Private Policies and Public Power

When Banks Act as Regulators within a Regime of Privilege

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Abstract

An emerging trend in financial services is banks' increasingly common refusal to do business with industries for political reasons rather than for traditional business justifications. Banks' refusals are often explained by a desire to make a difference or send a message. While this desire may not raise a concern in most cases, banks are not like most other businesses. Banks enjoy an extensive regime of privilege provided by federal and state governments that includes barriers to market entry and exit, more favorable regulatory treatment than nonbank competitors in some areas, and direct and privileged access to services provided by the government. This paper asks whether this public power, granted to banks for the purposes of facilitating lawful commerce, is being misused when banks try to regulate downstream markets through withholding services and what, if anything, should be done to address these actions by banks.

JEL codes: G2, G3, K1, K2, L2, L5, M1, N2

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Brian Knight and Trace Mitchell

In June 2019, Bank of America announced it would cease doing business with companies that run private prisons and detention centers.[1] JPMorgan Chase, SunTrust, and Wells Fargo had already announced similar policies.[2] Private prisons are not the only issue over which banks recently refused services to politically controversial firms. Shortly after *New York Times* DealBook columnist Andrew Ross Sorkin wrote an article in 2018 that proposed that credit card companies, credit card processors, and banks "effectively set new rules for the sales of guns in America" by refusing to serve retailers that offer certain legal guns and accessories,[3] Citigroup announced it would refuse to offer payments services to firearms retailers unless they met certain conditions above and beyond the legal requirements governing firearms sales. These included requirements to limit sales of firearms to people 21 years of age or older[4] and to refrain from selling bump stocks and "high-capacity" magazines. Bank of America followed suit, announcing that it would refuse to lend to clients involved in the manufacture of "military-style" weapons for civilian use.[5]

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[1] Kathleen Joyce, *Bank of America to Stop Financing Private Prisons, Detention Centers*, FOX BUS., June 27, 2019, https://www.foxbusiness.com/business-leaders/bank-of-america-announces-it-will-stop-financing-private-prisons-detention-centers.

[2] Emily S. Rueb, *JPMorgan Chase Stops Funding Private Prison Companies, and Immigration Activists Applaud*, N.Y. TIMES, Mar. 6, 2019, https://www.nytimes.com/2019/03/06/business/jp-morgan-prisons.html; *SunTrust Is Latest Bank to Halt Financing of Private Prisons*, AM. BANKER, July 8, 2019, https://www.americanbanker.com/articles/suntrust-is-latest-bank-to-halt-financing-of-private-prisons.

[3] Andrew Ross Sorkin, *How Banks Could Control Gun Sales if Washington Won't*, N.Y. TIMES, Feb. 19, 2018, https://www.nytimes.com/2018/02/19/business/banks-gun-sales.html.

[4] The legal age to purchase a long gun is 18 under federal law and many states' laws.

[5] Kevin McCoy, *Bank of America Halting Business with Makers of Military-Style Guns for Civilian Use*, USA TODAY, Apr. 11, 2018, https://www.usatoday.com/story/money/2018/04/11/bank-america-halting-business-makers-military-style-guns-civilian-use/506223002/.

In each case, the bank cast its decision as an effort not only to distance the bank from conduct its management found objectionable but also to force change in the market. Bank of America Vice Chair Anne Finucane described the firearms policy as an effort to help combat mass shootings,[6] and Citi explicitly called on the financial services industry to come together and "leverage collective action to encourage responsible practices by all who sell firearms."[7] Citi's statement did not mention traditional business concerns such as profit or efficiency.[8] Rather, it was couched in political terms, lamenting what Citi perceived as a lack of action by Congress and explicitly seeking to foster changes in the market for firearms by leveraging the critical position financial services play in the modern economy.[9] Likewise, in explaining Bank of America's decision to cut ties with companies that run private prisons, CEO Brian Moynihan did not claim that such business was unprofitable but rather that Bank of America wanted to "make a statement" about the need for immigration reform.[10]

"Responsible practices," judging by Citi's policy, are presumably more restrictive than those required by law and may include restrictions on the manufacture or sale of legal products. "Encouragement" appears to mean threatening to refuse services to companies that rely on them,

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[6] *Id.*

[7] Ed Skyler, *Announcing Our U.S. Commercial Firearms Policy*, CITIGROUP (Mar. 22, 2018), https://blog.citigroup.com/2018/03/announcing-our-us-commercial-firearms-policy/.

[8] The question of whether there may be traditional business justifications, such as profitability and risk, for denying service to certain firms or industries is outside the scope of this paper. This paper is only concerned with situations in which banks are seeking to leverage their government-granted privilege to suit their political preferences.

[9] The announcement begins by saying, "For too many years, in too many places, our country has seen acts of gun violence that have resulted in heartbreaking losses. We are all too familiar with them and there is no need to recount them here. Over the same amount of time, we have waited for our grief to turn into action and see our nation adopt common-sense measures that would help prevent firearms from getting into the wrong hands. That action has sadly never come and as the weeks pass after the most recent mass shooting, it appears we are stuck in the same cycle of tragedy and inaction. As a society, we all know that something needs to change. And as a company, we feel we must do our part." Skyler, *supra* note 7.

[10] Michael Van Schoik, *Why Bank of America Cut Ties with Businesses Operating Detention Centers*, FOX BUS., July 21, 2019, https://www.foxbusiness.com/business-leaders/why-bank-of-america-cut-ties-with-businesses-operating-detention-centers.

not mere persuasion.[11] In effect, Citi is calling for banks to impose extralegal restrictions on the sale of firearms. While this does not constitute "regulation" as the term is generally used,[12] it amounts to de facto regulation.

Banks are not the only firms that change their policies in order to further political goals. Most other entities, however, do not raise the same policy concerns. Banks may be different because much of their power—what Citi and Bank of America are explicitly trying to leverage to force change in downstream markets—is derived from privilege granted by government.[13]

Banks are granted a charter at the government's discretion. Bank charters confer regulatory advantages that nonbank competitors do not enjoy, particularly in the areas of lending and money transmission. Banks also receive access to government services such as deposit insurance and the Federal Reserve's payments systems that may result in a direct subsidy. Even if the service does not provide a subsidy in an economic sense, the government still acts as an unimpeachable service provider. And when banks, especially large banks, get into trouble, the government frequently bails them out. This not only saves them from failing but also makes it cheaper for them to access funding. All of this may make both the banking industry and specific banking firms more powerful in the market for "banking services"[14] than they would be otherwise—and may thus enable them to adopt policies that amount to de facto regulation.

It is one thing to say that a market participant should not be required to do business with people it disagrees with. It is another thing, however, to say that firms can use their government-

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[11] Skyler, *supra* note 7.

[12] "People intuitively understand the word 'regulation' to mean government intervention in liberty and choices—through legal rules that define the legally available options and through legal rules that manipulate incentives." Barak Orbach, *What Is Regulation?*, 30 YALE J. ON REG. ONLINE 1 (2012).

[13] Government-granted privileges exist on a spectrum, and there may be other privileged industries that raise similar questions—for example, the automobile industry has also been the recipient of significant government bailouts, and domestic airlines enjoy some level of protection from competition through cabotage laws—however, this paper focuses exclusively on the provision of banking services.

[14] We use the term *banking services* to include, inter alia, credit, payments processing and services, and savings.

granted privileges for purposes different from and potentially inconsistent with the reasons those privileges were granted. The protection banks enjoy is justified on the grounds that banks are considered essential to enabling the saving, payments, and credit intermediation necessary for a functioning economy. This protection has contributed to a situation in which banking does not operate in a free market.[15] Importantly, public policy also encourages stability in banking, which may have the result of privileging incumbents (especially large incumbents) at the expense of entrants and competitors.[16]

Banks are expected to exercise judgment to better facilitate commerce, and to reap profit for doing so effectively.[17] Some scholars have argued that banks should be considered public utilities and should have their discretion limited.[18] Conversely, the legitimate authority to regulate—that is, to decide what items or activities are legal and to back up those determinations with coercive force—has been the purview of representative government, whose authority is subject to political checks and balances. In other words, legitimate power in democracy is limited and constrained.

Certain banks, using the power granted to them by government, are adopting policies that amount to de facto regulation. This poses at least two serious problems: First, this use of government-granted privilege may be inconsistent with the purposes of the original grants, as

[15] *See infra* Section I.
[16] *See infra* Section I.
[17] While the subject is outside the scope of this paper, it should be noted that the law places both hard and soft limits on banks' judgment in other contexts. For example, the Community Reinvestment Act, intended as an antidiscrimination measure, has arguably also become a tool for off-the-book subsidization of certain politically favored groups. This reflects public actors' use of private actors as a tool of public policy, rather than private actors' use of public power for private purposes (which is the subject of this paper). CHARLES W. CALOMIRIS & STEPHEN H. HABER, FRAGILE BY DESIGN: THE POLITICAL ORIGINS OF BANK CRISES & SCARCE CREDIT 220–21 (2014).
[18] *See infra* Section II.B.

determined by the legislative process.[19] Second, because banking services are essential to commerce and because markets are distorted by regulation, banks can exercise significant power by facilitating or impeding access to these services. Therefore, an arbitrary denial of service to some customers may contradict the very rationale for the privileges and protections granted to banks in the law. Indeed, banks operate within a "regime of privilege"[20] granted to them by government to facilitate commerce, secure liquidity in credit markets, and accomplish similar objectives.[21] If this regime results in undesirable and unintended consequences, like abuse of power, the regime may need to be reconsidered.

This paper discusses these potential problems and considers ways to remedy them. The first section surveys many of the mechanisms by which the government enhances the power of banks, effectively granting them privileges and prerogatives. The second section discusses the normative and practical concerns posed by banks serving as de facto regulators. The third section discusses possible solutions to the problem of banks ascribing to themselves the right to act as regulators.

