September 28, 2008

As I have mentioned before, Members of Congress from both parties were fairly united in rejecting the bailout proposal that President Bush first sent to Congress a week ago. That Paulson Proposal sought to invest unlimited and unchecked power in Secretary of the Treasury Henry M. Paulson, Jr., and Republicans and Democrats both said no. As my late father, Henry B. Gonzalez, once said of another financial situation, back when he was Chairman of the House Banking Committee, "The issue is power," and no one man should have that much power.

In bipartisan and bicameral discussions earlier this week, House and Senate Democrats and Republicans came up with a new and better plan. Instead of giving the Secretary $700 billion dollars up front, the money would be delivered in phases, with Congress retaining control and demanding reports along the way to prove that it was being well spent. We would retain full and powerful oversight of the efforts to salvage the markets. Importantly, too, the money would be spent to purchase equity in the companies or to make loans that would be paid back with interest so that, if we do this right, the American people might even see a profit on your investment. And, though the Administration objected strenuously at first, we forced them to agree that CEO pay and severance packages must be reduced; no one should get a parachute made from taxpayer gold.

Unfortunately, on Thursday, the House Republican Leadership upended that consensus and injected partisan politics into what had been a cooperative effort, introducing what the editors of the Washington Post have described as a "plan whose merits are dubious and that in any event arrives on the scene far too late." In a roughly sketched outline, reminiscent of the Paulson Plan's three short pages of "Give me money and power and don't ask questions," the Republicans laid out a proposal of tax cuts for Wall Street investors and, what may be even worse, a convoluted insurance scheme. That plan presumes that the 15 percent tax on investment profits - in contrast, a teacher earning $40,000/year owes 25 percent in taxes - is what's standing in the way of Wall Street regaining its feet, and if we protect those investors, they'll pour their millions and billions of dollars back into the system. We must then, under this plan, deregulate the markets still further, because they don't believe that relaxing the rules helped lead to this situation in the first place.

Thus, as bad as it is, the so called "insurance" proposal may not even be the most reckless part of the proposal. According to Minority Leader Boehner, the plan would not require the taxpayers to spend any money. Of course, neither would invading Iraq. The problem is, we have seen this kind of credit swap before. Under the Republican plan, the assets would not be purchases, so the investment banks get to keep the mortgage-backed securities they bought, and simply pay for "insurance". That's what AIG used to do with such assets, providing insurance that they wouldn't go bad. You remember AIG, right? The insurance company we had to bail out to the tune of $85 billion just a week ago because their attempts to insure mortgage-backed securities proved so disastrous.

Basic economics, not to mention common sense, says that insuring securities that you already know are failing, securities that are not worth what they cost, is bad business. There is a reason

that the Administration was unable to convince private lenders to bail out AIG: they recognized the weaknesses of that business model. Now, Mr. Boehner wants to encourage the same practices across the board, while cutting taxes on rich executives and corporations and further relaxing the rules that govern them. I imagine that sounds as fishy to you as it does to me.

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