but he refused to take action. Measures like these can also push financial institutions to channel credit to projects that advance social welfare. Policy-makers could stipulate that, say, at least 5 percent of banks' loan portfolios be channeled to low-cost housing and 5 percent to green investments. If the banks fail to reach these quotas, they would then be required to hold this same amount of their total assets in cash.

4. Loan guarantees for priority productive investments. Financial bailouts are a form of credit risk insurance for reckless speculators. Instead we need to provide credit risk insurance—i.e., loan guarantees—to promote social priorities like affordable housing and green investments. Investments in these areas will expand. The securities sales tax and asset reserve requirements should prevent speculators from converting such initiatives into new casino opportunities. As such, the overall costs to taxpayers would be small.

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## Bridge Loan to Nowhere?

by THOMAS FERGUSON and ROBERT JOHNSON

Henry Paulson and Ben Bernanke's bailout plan is not only the most expensive; it is also the most likely to fail. But there is more than one way to restore trust and restart markets. First, take a leaf from the New Deal. That is, just send bank examiners into all the institutions—investment houses and insurance companies, as well as banks—to assess them. Insolvent ones are closed; everyone knows then that those that survive are solvent. Economic life restarts. The total cost to taxpayers is minimal.

Guess why Wall Street hates this one and why Bernanke and Paulson do not even consider it. In all likelihood much of the Street is insolvent, which is why short-sellers were going wild until the SEC restricted them.

A second way is for the government to inject capital directly into those financial institutions with a reasonable prospect of surviving in the long run. This was the essence of Senator Chuck Schumer's proposal, which surfaced just ahead of Paulson's announcement. The New Deal did this, too. It used the Reconstruction Finance Corporation, which put severe terms on banks receiving aid. Wall Street, of course, would love the money but not the terms. Somebody to inspect and certify the solvency of financial houses is also prerequisite for this option, which is anathema to the Street.