Having discussed what this paper *is* about, it is important to note what it is *not* about. This paper should not be read as an attack on the idea that firms could use their market power to further ideas they support, but rather as raising concern about the possibility of government power being used for private purposes that conflict with the intent for which the power was granted. This paper focuses on the direct role financial regulation plays in enhancing the power

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[19] To the extent that banks impose more stringent requirements than those required by law, they are acting inconsistently with the law, and in some cases may be in violation. For example, Citi's requirement that customers not sell guns to those under 21 may run afoul of laws prohibiting discrimination on the basis of age. *See, e.g.*, Suzanne Roig, *Two Oregon Men File Discrimination Complaints Against Fred Meyer, Bi-Mart over Gun-Sale Denials*, THE BULLETIN, Mar. 22, 2018, https://www.bendbulletin.com/business/6109148-151/two-oregon-men-file-complaints-against-fred-meyer.
[20] The authors are grateful to Walter Valdivia for suggesting this very apt phrase.
[21] Whether the regime itself is or could be legitimate is outside the scope of this paper.

of banks and on what such power entails. It is not a commentary on any of the underlying issues that may tempt banks to use that privilege to act as de facto regulators.

Nor do we mean to call into question the propriety of banks choosing customers on the basis of traditional business considerations, including profitability, efficiency, and safety and soundness. Our focus is purely on the extent to which banks can exercise discretion by controlling or limiting the availability of legal goods and services for de facto regulatory purposes.[22] We acknowledge that some decisions may have multiple motivating factors.[23] Ultimately, this paper seeks to highlight a possible area of concern and invites further research and debate, rather than providing a definitive answer.

Additionally, this paper will focus on direct financial regulation and will not discuss more indirect potential sources of privilege, including monetary policy or taxation or antitrust issues. Behavior may be objectionable and warrant government intervention when the firm in question has significant market power, regardless of whether that market power is the product of government protection. The same behavior may not justify government intervention if the firm has less market power. This is different from the question of whether it is appropriate for banks to use the power that government grants them to adopt business policies intended as de facto regulation. This paper focuses on the latter question.

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[22] We distinguish between the banks' goal and motivation. A bank's goal can be to de facto regulate while its motivation could vary. Motivations might include a desire by bank leadership to limit access to certain legal goods and services or to curry favor with politicians, government officials, or special interest groups that wish to see access restricted but lack the political power to restrict it. This paper focuses on the banks' goal.

[23] For example, banks might act to improve relations with their employees or politicians. Likewise, the increasing prominence of "environmental, social, and governance" (ESG) considerations in business decision making could be relevant, or could be used as a pretext. The legitimacy and role of ESG are beyond the scope of this paper.

I. Banks' Regime of Privilege

Banks operate in a highly distorted market. This distortion takes many forms, including barriers to entry, direct support from the government in the form of certain services, and, for some banks, government rescue from failure. Additionally, banks enjoy some regulatory advantages over their nonbank competitors, including in the areas of lending and money transmission. This section will discuss some of these distortions, but it is by no means an exhaustive catalogue. The section will proceed as follows: it will first discuss the barriers to entry that protect banks from competition; it will then discuss the advantages that banks enjoy over nonbank competitors, including regulatory advantages in lending and money transmission and services that the government provides to help banks operate; finally, it will discuss the direct and indirect impact of bailouts.

It is important to note that we do not claim that government support for banks is a binary characteristic. Rather, it operates on a continuum: some banks receive relatively less support and others receive relatively more. For example, as discussed below, only certain banks received or were credibly expected to receive the full spectrum of government assistance during the 2008 financial crisis. Likewise, arrangements such as deposit insurance provided by the Federal Deposit Insurance Corporation (FDIC) impact banks differently depending on how reliant the bank is on deposits.[24] In addition, we acknowledge that regulation imposes costs on banks as well as conveying benefits. That said, given the barriers to entry that face would-be competition, the regulatory advantages banks enjoy over nonbanks, and broad use of government-provided, bank-exclusive services, it is reasonable to assume that banks receive considerable government support. This support constitutes a major difference between banking and most other industries,

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[24] *See, e.g.*, GOVERNMENT ACCOUNTABILITY OFFICE, GOVERNMENT SUPPORT FOR BANK HOLDING COMPANIES: STATUTORY CHANGES TO LIMIT FUTURE SUPPORT ARE NOT YET FULLY IMPLEMENTED 4 (Nov. 2013).

and it should perhaps give us pause when banks seek to de facto regulate by cutting off access to the services for which they have received government benefits.

A. Barriers to Entry

Banking is not a market with open entry. Instead, prospective banks must obtain permission from the government in the form of a charter from either the Office of the Comptroller of the Currency (OCC) for nationally chartered banks or a state regulator for state-chartered banks. Deposit insurance from the FDIC, while arguably not required, is generally considered essential.[25] The charter and FDIC insurance are granted at the regulator's discretion. As discussed below, the need for a charter and FDIC insurance serve as barriers to entry and provide a competitive advantage to firms that have surmounted them.

1. CHARTERING

A fundamental way that the government empowers banks is by issuing bank charters. By issuing a bank charter, the OCC or a state regulator grants a firm the ability to engage in core banking functions such as receiving deposits, paying checks, and lending money.[26] The chartering system also limits the ability of nonchartered institutions to engage in many of these core banking functions.

Because nonchartered institutions are placed at a regulatory disadvantage[27] in their ability to engage in core banking functions such as accepting deposits, lending, and transmitting money, chartered banks face less-effective competition in these areas. This may mean that chartered

[25] Aside from the obvious benefit of insured deposits, FDIC insurance is a prerequisite for obtaining certain government-granted benefits. *See infra* Section I.B.3.
[26] 12 C.F.R. § 5.20(e)(i) (2019).
[27] *See infra* Section I.B.

banking institutions have greater market power than they would naturally have, as a result of the barriers to entry that the government establishes.

a. The chartering process. Bank charters are issued by the federal government for national banks and by state governments for state banks. Anyone attempting to organize a national bank is required to submit an application with the OCC, a bureau within the Department of the Treasury, for the purpose of obtaining approval before engaging in core banking functions.[28] The OCC is guided by specific principles when it is deciding whether to approve a national bank application.[29] Once the OCC receives an application, the Comptroller investigates to

> examine into the condition of such association, ascertain especially the amount of money paid in on account of its capital, the name and place of residence of each of its directors, and the amount of the capital stock of which each is the owner in good faith, and generally whether such association has complied with all the provisions . . . required to entitle it to engage in the business of banking.[30]

If, once the investigation is complete, the Comptroller finds that the applicant is "lawfully entitled to commence the business of banking," the OCC issues a certification acknowledging that the applicant is legally allowed to engage in the business of banking.[31]

There is no uniform bank charter application at the state level, but almost every jurisdiction follows the model of submission, investigation, decision, and ability to appeal.

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[28] 12 U.S.C. § 1 *et seq* (2019). Core banking functions include making loans, "paying checks" (which is interpreted as money transmission), and accepting deposits. 12 C.F.R. § 5.20(b) (2019).
[29] 12 C.F.R. § 5.20(f) (2019) (These principles are "(i) Maintaining a safe and sound banking system; (ii) Encouraging a national bank or Federal savings association to provide fair access to financial services by helping to meet the credit needs of its entire community; (iii) Ensuring compliance with laws and regulations; and (iv) Promoting fair treatment of customers including efficiency and better service.").
[30] 12 U.S.C. § 26 (2019).
[31] *Id.* § 27(a) (2019).

b. The benefits created by chartering. Bank chartering is a form of government-granted economic privilege. The bank chartering process, and government-granted economic privilege more generally, creates significant economic benefits for chartered institutions, giving them a marked advantage over nonchartered institutions. Because nonchartered institutions are limited in their ability to engage in core banking functions, they are not able to compete with banks on equal terms.[32] It has been suggested that one of the primary forces driving government-granted economic privilege is the desire to protect incumbent firms from emerging competition.[33] This understanding is commonly referred to as the "regulatory capture" theory of economic regulation, and it is based on the idea that when an industry benefits from regulation, this is not just an unintended consequence but may be the regulator's desired outcome. Regulatory capture theory proposes that "every industry or occupation that has enough political power to utilize the state will seek to control entry. In addition, the regulatory policy will often be fashioned so as to retard the growth of new firms."[34]

This theory is also aligned with what has sometimes been labeled the "producer-protection" theory of economic regulation. The producer-protection theory holds that "the actual effect of regulation is to increase or sustain the economic power of an industry."[35] Whether the industry-benefiting effect of regulation is an actively sought outcome or an unintended consequence, it exists. As regulatory barriers to entry become more prevalent and pervasive within a given industry, we are likely to see less competition within that industry.[36] In the case of

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[32] *See infra* Section I.B.
[33] George J. Stigler, *The Theory of Economic Regulation*, 2 BELL J. OF ECON. & MAN. SCI. 1, 3 (1971) ("A central thesis of this paper is that, as a rule, regulation is acquired by the industry and is designed and operated primarily for its benefit.").
[34] *Id.*
[35] William A. Jordan, *Producer Protection, Prior Market Structure and the Effects of Government Regulation*, 15 J.L. & ECON. 151, 153 (1972).
[36] *See* Stigler, *supra* note 33, at 3.

government-granted charters, the barriers to entry are much higher than would exist in a free market. You are either granted a charter or you are not able to operate as a bank. This reduced level of competition may allow chartered institutions more market power within the banking services industry than they would naturally have.

Historically, bank regulators have been known to be wary of "unbridled competition."[37] This wariness is reflected in the words of a former Comptroller of the Currency, who once said, "Sound and ethical competition is . . . a healthy thing but, of course, not to the extent of hazard to existing banking institutions."[38] This mentality on the part of regulators may be particularly problematic because the federal government and some state governments allow existing banks—would-be banks' direct competition—to comment on new banks' applications during the public comment period.[39] Some states even explicitly mandate that banks currently existing in the proposed bank's area of operations have an opportunity to weigh in and object to new bank applications.[40] This means that incumbent firms are part of the process of deciding whether a new competitor should or should not be allowed to enter the market, a power incumbents in most industries do not enjoy.[41] Imagine giving a town's incumbent pizza restaurants the opportunity to prevent a competitor from opening by objecting that their community does not "need" a new pizzeria.

