***Still* Million Dollar a Month Salaries…**
***Still* Tens of Billions to the Bank of China…**

Be Skeptical of Senate Bailout Bill

All the Old Problems Remain

A Single Comprehensive Updated Article by Congressman Brad Sherman
October 1, 2008

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New Senate Provisions: No Reason to Switch to "Yes" Vote

The Senate will attach its tax extenders bill to the House-defeated Bailout Bill. The Senate tax extenders bill is the very bill Hoyer refused to bring to the floor Monday, September 29, because of its gross violation of pay-go. If the Bailout Bill is open to tax provisions, why not attach the bills that prevent hedge fund managers from paying zero tax by using Cayman Island tax havens? Why not add the Credit Card Holders Bill of Rights, which recently passed the House?

The Senate Bill also increases the FDIC limit to $250,000. We don't need to send $700 billion to Wall Street to make this change.

Experts Say: Congress Should Not Panic

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Taxpayers Highly Unlikely to Recoup Any of the Costs

I. Section 134 of the Bailout Bill merely says that the President must submit a revenue bill to Congress in 2013 that recoups from the financial industry the taxpayers' net losses.
   a. If the President has any revenue ideas he actually likes, he would submit them to us anyway.
   b. If the President submits revenue ideas only because he is forced to by Section 134, he will send it to us with a note saying that he believes they are bad for the country and reserves the right to veto.
   c. **The Bailout Bill does not automatically enact any revenue increases, nor protect a revenue bill from filibuster or veto.**

II. Congress is unlikely to pass a bill with hundreds of billions of dollars worth of tax increases in 2013.
   a. Tax increase bills are anathema to many.
   b. 41 Senators can block the plan. We're giving Wall Street enough money to hire 4,100 lobbyists.
   c. In recent years, Wall Street has easily defeated every attempt to close every loophole that they exploit, no matter how pernicious—even the abusive use of Cayman Island tax havens by hedge fund managers, who thereby pay zero tax.

III. **Any tax on the financial industry would make the good banks pay a huge tax so we can recoup what we gave to the bad banks.**
   a. Section 134 says the tax will be on "the financial industry." It does not provide for a tax on just those firms that received bailout payments.
   b. A bank that doesn't get a bailout payment still pays the tax.
   c. Community banks and perhaps credit unions will also be subject to the tax, so we can recoup what we gave to Wall Street.

IV. **It is impossible to draft a tax that hits only those firms that received bailout payments, and even more impossible to draft one that taxes each bank in proportion to how much money we lost on its toxic assets.**
   a. There are no provisions to even keep track of losses on each asset purchased as it is managed over the years. Assets purchased from several banks will be pooled, managed, and sold together, and we can never know how much we lost on assets purchased from any one bank.
   b. If three banks in the year 2013 have the same income and size and operations, they will all pay the same tax—even if one got no bailout payments, a second got a million dollars, and a third got a billion dollars.
   c. **Many bailed out firms won't exist in 2013.**
      1. Some will go under.
      2. Some bailed out firms are only shell companies. *Example*: Assume the Bank of Shanghai has $30 billion in toxic assets. It will sell these to the tiny subsidiary it has incorporated in

California. The subsidiary will then sell these to the Treasury in 2009 and will be dissolved long before 2013.

3. Many bailed out firms will still be unprofitable in 2013.
4. Some bailed out firms will move offshore before 2013.

d. The whole purpose of the Bill is to improve the balance sheets of the bailed-out firms. If particular bailed-out firms *owe* us the money they receive, they would have to list this as a liability, and the Bill would fail to improve their balance sheets.

In 2013, we will not pass a tax bill that imposes hundreds of billions of dollars of taxes on the financial services industry, including those banks that got no bailouts, community banks, and credit unions. A tax bill imposed only on those entities that got bailout payments is impossible to draft and contrary to the purposes of the bill.

If it were easy to pass a bill to recoup hundreds of billions of dollars through taxes to be imposed in 2013 and thereafter, then provisions imposing such taxes would be in today's bill.

Wall Street gets their money now, and we get it back never.

New Insurance Provisions Meaningless—Won't be Used

The Bill requires the creation of a new insurance program but does not require Treasury to use it. Treasury won't use this authority because Paulson hates it and because initial cost projections say it is even more expensive than the bailout approach.

Hundreds of Billions Will Be Used to Buy Toxic Assets Currently Held by Foreign Investors

Under the Bill, the Administration can buy any asset from any financial institution for any price. Some think that only U.S. investors will be bailed out.