There is significant historical evidence that regulators' discretion in granting charters, as well as FDIC insurance (discussed below),[42] has reduced the rate of entry into the banking

[37] David A. Alhadeff, *A Reconsideration of Restrictions on Bank Entry*, 76 Q. J. ECON. 246, 247 (1962).
[38] *Id.* at 248.
[39] 12 C.F.R. § 5.10 (2019).
[40] *See, e.g.*, ALA. CODE § 5-5A-5 (2019) (Alabama); MCA 31-1-204(1)(d) (2019) (Montana); N.J. Stat. § 17:9A-10 (2019) (New Jersey).
[41] David Zaring, *The Bank Charter and Its Would-Be Modernizers*, CSAS 22 (2018), https://administrativestate.gmu.edu/research/working-papers/.
[42] *See infra* Section I.A.2.

system.[43] For example, Sam Peltzman found evidence that regulatory entry restrictions instituted beginning in 1935 reduced the rate of entry such that, absent those restrictions, the rate of entry would have been between 50 percent and 100 percent higher than it actually was for the period 1935–1962.[44] Following Peltzman, Mark Ladenson and Kenneth Bombara found that Comptroller James Saxon's pro-entry policies dramatically increased entry during his tenure and that when the policies were abandoned the rate of entry into banking was reduced to well below what economic factors might dictate.[45]

This makes a certain amount of sense when one considers that state and federal regulators have traditionally been concerned that too many banks might jeopardize depositors, existing banking institutions, and the broader economy by destabilizing the banking industry.[46] Even if bank charters are not intended to keep out new entrants per se, and even if they may be justifiable on other grounds, including protecting the safety and soundness of the banking system, the net result is that the chartering process likely serves to reduce entry and protect incumbents.

2. FEDERAL DEPOSIT INSURANCE

One of the other primary ways the government restricts entry into the banking industry is through the issuance (or refusal) of FDIC insurance. The FDIC is an independent agency of the U.S. federal government that was created by statute.[47] It was formed in 1933 after a series of

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[43] *See, e.g.*, Sam Peltzman, *Entry in Commercial Banking*, 8 J. LAW & ECON. 11 (1965); Mark L. Ladenson & Kenneth J. Bombara, *Entry in Commercial Banking 1962–1978*, 16 J. MONEY CREDIT & BANKING 165 (1984); Daniel R. Fischel et al., *The Regulation of Banks and Bank Holding Companies*, 73 VA. L. REV. 301, 330–31 (1987); Prasad Krishnamurthy, *George Stigler on His Head: The Consequences of Restrictions on Competition in (Bank) Regulation*, 35 YALE J. ON REG. 823, 842 (2018); *but see* Burton A. Abrams & Russell F. Settle, *What Can Regulators Regulate? The Case of Bank Entry*, 24 J. MONEY CREDIT & BANKING 511 (1992).
[44] Peltzman, *supra* note 43, at 47.
[45] Ladenson & Bombara, *supra* note 43, at 173.
[46] Alhadeff, *supra* note 37, at 247–48; Krishnamurthy, *supra* note 43, at 848–60 (arguing that diminished competition could lead to enhanced stability).
[47] 12 U.S.C. § 1811 (2019).

bank failures in order to "restore public confidence in the nation's banking system."[48] The FDIC seeks to accomplish this goal by insuring "deposits at the nation's . . . banks and savings associations" and promoting "the safety and soundness of these institutions by identifying, monitoring [and] . . . addressing [the] risks to which they are exposed."[49] FDIC insurance is backed by the full faith and credit of the United States,[50] and it is a requirement for obtaining a bank charter in many states.[51]

Like bank charters, FDIC insurance can serve as a barrier to entry because granting insurance is a discretionary decision on the part of the FDIC,[52] and the agency can make determinations on the basis of ambiguous criteria such as the "needs of the community."[53] As with charters, there is historical evidence that this discretion has resulted in the restriction of entries by new banks.[54]

This restriction can be meaningful even if a bank obtains a charter from the OCC or a state regulator, because the FDIC must make an independent determination about whether to grant insurance.[55] For example, between 2005 and 2007 Wal-Mart applied for its own industrial

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[48] FDIC, A BRIEF HISTORY OF DEPOSIT INSURANCE IN THE UNITED STATES (Sept. 1998); FDIC, BASIC FDIC INSURANCE COVERAGE PERMANENTLY INCREASED TO $250,000 PER DEPOSITOR (July 21, 2010), https://www.fdic.gov/news/news/press/2010/pr10161.html.

[49] FDIC, BASIC FDIC INSURANCE COVERAGE PERMANENTLY INCREASED, *supra* note 48.

[50] 12 U.S.C. § 1828(a)(1)(B) (2019). It is worth noting that there is an argument that FDIC insurance is only implicitly backed by the full faith and credit of the United States government, because while Congress has required the FDIC to adopt language saying deposits are supported by the government, it has not passed a law explicitly establishing that support. *See* Alex J. Pollock, *Deposits Guaranteed up to $250,000—Maybe*, WALL ST. J. (May 28, 2013), https://www.wsj.com/articles/SB10001424127887323744604578472770934666526.

[51] *See, e.g.*, AL. CODE § 5-5A-12 (2019) (Alabama); R.I. GEN. LAWS § 19-4-10 (2019) (Rhode Island); FLA. STAT. § 658.38 (2019) (Florida). These are just a few of the states that require chartered institutions to obtain federal deposit insurance.

[52] Jelena McWilliams, *We Can Do Better on De Novos*, AM. BANKER, Dec. 6, 2018, https://www.americanbanker.com/opinion/fdic-chairman-jelena-mcwilliams-we-can-do-better-on-de-novos ("[The decision whether to grant insurance] gives the FDIC a significant gatekeeper role for firms that want to enter the banking system.").

[53] 12 U.S.C. § 1816(6) (2019).

[54] Peltzman, *supra* note 43.

[55] 12 U.S.C. § 1815 (2019).

loan company charter,[56] but it ultimately withdrew its application because it was not able to obtain FDIC insurance owing to fierce opposition from the banking community.[57] In addition, since 1997 the FDIC has failed to make a determination about whether to grant insurance to at least fourteen banks that received preliminary charters from the OCC.[58]

The FDIC's use of discretion has in fact recently drawn criticism for causing just such a slow-down in the entry of new banks. Former acting comptroller of the currency Keith Noreika has recently criticized the FDIC for taking too long to approve insurance applications after the OCC or state regulator has approved the charter, or simply not making a determination at all.[59] The FDIC responded by pointing out that chartering agencies have different incentives from the FDIC as protector of the deposit insurance fund.[60]

FDIC insurance is not only important in its own right but also serves as a prerequisite for other important government-granted advantages available to banks. For example, a state-charted bank is required to be an FDIC-insured depository institution before it can export the laws of its home state governing interest.[61] This is a significant advantage banks enjoy over nonbank lenders, because it allows them to offer credit nationwide under one consistent set of rules.[62]

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[56] An industrial loan company charter is a type of state-bank charter that is available to commercial firms that would otherwise be prevented from obtaining a bank charter. This charter confers many of the same powers as a traditional bank charter but also imposes significant limitations. It is worth noting that the historical separation of commerce and banking effectively excludes numerous commercial firms from fully competing in the market. *See generally* Bernard Shull, *The Separation of Banking and Commerce in the United States: An Examination of Principle Issues*, FINANCIAL MARKETS, INSTITUTIONS & INSTRUMENTS (1999).

[57] Eric Dash, *Wal-Mart Abandons Bank Plans*, N.Y. TIMES, Mar. 17, 2007, https://www.nytimes.com/2007/03/17/business/17bank.html.

[58] Keith Noreika, *Streamline Application Process to Spur New Banks: OCC's Noreika*, AM. BANKER, Oct. 30, 2017, https://www.americanbanker.com/opinion/streamline-application-process-to-spur-new-banks-occs-noreika.

[59] *Id.*

[60] Rob Tricchinelli, *OCC's Noreika Knocks FDIC Pace on New Bank Charters* (Aug. 4, 2017).

[61] *See* 12 U.S.C. § 1831d(a) (2019) (granting FDIC-insured depository institutions the right to lend nationwide on the basis of their home state's laws governing interest).

[62] *See infra* Section I.B.1.

B. Government-Granted Advantages over Nonbank Competitors

The government-imposed barriers to entry into banking would not provide much power if nonbanks could provide comparable services and compete with banks on effectively equal terms. However, this is not the case. Federal and state laws grant banks significant advantages over nonbanks in the core business lines of lending and money transmission, as well as in raising money.[63] These advantages artificially elevate banks over their nonbank competitors and may give them more power than they would likely have in a free, or even a consistently regulated, market. This section will discuss some of the advantages banks enjoy over nonbanks as a result of law and regulation.[64]

1. LENDING

Lending is a core function of banking[65] and a source of significant revenue and profit for banks.[66] To help banks facilitate the provision of credit, federal law has given banks certain powers that help them serve a national market and fund loans—particularly the ability to lend nationwide on the basis of their national or state charters and under their home state's laws governing interest. Nonbank lenders do not enjoy the same powers, which places them at a

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[63] *See* 12 C.F.R. § 5.20(e) (2019) (listing lending, receiving deposits, and paying checks as three "core banking functions"). "Paying checks" has come to include other forms of money transmission. For example, the OCC has argued that "issuing debit cards or engaging in other means of facilitating payments electronically are the modern equivalent of paying checks." OFFICE OF THE COMPTROLLER OF THE CURRENCY, EXPLORING SPECIAL PURPOSE BANK CHARTERS FOR FINTECH COMPANIES 4 (2016), https://www.occ.gov/topics/responsible-innovation/comments/special-purpose-national-bank-charters-for-fintech.pdf.

[64] An argument can be made that the burden of regulation faced by banks is greater than that faced by their nonbank competitors and therefore serves as a disadvantage. An assessment of whether this is true is beyond the scope of this paper. However, we note that, to the extent that the additional regulatory burden is in response to unique powers or privileges that banks enjoy, such as FDIC insurance, the regulation of nonbanks is not directly comparable.

[65] *See, e.g.*, 12 C.F.R. § 5.20(e)(1) (2019) (listing lending, receiving deposits, and "paying checks," which is interpreted as money transmission, to be three core banking functions).

[66] Adam Shell, *Bank of America, Boosted by Consumer Loan Business, Tops Profit Forecast*, USA TODAY (Jan. 17, 2018), https://www.usatoday.com/story/money/2018/01/17/bank-america-boosted-consumer-loan-business-tops-profit-forecast/1039374001/.

competitive disadvantage. This insulates banks and gives them significantly more market power than they would have if they faced a market that was less distorted by government intervention.

The maximum amount a lender can charge a borrower for a loan has long been a subject of government regulation.[67] In the United States, this regulation has traditionally been done at the state level.[68] However, in the 1860s the federal government established a national banking system to help support the Union's efforts in the Civil War.[69] The national banking system was meant to displace the traditional state-chartered banking system.[70] To this end, Congress took several steps to make sure that nationally charted banks could compete on advantageous terms with their state-chartered brethren,[71] or at least not be disadvantaged by state regulation.[72]

One way Congress sought to protect national banks was by relieving them of the requirement of obtaining a charter or license from every state in which they wanted to do business. National banks are empowered by federal law to lend, and states cannot burden that power.[73] Another way Congress sought to protect national banks was by allowing them to charge either the maximum rate allowed by law in the bank's home state or the maximum allowed by the

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[67] Thomas W. Miller Jr. & Harold A. Black, *Examining Arguments Made by Interest Rate Cap Advocates*, *in* REFRAMING FINANCIAL REGULATION: ENHANCING STABILITY AND PROTECTING CONSUMERS 342, 343 (Hester Peirce & Benjamin Klutsey eds., 2016) ("Interest rate caps, in the form of usury rate laws, likely represent the longest, and most repeated, government intervention in financial markets."). *See also* Efraim Benmelech & Tobias J. Moskowitz, *The Political Economy of Financial Regulation: Evidence from U.S. State Usury Laws in the 19th Century*, 65 J. FIN. 1029, 1036 (2010).
[68] Benmelech & Moskowitz, *supra* note 67, at 1036.
[69] Kirby M. Smith, *Banking on Preemption: Allowing National Bank Act Preemption for Third-Party Sales*, 83 U. CHI. L. REV. 1631, 1633–34 (2016).
[70] CONG. GLOBE, 38th Cong., 1st Sess. 1256 (1864) (statement of Rep. Samuel Hooper) (stating that the purpose of the National Bank Act was to "render the law so perfect that the State banks may be induced to organize under it, in preference to continuing under their State charters"). *See also* Smith, *supra* note 69, at 1633–34.
[71] Smith, *supra* note 69, at 1634–35. *See also* Tiffany v. Nat'l Bank of Missouri, 85 U.S. (18 Wall.) 409, 413 (1873) ("National banks have been National favorites. . . . [M]uch has been done [by Congress] to insure their [national banks'] taking the place of State banks.").
[72] *Tiffany*, 85 U.S. at 413.
[73] McCulloch v. Maryland, 17 U.S. 316, 436 (1819).

host state for any state-licensed or chartered lender.[74] Subsequent Supreme Court cases have interpreted this power to allow nationally chartered banks to charge the rate of interest allowed by the bank's home state rather than by the borrower's home state in cases where the bank extends credit to borrowers in another state.[75] Banks are also able to use the definition of what constitutes interest found in the law of their home state rather than the law of the borrower's state.[76]

In the high-interest-rate environment of the 1970s, state-chartered banks found themselves at a disadvantage compared to their nationally chartered peers because they could not export their home state's interest rates into interstate commerce. Congress, in order to provide competitive regulatory parity,[77] passed Section 521 of the Depository Institutions Deregulation and Monetary Control Act of 1980 (Monetary Control Act),[78] which granted FDIC-insured state-chartered depository banks comparable powers to export the laws of their home state governing both the maximum rate of interest that can be charged and the definition of interest.[79] State banks also enjoy the same "most-favored lender" status enjoyed by nationally chartered banks.[80] Likewise, state-chartered banks are generally exempt from the requirement to obtain a license to lend in other states.[81]

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[74] 12 U.S.C. § 85 (2012); 12 C.F.R. § 7.4001(b) (2001).
[75] Marquette Nat'l Bank of Minneapolis v. First of Omaha Serv. Corp., 439 U.S. 299 (1978) (allowing a nationally chartered bank to extend a credit card to a borrower under the terms of the law of the bank's home state even though the terms were usurious under the law of the borrower's state).
[76] Smiley v. Citibank (S.D.), N.A., 517 U.S. 735, 743–46 (1996).
[77] Greenwood Tr. Co. v. Mass., 971 F.2d 818, 826 (1st Cir. 1992).
[78] Depository Deregulation and Monetary Control Act of 1980, Pub. L. No. 96-221, § 521, 94 Stat. 132, 164–65 (1980) (codified as amended at 12 U.S.C. § 1831d (2012)).
[79] *See, e.g.*, *Greenwood*, 971 F.2d at 826; General Counsel's Opinion No. 10 on Interest Charges Under Section 27 of the Federal Deposit Insurance Act, 63 Fed. Reg. 19,258, 19,259 (Apr. 17, 1998).
[80] "Most-favored lender" status allows a bank to charge the rate of interest authorized by either the law of the bank's home state or the law of the borrower's state, whichever is higher. *See* General Counsel's Opinion No. 10, 63 Fed. Reg. at 19,259.
[81] John L. Douglas, *"New Wine into Old Bottles": Fintech Meets the Bank Regulatory World*, 20 N.C. BANKING INST. 17, 34 (2016).

By contrast, nonbank lenders are generally subject to state-by-state licensing requirements and regulation of what amount of interest they can charge and what counts as interest.[82] The laws are often, to borrow a description used by Elizabeth Schiltz, "idiosyncratic," and lack consistent definitions or requirements.[83] Additionally, numerous states have relatively low interest rate ceilings, which, while not binding on out-of-state banks, are binding on nonbank lenders.[84]

This state-by-state regulation has placed nonbank lenders at a competitive disadvantage relative to their bank peers because of the costs involved in obtaining licenses and the inability to offer a consistent product nationwide. Nonbanks are required to obtain licenses from every state they wish to do business in, which is expensive and time consuming.[85] Additionally, firms must, as Kevin Tu points out in the context of money transmission, undertake considerable "search costs" to identify and monitor the requirements of state law.[86]

While many nonbanks have sought to address this problem by partnering with banks,[87] this does not eliminate banks' advantages. First, the nonbank must generally compensate the partner bank,[88] which means the nonbank must pay a bank to access government-granted rights that the bank inherently enjoys.

Second, the bank-partnership model is currently under attack from regulators and litigants. Some argue that in these situations the nonbank, rather than its bank partner, is the "true

[82] *Id.* at 34; U.S. DEP'T OF THE TREASURY, OPPORTUNITIES AND CHALLENGES IN ONLINE MARKETPLACE LENDING 5 (2016) [hereinafter TREASURY REPORT], https://www.treasury.gov/connect/blog/Documents/Opportunities_and_Challenges_in_Online_Marketplace_Lending_white_paper.pdf [https://perma.cc/Y7UH-GPGR].
[83] Elizabeth R. Schiltz, *The Amazing, Elastic, Ever-Expanding Exportation Doctrine and Its Effect on Predatory Lending Regulation*, 88 MINN. L. REV. 518, 525 (2004).
[84] For example, New York's maximum rate of interest is 16 percent per annum. N.Y. C.L.S. Bank § 14-a (2019).
[85] Brian Knight, *Federalism and Federalization on the Fintech Frontier*, 20 VAND. J. ENT. & TECH. L. 129, 144–45, 188–191 (2017).
[86] Kevin V. Tu, *Regulating the New Cashless World*, 65 ALA. L. REV. 77, 112 (2013); Knight, *supra* note 85, at 186.
[87] Knight, *supra* note 85,at 145.
[88] TREASURY REPORT, *supra* note 82, at 8.

lender" and therefore should not be able to take advantage of the powers granted to banks by federal and state laws.[89] Another argument, boosted by the recent *Madden v. Midland Funding, LLC* case,[90] is that even if a loan is made by a bank, once the bank sells the loan to a nonbank, the loan is no longer treated as a bank loan for the purposes of determining which state's usury law applies, which means that the borrower's state law will control.[91]

There is no compelling consumer-protection reason why banks should enjoy these advantages while nonbanks do not. Nonbank lenders offer comparable products to those offered by banks and are subject to the same federal consumer protection laws.[92] They are also subject to regulation at the federal level by, inter alia, the Bureau of Consumer Financial Protection, the Federal Trade Commission, and the Department of Justice.[93] The advantages banks enjoy when competing on a national level are not justified and could in fact harm consumers by denying them access to a more competitive[94] and potentially more inclusive and less discriminatory[95] credit market.

Ultimately, banks' ability to lend nationwide on the basis of their home state law is a significant advantage not afforded to their nonbank competitors. This advantage helps insulate banks from the competitive pressure they would otherwise face, potentially increasing banks' market power beyond what it would be in a less distorted market.

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[89] Knight, *supra* note 85, at 148–52.
[90] 786 F.3d 246 (2nd Cir. 2015).
[91] Knight, *supra* note 85, at 146–48.
[92] TREASURY REPORT, *supra* note 82, at 10; Knight, *supra* note 85, at 189–90 (discussing in more detail the application of federal consumer protection laws to banks).
[93] TREASURY REPORT, *supra* note 82, at 38–39 (listing federal laws nonbanks are subject to and the agencies that enforce them).
[94] Knight, *supra* note 85, at 185–88.
[95] *See, e.g.*, Robert P. Bartlett et al., *Consumer Lending Discrimination in the FinTech Era* (UC Berkeley Public Law Research Paper, Dec. 7, 2017), https://ssrn.com/abstract=3063448 (finding that fintech lenders discriminated less than traditional lenders in the provision of mortgage credit).