Major foreign investors have already been assured that they can benefit from the Bailout. Under the Bill, **the Bank of China can sell a portfolio of toxic assets to a U.S.-headquartered investment bank on Monday**, and that investment bank can then sell those same assets to the Treasury on Tuesday. The foreign financial press indicates that foreign investors are sure that they will get at least tens of billions of dollars.

The Bill should contain a provision stating that the Treasury can buy only assets proven to be held by an American investor on September 20, 2008. This provision has been rejected by the Administration, the same Administration that has promised foreign investors that they too will be bailed out.

While the transparency provisions of the Bill are generally good, they do not require disclosure of how long the seller of a toxic asset owned it or from whom they purchased it. Accordingly, if the Treasury buys a package of toxic assets from a U.S. investment bank for $20 billion, the amount paid and the nature of the assets purchased will be disclosed—but the fact that those same assets had been owned by the Bank of China just two days prior will not be disclosed.

Million-Dollar a Month Salaries Will Continue

The bill contains limits on the use of certain esoteric formulas to compute executive bonuses at bailed-out banks. It has some limits on golden parachute contracts for departing executives. It provides that certain executives who benefitted from fraud may lose those benefits in the event that such fraud is proven in court.

However, the Bill has no limits on regular, plain vanilla salaries paid to executives of bailed-out firms. Million-dollar a month salaries will continue. And, any executive who feels that his bonus is too low is free to ask his firm for a multi-million dollar increase in base salary.

The President stated that "taxpayer dollars will not be used" to pay enormous compensation to Wall Street executives. The President's words were chosen carefully. Bailed-out banks are free to use all their other assets to pay million-dollar a month salaries and to use the bail-out money to pay all their other expenses.

Under the latest bill, bailed-out banks may not get tax deductions for excessive compensation paid to executives. This has no effect on the executive or *his* tax return. And, the banks we are bailing out are not likely to be profitable—so they hardly have a need for tax deductions.

Five Member Oversight Board Includes 3 Bush Appointees/Separate Democratic-Majority Board Is Powerless

Much has been discussed about the Financial Stability Oversight Board provided by the bill. The five-member Board consists of Bush appointees. The Bill also creates a Congressional Oversight Panel. These panels can critique any action Paulson takes, but it cannot delay, halt, or reverse anything.

Few if Any Homeowners Will Get Mortgage Relief

As you know, the Bill will not contain any provision allowing the terms of a mortgage to be changed without the consent of *all* the investors who own the mortgage. However, we are told that by investing $700 billion in toxic assets the federal government will be in a position to provide reasonable loan modifications to the homeowners whose mortgages it buys.

As well-detailed in a document from the Center for Responsible Lending[1], few homeowners will benefit from this provision. This is because the Treasury will chiefly purchase mortgage-backed securities which **will make the federal government one of several co-owners of millions of mortgages. Whether or not any mortgages are modified will be determined by the loan servicer acting on behalf of all the various investors who own a piece of the mortgage.** That is why Section 108(d) states in part "The Secretary shall *request* loan servicers servicing the mortgage loans to avoid preventable foreclosures… [Emphasis added.]" Congress has already requested all loan servicers nationwide avoid preventable foreclosures, so an additional request from the Treasury is unlikely to change current behavior.

The Bill has non-binding provisions urging Paulson to buy whole mortgages, rather than mortgage-backed securities, but he is unlikely to do so.

All $700 Billion Can Be "Invested" Before January 20, 2009

The Bill provides that after the first $250 billion is spent, President Bush needs to sign a letter to get the next $100 billion. Some therefore believe that the President is only receiving $350 billion that he can expend now and the rest depends on Congressional action.

The Bill provides that the second half of the $700 billion can be spent *unless* Congress passes a resolution of disapproval within a short period. Such a resolution would have to pass the House and then the Senate and would then be subject to veto. Then any **veto** would have to be overridden by both the House and the Senate. Unless the resolution clears all these hurdles, the President is free to spend the second half of the $700 billion.

The fact that such a resolution of disapproval is given fast-track procedures simply means that the inevitable veto, and the inevitable failure to override that veto, will happen quickly.

Paulson has said that he doesn't expect to spend more than $50 billion per month. **Paulson clearly could spend the entire $700 billion by January 20th. The Merrill Lynch $50 billion sale took place in roughly two days**—and both parties were negotiating hard for the best deal. Paulson's announced purpose is to pay generously for the toxic assets held by Wall Street firms, to help those firms prosper—so negotiations should be even quicker.