2. MONEY TRANSMISSION

Banks also enjoy significant government-granted advantages in the area of money transmission. National banks are authorized under the National Bank Act of 1863 to engage in money transmission.[96] State-chartered banks are frequently permitted to engage in money transmission as part of the powers granted by their bank charter.[97] State money transmission licensing regimes also frequently exempt banks from the requirement to obtain a license.[98]

Conversely, nonbank money transmitters are generally subject to a state-by-state licensing regime that is both broad and inconsistent.[99] As in the case of lending,[100] this regime can be costly, in terms both of the expense of obtaining and maintaining licenses[101] and of the search costs imposed on firms, which must constantly monitor developments in state law to ensure compliance.[102] These costs and impediments place nonbank money transmitters at a disadvantage compared to their bank counterparts.

Congress has called for harmonization of state money transmission law, including licensing requirements to help protect the payments system,[103] and the states have undertaken an effort to streamline supervision of money transmitters.[104] States have also recently taken steps to make it easier for nonbanks to apply for multiple state licenses[105] and some states have agreed to

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[96] *See* 12 U.S.C. § 24 (Seventh) (2008); 12 C.F.R. § 5.20(e) (2017).
[97] *See, e.g.*, TENN. CODE ANN. § 45-2-605 (2019); N.C. GEN. STAT. § 53C-5-1(a)(1) (2017); GA. CODE ANN. § 7-1-280(6) (1986); IOWA CODE § 524.820 (2017).
[98] Tu, *supra* note 86, at 89. *See also, e.g.*, VA. CODE ANN. § 6.2-1902 (2013); TENN. CODE ANN. § 45-7-204 (2019).
[99] Tu, *supra* note 86, at 87–89.
[100] *See supra* Section I.B.1.
[101] Ashley Grimes, *Money Transmitter Licensing*, GRIMES L. PLLC, http://www.grimeslawaz.com/money-transmitter-licensing/#_ftn4 (estimating the cost of becoming a licensed money transmitter in all 53 states and territories as approximately $176,226 and the yearly expenses as $136,855).
[102] Tu, *supra* note 86, at 112; Knight, *supra* note 85, at 186.
[103] Riegle Community Development and Regulatory Improvement Act of 1994, Pub. L. No. 103-325, § 407(a)(1), 108 Stat. 2160, 2246–48 (1994) (codified as amended at 31 U.S.C. § 5311 (2012)).
[104] Knight, *supra* note 85, at 157–58.
[105] Conference of State Bank Supervisors, *Vision 2020 for Fintech and Non-bank Regulation* (June 7, 2018), https://www.csbs.org/vision2020.

standardize some elements of the licensing process.[106] However, to date, state laws contain significant substantive differences, and acquiring multiple licenses remains costly. As in the case of lending, regulatory costs disadvantage nonbank money transmitters, potentially granting banks more market power than they would have under a more evenhanded regulatory regime.

3. FDIC INSURANCE

As mentioned above,[107] the FDIC insures certain bank deposits at member banks. The FDIC pays for its insurance by collecting assessment revenue from each of its insured institutions calculated using a risk-based assessment system established by the FDIC's Board of Directors.[108] The risk-based assessment system differs depending on whether the insured firm is a small or large bank. Large banks are institutions with more than $10 billion in assets, whereas small banks are institutions with less than $10 billion in assets.[109] Large banks are assigned an individual rate on the basis of a scorecard of various risk factors.[110] Small banks are placed into one of four risk categories and are assigned a rate on the basis of their placement in this risk category.[111]

While banks do pay a specified amount determined by this risk-based assessment system, FDIC insurance may still act as a subsidy to covered institutions. Research suggests that, absent

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[106] Conference of State Bank Supervisors, *State Regulators Take First Step to Standardize Licensing Practices for Fintech Payments* (Feb. 6, 2018), https://www.csbs.org/state-regulators-take-first-step-standardize-licensing-practices-fintech-payments.
[107] *See supra* Section I.A.2.
[108] 12 U.S.C. § 1817(b)(1)(A) (2019).
[109] 12 C.F.R. § 327.8(e)–(f) (2019).
[110] This scorecard evaluates banks' weighted average capital adequacy, asset quality, management, earnings, and liquidity or CAMELS rating, their ability to withstand asset-related stress, their ability to withstand funding-related stress, and the severity of the potential loss that the FDIC would face if the bank failed. *See* 12 C.F.R. § 327.9(b).
[111] 12 C.F.R. § 327.9(a) (2019).

the costs associated with regulatory control, FDIC insurance is likely underpriced and banks pay less for this insurance than they would on the open market.[112]

FDIC insurance also serves as a subsidy because it is backed by the full faith and credit of the United States. As former vice chair of the FDIC Thomas M. Hoenig explained, "The government safety net of deposit insurance, central bank loans, and ultimately taxpayer support provides a multibillion-dollar subsidy to firms that engage in both commercial and investment banking. This government backstop means that they have cheaper access to funding and face less discipline from the market."[113]

Risk substantially affects the perceived and actual benefit of insurance. In the case of bank deposits, the bank in effect "borrows" money from the depositor. The potential for nonpayment of the loan in the event of a bank failure influences the rate at which banks are able to borrow money. When the risk of nonpayment is minimized, the cost associated with loaning money is also minimized. Because FDIC insurance is backed by the full faith and credit of the United States, there is little or no risk of nonpayment in the event of an emergency. This allows banks to borrow money at a much lower interest rate than their competitors can, which gives them a marked advantage. This government-granted advantage can be viewed as a subsidy given to insured institutions even if it is not a direct subsidy in the form of explicit underpricing. In addition, because depositors are insured against loss in the case of an emergency, they may have

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[112] *See* Kathryn Judge, *Three Discount Windows*, 99 CORNELL L. REV. 795, 830 (2014) (citing Arthur E. Wilmarth, Jr., *The Transformation of the U.S. Financial Services Industry, 1975–2000: Competition, Consolidation, and Increased Risks*, 2002 U. ILL. L. REV. 215, 266–67 (2002) (describing why most banks pay too little for deposit insurance)). *See also* George G. Pennacchi, *A Reexamination of the Over- (or Under-) Pricing of Deposit Insurance*, 19 J. MONEY, CREDIT & BANKING 340, 354 (1987) ("[I]f the FDIC is viewed as exercising no effective regulatory control over banks, then its deposit insurance program can be thought of as 'unlimited-term' insurance. Estimates of fair premia for this case indicate that for every bank in our sample, the FDIC would currently be undercharging each for the provision of deposit insurance.").

[113] THOMAS M. HOENIG, ENDING THE GOVERNMENT SUBSIDY, https://www.fdic.gov/about/learn/board/hoenig/govsubsidy.pdf, last accessed August 20, 2019.

less incentive to monitor banks in order to assess their risk. This could allow banks to engage in more aggressive lending with a diminished expectation that their behavior will be factored into the terms of future agreements. Kathryn Judge explains that “because a bank’s shareholders often benefit from a bank assuming excessive risk, deposit insurance can subsidize and incentivize banks’ risk taking.”[114] FDIC insurance serves as a privilege that allows banks to engage in behavior that would be riskier absent the insurance.

4. PAYMENTS SYSTEMS

Another way in which the government creates benefits for banks that are not enjoyed by their nonbank competitors is the creation and operation of government-run payments systems. Government-provided payments systems allow chartered institutions to transfer money with other chartered institutions. These systems include the Fedwire Funds Service, the FedACH, and the National Settlement Service.[115] All of these are provided and operated by the Federal Reserve (Fed).[116] The Fed began providing these services right after it was founded in 1913, and historically it did not require banks to provide an explicit payment for access to these services.[117] The Fed became more active in the provision of payments systems after Congress passed the Monetary Control Act.[118]

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[114] Judge, *supra* note 112, at 830.
[115] Federal Reserve, *Payment, Clearing and Settlement Systems in the United States*, RED BOOK 482 (2012), https://www.bis.org/cpmi/paysysinfo.htm.
[116] There are private alternatives to these systems. For example, the Clearing House Interbank Payments System (CHIPS) competes with FedWire. However, this system uses the Fed’s National Settlement Service to settle its transactions. *Payment Systems in the United States*, BANK FOR INTERNATIONAL SETTLEMENTS (2003).
[117] Federal Reserve, *Federal Reserve’s Key Policies for the Provision of Financial Services* (2016), https://www.federalreserve.gov/paymentsystems/pfs_about.htm.
[118] 94 Stat. 132 (1980).

The Monetary Control Act, among other things, required the Fed to charge banks a fee in order to try to recover the cost associated with government-provided payments systems.[119] This means that access to these payments systems may no longer be the explicit subsidy that it once was.[120] However, nonprice factors may still render the Fed's provision of payments services a subsidy to some banks. The Fed is charged with providing payments services to banks on an "equitable" basis[121] and with an eye toward ensuring access. This means that the Fed may offer services to banks that would not be able to access them in a private market, a fact the Fed explicitly acknowledges in its recent notice discussing its decision to provide real-time gross settlement payments services.[122] Further, the Fed's offer of payments services allows banks to avoid liquidity and credit risk that might exist with a private alternative.[123] The Fed will also support private payments systems; for example, the Clearing House's real-time system uses a joint account at a Federal Reserve bank.[124] This allows the Clearing House to avoid the risk of

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[119] 12 U.S.C. § 248a(c)(1) (2019).

[120] That being said, some have argued that the Fed still may not fully comply with cost-recovery provisions because it does not pay taxes or incur the costs of regulatory compliance. *See* George Selgin, *Re: Potential Federal Reserve Actions to Support Interbank Settlement of Faster Payments: Docket No. OP-1625*, CATO (Dec. 14, 2018), https://www.cato.org/publications/public-comments/re-potential-federal-reserve-actions-support-interbank-settlement ("The difficulty of achieving full compliance is especially acute with regard to 'imputed' costs the Fed is supposed to take into account, including taxes that it would have to pay were it also a profit-making private-sector provider. Among other problems, the Fed is not required to take account of many of the regulatory compliance costs that private-sector payments service providers incur. That the Fed's internal cost-accounting system has not been reviewed by an external auditor in several decades supplies that much more reason for fearing that it might offer fast payments services for less than their true cost."); *see also* GOVERNMENT ACCOUNTABILITY OFFICE, FEDERAL RESERVE'S COMPETITION WITH OTHER PROVIDERS BENEFITS CUSTOMERS, BUT ADDITIONAL REVIEWS COULD INCREASE ASSURANCE OF COST ACCURACY 16–24 (Aug. 2016) (discussing whether the Fed fully incorporates regulatory costs borne by private sector competitors into is calculations).

[121] Federal Reserve Actions to Support Interbank Settlement of Faster Payments, 84 Fed. Reg. 39,297, 39,303 (Aug. 9, 2019).

[122] *Id.* at 39,300.

[123] *Id.* at 39,298, *citing* COMMITTEE ON PAYMENT AND SETTLEMENT SYSTEMS, BANK FOR INTERNATIONAL SETTLEMENTS, THE ROLE OF CENTRAL BANK MONEY IN PAYMENT SYSTEMS (Aug. 2003), https://www.bis.org/cpmi/publ/d55.pdf.

[124] 84 Fed. Reg. at 39,321.

loss of funds that might occur if it used a commercial bank to hold the joint account by "reproducing, as closely as possible, the risk-free nature of settlement in central bank money."[125]

In addition, these services are only made available to chartered banks and are not made available to nonbank institutions.[126] Nonbank institutions have to go through banks if they want access to these government-created systems. Access to these services is very valuable: businesses often need to transfer funds with other institutions, both banks and nonbanks. This means that government-provided payments systems available only to chartered banking institutions may function as an implicit subsidy because they artificially restrict access in a way that guarantees additional customers and interactions for the banks. Restricting access exclusively to banks ensures that nonbank money lenders are forced to use banks as third-party intermediaries to gain access to these government-provided systems. Not only does this give banks access to customers that they might not otherwise have had, it also creates an extra step and cost for nonbank institutions that disadvantages them as they compete with chartered banking institutions. Both the advantage given to banks and the disadvantage imposed on nonbank institutions empower banks beyond what would occur in a system without this government-granted privilege.

C. Explicit Bailouts and Implicit Subsidies

The government provides banks with various explicit and implicit guarantees. These guarantees can provide significant value to banks, protecting them from insolvency and allowing them to attract investment on more favorable terms than they would in a pure market environment.

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[125] 84 Fed. Reg. at 39,322.
[126] *See* Selgin, *supra* note 120. However, nonbanks can access these payments systems if they are acting as an agent of a bank. 83 Fed. Reg. 57,360 (Nov. 15, 2018).

While many of the benefits government provides apply to all banks, some benefits are reserved for only a select few. As discussed below, while the federal government has allowed a number of banks to fail, it has also stepped in to save some banks from likely lethal market discipline via explicit government support. However, the impact of those decisions extends beyond the mere one-time salvation of banks. In the case of banks deemed "too big to fail" (TBTF), the government likely has conditioned the market to expect government rescue of larger firms in the event the banks require it—in spite of legislation seeking to prevent future bailouts.[127] This market conditioning has granted the banks expected to receive future government rescue certain advantages over their rivals. These include advantages in funding and investment that allow them to raise capital more cheaply because investors expect that in the event of a crisis, an investment in a bank deemed too big to fail will be protected by government intervention, while an investment in a non-TBTF bank risks being wiped out.

1. BAILOUTS

While many banks fail and are liquidated,[128] the government has intervened in the past to directly prop up distressed banks, preventing them from failing. Rescue efforts are frequently justified as necessary to protect the broader financial system or stave off economic calamity.[129] An additional justification is often expressed: that protecting banks helps protect the broader

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[127] *See* Aaron Klein, *A Primer on Dodd-Frank's Orderly Liquidation Authority*, BROOKINGS (June 5, 2017), https://www.brookings.edu/blog/up-front/2017/06/05/a-primer-on-dodd-franks-orderly-liquidation-authority/.
[128] FDIC, FAILED BANK LIST, https://www.fdic.gov/bank/individual/failed/banklist.html (last visited Aug. 17, 2019).
[129] For example, the bailout of Continental Illinois was driven, at least in part, by a concern on the part of regulators that if it were allowed to fail other, larger institutions might also fail. FDIC, AN EXAMINATION OF THE BANKING CRISES OF THE 1980S AND EARLY 1990S 251 (1997), https://www.fdic.gov/bank/historical/history/235_258.pdf. Likewise, regulators felt that allowing Citi to fail would have risked destabilization of the broader financial system. SPECIAL INSPECTOR GENERAL FOR THE TROUBLED ASSET RELIEF PROGRAM, EXTRAORDINARY FINANCIAL ASSISTANCE PROVIDED TO CITIGROUP, INC. 15 (Jan. 13, 2011) [hereinafter EXTRAORDINARY FINANCIAL ASSISTANCE], https://www.sigtarp.gov/Audit%20Reports/Extraordinary%20Financial%20Assistance%20Provided%20to%20Citigroup,%20Inc.pdf.

economy by allowing banks to provide credit and payments services in times of need.[130] However, bailouts also have the effect of augmenting the market power of the bank or banks that receive assistance, because—to be blunt—you can't exercise market power if you no longer exist. For this reason, a bailout not only preserves the bank but also preserves, absent explicit restrictions, the ability of the bank's leadership to exercise control over the bank's assets. A bailout also helps preserve the bank's position relative to its competition, since preventing a firm's failure denies the competition the full opportunity it would otherwise have had to gain market share and power at the failing firm's expense.

Bank holding companies can be sprawling tangles of different types of financial firms, and the government had policies to help most if not all of them.[131] We focus on the largest programs targeting the depository banks themselves. Congress and the relevant regulators undertook multiple programs with different objectives, some of which aimed to benefit all banks while others focused on specific types of banks, and in a few cases on the direct rescue of specific systemically significant banks. This section is not an exhaustive list of all the actions taken by the government during the 2008 financial crisis that have preserved bank market power. Rather, it is meant to illustrate the scope and directness with which the government intervened in the market during the crisis.

The financial crisis featured significant direct federal support for the banking sector, as well as for other types of financial firms. This support took a host of forms, ranging from expanding deposit insurance to granting loan guarantees to providing direct cash injections to

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[130] A representative of the New York Federal Reserve cited this as one of the justifications for the Capital Purchase Program, discussed below. EXTRAORDINARY FINANCIAL ASSISTANCE, *supra* note 129, at 13.
[131] *See, e.g.*, GOVERNMENT ACCOUNTABILITY OFFICE, *supra* note 24, at 16 (noting that bank holding companies were indirect beneficiaries of government programs that supported other market participants because of the interconnected nature of the market).

specific banks by the government to prevent their failure. These programs provided bank holding companies with several benefits: "Access to funding in quantities and/or at prices that were generally not available in the markets; Access to funding at longer maturities; Stabilizing deposit funding; Funding support for a broad range of collateral types."[132]

Some programs were meant to support banking as a whole while others targeted specific banks on the basis of size, interconnectedness, systemic importance, and, potentially, political clout.[133] In some cases the programs were designed to reduce the risk that the recipients of the support would suffer market stigma,[134] which is another way of saying the programs were designed to conceal important information from the markets and protect firms that would otherwise be punished. While this may arguably be justified on the grounds that a firm's failing may cause panic or exacerbate a financial crisis, the unavoidable side effect is that an institution's market power is protected by government policy.

2. FEDERAL RESERVE—LENDER OF LAST RESORT

The Federal Reserve (Fed) is designed to serve as a "lender of last resort" for depository institutions to provide needed liquidity when otherwise solvent banks are unable to access liquidity in the private market.[135] The traditional method the Fed uses is the discount window,

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[132] *Id.* at 19–20.
[133] *See generally* JAMES FREEMAN & VERN MCKINLEY, BORROWED TIME: TWO CENTURIES OF BOOMS, BUSTS, AND BAILOUTS AT CITI 274–306 (2018) (discussing the links between Citigroup and financial regulators). *See also* Benjamin M. Blau et al., *Corporate Lobbying, Political Connections, and the Bailout of Banks*, 37 J. BANKING & FIN. 3007, 3016–17 (2013); Ran Duchin & Denis Sosyura, *The Politics of Government Investment*, 106 J. FIN. ECON. 24, 26 (2012); Nikolaos I. Papanikolaou, *To Be Bailed Out or to Be Left to Fail? A Dynamic Competing Risks Hazard Analysis*, 34 J. FIN. STABILITY 61, 70 (2018).
[134] *See, e.g.*, OLIVER ARMANTIER ET AL., STIGMA IN FINANCIAL MARKETS: EVIDENCE FROM LIQUIDITY AUCTIONS AND DISCOUNT WINDOW BORROWING DURING THE CRISIS, STAFF REPORT, NO. 483, FEDERAL RESERVE BANK OF NEW YORK, at 9 (2011); Michael J. Fleming, *Federal Reserve Liquidity Provision During the Financial Crisis of 2007–2009*, 2012 ANN. REV. FIN. ECON. 161, 163, 170.
[135] ARMANTIER ET AL., *supra* note 134, at 5.

whereby the Fed makes short-term, collateralized loans to banks.[136] Originally, the Fed would lend at below-market rates but, to avoid subsidizing banks, would require banks to prove they could not access private credit and legitimately needed the money.[137] This arrangement gave rise to the concern that discount window usage would "stigmatize" the bank because it revealed a need for short term credit and an inability to get it in the market, so the Fed changed its policy in 2003.[138] After 2003, discount window loans were made "no questions asked" but at a rate of interest intended to exceed the current market rate, and the names of the banks using the discount window were not disclosed.[139] However, banks were still hesitant to use the discount window for fear of being stigmatized.[140]