This Administration has a history of using every authority granted by Congress. The Administration has threatened to veto any bill which contains a provision which would prevent them from spending the full $700 billion by January 20th.

[1] http://www.responsiblelending.org/issues/mortgage/quick-references/the-problem-with-the-paulson-bailout-plan.html

Taxpayers will get little or no equity upside—and will probably overpay for what they do get

Section 112(d) of the Bill states that whenever the Treasury purchases toxic assets, it must also receive, as part of the deal, at least some warrants or senior debt instruments. However, a couple of dozen small warrants or a tiny senior debt instrument fulfills this statutory requirement. It is totally up to the Treasury to decide whether the price being paid for a combination of toxic assets and warrants is appropriate.

In the AIG deal, the taxpayers received 80% of the company. In contrast, Paulson did not want any warrants to be received under this bailout program. He is being dragged kicking and screaming into a provision that requires him to get some warrants, but allows him to get as few as he wishes.

Meaningful Regulatory Reform and Corporate Governance Reform will be Subject to Filibuster in the 111th Congress/Bill Contains No Applicable Fast-track Provision

We are promised that next year we will pass the legislation to make sure that this travesty does not repeat itself. We are promised strong, tough legislation that Wall Street has traditionally hated dealing with regulatory reform and corporate governance reform.

Any tough regulatory reform or corporate governance reform proposed in the 111th Congress will be subject to regular Senate rules. Wall Street may not be able to defeat good reform—instead, they will delay and then dilute. It will take only 41 Senators to insist on delaying any legislation until it is diluted. This Bill makes sure that Wall Street has the liquidity necessary to hire 4,100 lobbyists.

We Have Time to Write a Good Bill: The Sky Will Not Fall

It is in the interest of Wall Street to cause us to panic and pass bad legislation.

No one can say for certain whether our economy will be better off next year if we pass the bill or if we defeat it. Only by avoiding a panic vote can we write a good bill next week.

The White House declared that the sky would fall if we did not pass a bill by September 24. They also said they would *veto* a bill with significant controls on the Administration or on the salaries of executives of bailed out firms. If not for Administration interference, we would have passed a good bill already.

Last Thursday night (September 25), there was a precipitous decline in the likelihood that Congress would immediately rubber-stamp Bush's proposal. Most stock markets went up Friday, September 26, indicating that investors would buy equity in the American economy even if the bill stalled.

Fear mongers claim the Monday stock market drop was the greatest single-day drop ever, and was due to our Bailout Bill vote. **Monday's drop was the 17th largest daily drop**

as a percentage of the market's value, and almost half of Monday's drop took place while investors were certain the Bill would pass.

On Monday morning (September 29), *everyone was certain* that we would pass the bill, and the market dropped still about 340 points before 10:00am. The fear mongers are falsely trying to ascribe this 340-point drop to the Bailout Bill's defeat. The Dow was then stable for three hours until we began to vote and dropped another 440 points after the vote. **Yesterday, the Dow then returned to virtually the same level it had stood at just before the vote at 1:28pm Monday**.

The markets may fall if we vote "No" on the latest bill—but we now know that the sky will not fall.

Experts Say: Congress Should Not Panic

"We ask Congress not to rush, to hold appropriate hearings, and to carefully consider the right course of action." – 231 eminent Professors of Economics, including 3 Noble Laureates, organized by Professor John Cochrane (University of Chicago). September 25, 2008.[2]

"There is a kind of suggestion in the Paulson proposal that if only we provide enough money to financial markets, this problem will disappear. But that does nothing to address the fundamental problem of bleeding foreclosures and holes in the balance sheets of banks." –Joseph Stiglitz (Nobel Laureate, Columbia University). September 26, 2008[3]

"I have doubts that the $700 billion Bailout if enacted, would work." -William M. Isaac, (Former Chairman, Federal Deposit Insurance Corporation).[4]

Under the latest bill, only two things are for certain: Wall Street firms and executives will benefit, and our children will be stuck with an enormous debt.

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[2] http://faculty.chicagogsb.edu/john.cochrane/research/Papers/mortgage_protest.htm

[3] Neil Irwin and Cecilia King. "Away from Wall Street Economists Question the Effectiveness of Paulson's Plan." Washington Post. 9/26/08.
http://www.washingtonpost.com/wpdyn/content/article/2008/09/25/-AR2008092504531_pf.html

[4] Washington Post, September 27, 2008, p. A19