During the financial crisis, the Fed wanted to address the mounting liquidity crisis in the banking sector. To make borrowing from the discount window more attractive, it reduced the interest rate it charged banks and extended the term of the loans it offered.[141] In an effort to overcome the stigmatizing nature of discount window borrowing, it also announced that taking advantage of the window would be seen as a "sign of strength."[142] However, these changes did not appear to significantly increase the amount of discount window borrowing that occurred.[143]

While stigma is one likely reason for the limited lending, some banks may have had a cheaper option than the discount window in the form of Federal Home Loan Bank (FHLB)

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[136] *Id.*
[137] *Id.*; Fleming, *supra* note 134, at 163.
[138] ARMANTIER ET AL., *supra* note 134, at 6; Fleming, *supra* note 134, at 163, 170.
[139] ARMANTIER ET AL., *supra* note 134, at 8. However, it should be noted that the Dodd-Frank Wall Street Reform and Consumer Protection Act now requires the Fed to reveal discount window participants after a two-year delay. *See* Fleming, *supra* note 134, at 163.
[140] ARMANTIER ET AL., *supra* note 134, at 7.
[141] *Id.*; Fleming, *supra* note 134, at 166.
[142] ARMANTIER ET AL., *supra* note 134, at 7.
[143] *Id.*

advances.[144] The FHLB is a government-sponsored enterprise made up of 11 regional banks established to serve their member banks and credit unions by providing funds for home mortgages.[145] The FHLB funds its advances by accessing the credit markets.[146] While the FHLB's structure is superficially similar to that of the Fed, the FHLB is considered by some to be "more private, less publicly accountable, and less centralized than the Fed."[147] Therefore, while the FHLB was a major provider of credit to depository institutions during the early period of the financial crisis,[148] the argument that it represents government directly and intentionally protecting bank market power is arguably attenuated.

The Fed expanded its lending to banks in December 2007 with the creation of the Term Auction Facility (TAF).[149] The TAF had several features designed to reduce the stigmatization banks that used it might suffer, including a group auction structure whereby all banks bidding above the closing price would pay the closing price for funds, a limit on the amount of credit any one bank could obtain, and a delay on accessing the funds.[150] As Oliver Armantier, Eric Ghysels, Asani Sarkar, and Jeffrey Shrader point out, these attributes were designed to make the TAF look less like a rescue by the Fed and more like a competitive market operation.[151] The TAF, like the discount window, did not require the identification of the borrowing firms.[152] These differences were apparently valuable to banks, because they were willing to pay an estimated premium of at

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[144] ADAM B. ASHCRAFT ET AL., THE FEDERAL HOME LOAN BANK SYSTEM: THE LENDER OF NEXT-TO-LAST RESORT?, FEDERAL RESERVE BANK OF NEW YORK STAFF REPORT NO. 357, at 21 (Nov. 2008).
[145] *Id.* at 6.
[146] *Id.*
[147] Judge, *supra* note 112, at 826–27.
[148] As of November 2008, the FHLB was the largest lender to depository institutions specifically. ASHCRAFT ET AL., *supra* note 144, at 5.
[149] ARMANTIER ET AL., *supra* note 134, at 7.
[150] *Id.*
[151] *Id.* at 7–8.
[152] *Id.* at 8.

least 37 basis points (and much more after the failure of Lehman Brothers in 2008) to borrow from the TAF instead of the discount window.[153]

The TAF had approximately $493 billion outstanding at its peak, compared with only $111 billion for the discount window.[154] Cumulatively, the TAF extended almost $4 trillion in credit.[155] Banks were likely able to access credit at lower rates and on better terms through the TAF than they could have through the market at the time: the Government Accountability Office (GAO) estimated that banks paid between 22 and 39 basis points less in interest.[156] However, as the markets normalized, TAF borrowing declined significantly, indicating that the TAF, while a superior option during the most acute part of the financial crisis, was inferior to market alternatives under more normal conditions.[157]

The Fed's lending to banks is a clear case of government protecting banks. Serving as a lender of last (or at least latter) resort, the government prevents a borrowing bank from doing the next-worst thing to obtain needed liquidity, which might include forgoing profitable opportunities, taking a private loan at more onerous terms (if one is available), selling assets, restricting operations, being acquired, or failing. Protecting banks from these outcomes may arguably be justified, especially in a crisis, on the grounds that bank liquidity problems may threaten the broader economy—but when the government steps in to insulate banks from market forces, they emerge better positioned (and potentially more alive) than they would have been but for government intervention.

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[153] *Id.* at 20.
[154] GOVERNMENT ACCOUNTABILITY OFFICE, *supra* note 24, at 14. *See also* Fleming, *supra* note 134, at 164.
[155] James Felkerson, *$29,000,000,000,000: A Detailed Look at the Fed's Bailout by Funding Facility and Recipient* 32 (Levy Econ. Inst. of Bard College Working Paper No. 698, 2011).
[156] GOVERNMENT ACCOUNTABILITY OFFICE, *supra* note 24, at 22–23.
[157] Fleming, *supra* note 134, at 169.

Additionally, the decision to conceal the identities of banks accessing Federal Reserve liquidity facilities and to structure those facilities to avoid stigmatizing banks may also have insulated banks from market discipline, because *stigma* in this context simply means markets incorporating relevant information. For example, there is some evidence that visiting the discount window causes banks to experience an increase in borrowing costs and a decrease in stock prices.[158] The decision to avoid stigmatization may make sense from the perspective that allowing the market to identify firms in distress may harm the broader economy. However, it also benefits the specific firms avoiding stigmatization by protecting their reputations, their access to private credit, and their stock prices, granting them market power they might not have otherwise enjoyed.

3. FDIC

During the financial crisis, the scope of FDIC insurance was expanded and the FDIC became guarantor of certain nondeposit bank liabilities. These changes helped banks, especially those in distress, retain or attract deposits because the risk of loss was shifted to the FDIC for more depositors and for larger amounts of funds.

a. Expansion of deposit insurance. As discussed above,[159] deposit insurance is a valuable asset to banks; it can prevent runs and maintain stability. In response to the financial crisis, several changes were made to expand the amount of deposit insurance available per account and the types of accounts the FDIC insured. The coverage limit for traditional interest-bearing accounts

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[158] ARMANTIER ET AL., *supra* note 134, at 26; *but see* Celine Gauthier et al., *Emergency Liquidity Facilities, Signaling and Funding Costs* (Bank of Canada Staff Working Paper 2015-44, 2015) (arguing that TAF restrictions allowed banks to signal they were less desperate than discount window borrowers).
[159] *See supra* Section I.B.3.

was temporarily expanded from $100,000 to $250,000 in 2008 by the Emergency Economic Stabilization Act;[160] the expansion was made permanent following passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010.[161]

In late 2008, the FDIC also expanded the scope of coverage to include non-interest-bearing transaction accounts, without a coverage limit, through the Transaction Account Guarantee Program (TAGP).[162] TAGP was a voluntary program designed to reduce the risk of bank runs sparked by businesses pulling their money out of the non-interest-bearing (and noninsured) accounts they used to handle regular transactions (e.g., payroll).[163] TAGP was popular with the businesses whose bank accounts were now insured and with banks, including smaller banks that previously were at a disadvantage to big banks because the big banks were perceived to be safer.[164] At its peak TAGP covered more than $800 billion,[165] and it was extended twice by the FDIC before the Dodd-Frank Act mandated a temporary expansion of coverage to all non-interest-bearing bank accounts until the end of 2012.[166]

The expansion of deposit insurance provided significant support to banks because it, in conjunction with other government support, helped them retain and obtain deposits, a critical source of liquidity.[167] While large, TBTF institutions may not have paid higher interest during

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[160] Press Release, FDIC, Basic FDIC Insurance Coverage Permanently Increased to $250,000 per Depositor (July 21, 2010), https://www.fdic.gov/news/news/press/2010/pr10161.html.
[161] Pub. L. No. 111-203 (2019).
[162] FDIC, CRISIS AND RESPONSE: AN FDIC HISTORY, 2008–2013, at 51–52 (2017) (available at https://www.fdic.gov/bank/historical/crisis/).
[163] *Id.*
[164] Jed Horowitz, *Banks Urge Congress to Extend Crisis-Era Deposit Insurance*, REUTERS (July 30, 2012), https://www.reuters.com/article/us-fdic-tag-extension/banks-urge-congress-to-extend-crisis-era-deposit-insurance-idUSBRE86T02U20120730.
[165] FDIC, CRISIS AND RESPONSE, *supra* note 162, at 53.
[166] *Id.* at 52–53.
[167] Viral V. Acharya & Nada Mora, *A Crisis of Banks as Liquidity Providers*, 70 J. FIN. 1, 10–11 (2015) (discussing how the crisis did not produce an inflow of deposits until FDIC insurance expansion and other government supports were provided to banks); Judge, *supra* note 112, at 817–18.

the crisis,[168] there is evidence that banks in worse shape were able to attract deposits by offering higher interest rates,[169] and that the mix of deposits in less stable banks shifted, with insured deposits replacing uninsured deposits[170] or at least not being withdrawn at the same rate.[171] Therefore, the government support provided by expanded FDIC insurance likely allowed banks, especially those in poorer health, to remain in better shape than they would have without assistance. As with other actions taken during the crisis to stabilize the banking system, the expansion of deposit insurance may be justifiable on systemic grounds, or to protect depositors from losing their savings. But it also had the side effect of preserving bank market power that would otherwise have been lost owing to banks losing customers, forgoing profitable investment opportunities, and potentially failing.

b. Debt guarantees. In addition to insuring bank deposits, the FDIC became the guarantor of bank debt through the Debt Guarantee Program.[172] This was a voluntary program that allowed the FDIC to guarantee participating banks' newly issued senior unsecured debt for a fee, with some exceptions.[173] The program initially was supposed to run until June 2009, with the guarantee set to expire by June 2012, but the program and expiration were extended until October 2009 and December 2012, respectively.[174]

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[168] Acharya & Mora, *supra* note 167, at 18.
[169] *Id.*; Judge, *supra* note 112, at 817–18.
[170] Christopher Martin et al., *Deposit Inflows and Outflows in Failing Banks: The Role of Deposit Insurance* (Nat'l Bureau of Econ. Research, Working Paper No. 24589, May 2018) (examining a failing bank and finding that while there were significant outflows of uninsured deposits there were also significant inflows of insured deposits that partially offset the outflows).
[171] Rosalind L. Bennett et al., *Market Discipline by Bank Creditors During the 2008–2010 Crisis*, 20 J. FIN. STABILITY 51 (2015) (finding that the proportion of insured deposits generally increased at failed banks before a failure and increased for banks with CAMELS ratings of 4 or 5 during the crisis, while it decreased for banks with CAMELS ratings of 1 or 2).
[172] FDIC, *supra* note 162, at 44.
[173] *Id.*; GOVERNMENT ACCOUNTABILITY OFFICE, *supra* note 24, at 15.
[174] FDIC, *supra* note 162, at 44.

The purpose was to allow banks to roll over maturing debt or issue new debt at rates lower than those available in the market at the time. The GAO estimates that the cost of an FDIC guarantee for the bank debt was, on average, 278 basis points lower than the market price for comparable protection during the crisis, though it was higher than precrisis pricing.[175] The FDIC guaranteed approximately $346 billion at the Debt Guarantee Program's peak,[176] and 121 institutions issued debt under the program.[177] Citigroup was the largest issuer, with about $175 billion of debt issued, followed by General Electric Capital Corporation, Bank of America, and JPMorgan Chase.[178]

As with deposit insurance, providing a guarantee for bank debt, especially at below-market rates, may be justifiable to protect the stability of the banking system or bank customers. However, it also protects specific banks from market discipline by allowing them to avoid going to the market to roll over or issue new debt and pay the price the market would demand on the basis of their risk profile.

4. DEPARTMENT OF THE TREASURY

The severity of the 2008 financial crisis prompted Congress to authorize the Department of the Treasury to directly intervene by, inter alia, making direct investments into financial firms, including banks.[179]

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[175] *Id.*; GOVERNMENT ACCOUNTABILITY OFFICE, *supra* note 24, at 29.
[176] GOVERNMENT ACCOUNTABILITY OFFICE, *supra* note 24, at 15.
[177] FDIC, *supra* note 162, at 57.
[178] *Id.* at 50.
[179] 12 U.S.C. § 5211(a)(1) (2019).

a. Capital Purchase Program. The Capital Purchase Program (CPP) was an initiative launched by the Treasury under the Troubled Asset Relief Program (TARP) that allowed the Treasury to purchase assets "necessary to promote financial market stability."[180] This allowed the Treasury to purchase preferred shares and subordinated debt, taking a direct investment in depository institutions and their affiliates.[181] The first investment was made in October 2008 when the Treasury selected nine commercial, investment, and custody banks and informed them they would receive money "for the good of the country."[182] These capital injections included $25 billion investments in Citigroup, Wells Fargo, and JPMorgan Chase, and a $15 billion investment in Bank of America paired with a $10 billion investment in Merrill Lynch, which Bank of America was in the process of acquiring.[183] The recipients were selected because they were large and interconnected institutions that were seen as systemically important.[184] Some bank leaders felt that the government pressured the banks to accept the funds.[185] Part of the reason why the government pressured the banks to accept the funds as a group was to avoid the risk of stigmatizing weak institutions in the market by revealing which institutions needed government capital to survive.[186]

Subsequent CPP investments required the requesting firm to fill out an application and be evaluated by the Treasury on the basis of firm strength and viability.[187] The Treasury went on to

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[180] CONGRESSIONAL OVERSIGHT PANEL, MARCH OVERSIGHT REPORT: THE FINAL REPORT OF THE CONGRESSIONAL OVERSIGHT PANEL 22 (Mar. 16, 2011).
[181] GOVERNMENT ACCOUNTABILITY OFFICE, *supra* note 24, at 15.
[182] OFFICE OF THE SPECIAL INSPECTOR GENERAL FOR THE TROUBLED ASSET RELIEF PROGRAM, EMERGENCY CAPITAL INJECTIONS PROVIDED TO SUPPORT THE VIABILITY OF BANK OF AMERICA, OTHER MAJOR BANKS, AND THE U.S. FINANCIAL SYSTEM 17–18 (Sigtarp-10-0001, Oct. 5, 2009).
[183] *Id.* at 20.
[184] *Id.* at 17.
[185] *Id.* at 18.
[186] *Id.* at 18–19.
[187] *Id.* at 21.

invest in 707 institutions over the course of the program,[188] though it is unclear whether smaller institutions were as well served by the program as the larger banks, because larger banks have been able to exit the program more quickly.[189] At its peak, the Treasury had invested $205 billion through the CPP.[190] The GAO estimates that government investments made under the CPP were made at an 18–27 percent premium over market prices.[191] The Treasury justifies this by arguing that the point of the program was to bolster the banking system, not accurately price risk.[192] While the program may be defensible as a matter of policy, the issue remains that banks were able to access funds more cheaply than they would have otherwise, allowing them to maintain market power at a reduced cost thanks to government policy.

Because the Treasury did not invest in every bank equally, it is possible that TARP allowed some banks to improve their market power at the expense of both bank and nonbank rivals. First, to the extent the difference between life and death was getting investment from TARP, the banks that received it would be advantaged over those that did not. Ettore Croci, Gerard Hertig, and Eric Nowak find that TARP investment through the CPP made a significant difference in whether a bank would fail, controlling for other bank characteristics.[193]

Second, besides keeping receiving banks alive when comparable banks might have succumbed to market forces, TARP may have helped receiving banks improve their market share and market power by enabling them to perform better than their rivals.[194] TARP helped these

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188 GOVERNMENT ACCOUNTABILITY OFFICE, CAPITAL PURCHASE PROGRAM: REVENUES HAVE EXCEEDED INVESTMENTS, BUT CONCERNS ABOUT OUTSTANDING INVESTMENTS REMAIN 8 (GAO-12-301, Mar. 8, 2012).
189 CONGRESSIONAL OVERSIGHT PANEL, *supra* note 180, at 64.
190 GOVERNMENT ACCOUNTABILITY OFFICE, *supra* note 24, at 15.
191 *Id.* at 27.
192 CONGRESSIONAL OVERSIGHT PANEL, *supra* note 180, at 62.
193 Ettore Croci et al., *Decision-Making During the Credit Crisis: Did Treasury Let Commercial Banks Fail?*, 38 J. EMPIRICAL FIN. 476, 486–88 (2016).
194 Allen N. Berger & Raluca A. Roman, *Did TARP Banks Get Competitive Advantages?*, 50 J. FIN. & QUANT. ANALYSIS 1199, 1213–17 (2015).

banks by lowering the amount they needed to pay for deposits and other funding because they were perceived as safer, and in the case of banks that were able to repay TARP funds more quickly, TARP may also have allowed them to charge more for loans.[195]

Distressingly, there is also evidence that allocation of TARP funds may have been influenced by political connections and lobbying, rather than merely by objective economic considerations. For example, there is evidence that banks that were active in lobbying, were headquartered in the district of a member of Congress that sat on the House Financial Services Committee, or employed former government officials were more likely to receive TARP funding and to receive it faster than non-politically-connected banks, and they were less likely to be allowed to fail.[196]

b. Extraordinary aid to specific banks. While the programs described above were available to multiple banks, the Treasury also directly targeted two large banks that needed additional help. In November 2008, the Treasury, Fed, and FDIC announced a support plan for Citigroup including a direct $20 billion investment by the Treasury through the Targeted Investment Program (TIP) under TARP, as well as a loss-sharing agreement for approximately $300 billion worth of assets.[197] The arrangement was created in response to a fear that Citigroup was in danger of facing a run and potentially collapsing.[198]

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[195] *Id.* at 1218–19.
[196] Blau et al., *supra* note 133, at 3016–17; Duchin & Sosyura, *supra* note 133, at 26; Papanikolaou, *supra* note 133, at 70.
[197] GOVERNMENT ACCOUNTABILITY OFFICE, *supra* note 24, at 39.
[198] OFFICE OF THE SPECIAL INSPECTOR GENERAL FOR THE TROUBLED ASSET RELIEF PROGRAM, EXTRAORDINARY FINANCIAL ASSISTANCE PROVIDED TO CITIGROUP, INC. 6, 11 (Sigtarp 11-0002, Jan. 13, 2011).

Given Citigroup's size and degree of interconnectedness, it was determined that Citigroup needed to be "saved at all costs,"[199] though at least one regulator, Sheila Bair of the FDIC, wondered whether resolution might be a viable and preferable option.[200] While the point of saving Citigroup was to protect the financial system and prevent further disruption,[201] regulators also appreciated that many of Citigroup's problems were unique to Citigroup[202] and that a bailout of Citigroup served to save the firm from "the consequences of its own poor decisions."[203]

In January 2009 the health of Bank of America was a source of concern for the FDIC, which viewed the bank's "capital situation as 'strained.'"[204] Bank of America received an investment of $20 billion under TIP.[205] Bank of America's need for assistance was in part driven by problems caused by its government-directed acquisition of Merrill Lynch[206] as well as by significant losses due to increased credit costs and write-downs in Bank of America's capital market operations.[207] A loan-sharing agreement similar to the one in place for Citigroup was announced but never finalized.[208]

The benefit to a bank's market power from the extraordinary intervention to save Citigroup and Bank of America is obvious. Not only was obtaining investment at below-market rates beneficial to those banks (the GAO estimates that the Treasury paid a 26–50 percent premium over the market price for its TIP investments),[209] but it was also valuable because the U.S. government demonstrated that it would not allow these specific firms to fail and may have

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[199] *Id.* at 13.
[200] FREEMAN & MCKINLEY, *supra* note 133, at 300–303.
[201] OFFICE OF THE SPECIAL INSPECTOR GENERAL, *supra* note 198, at 13–16.
[202] *Id.* at 23.
[203] FREEMAN & MCKINLEY, *supra* note 133, at 300–303 (quoting Ben Bernanke).
[204] CONGRESSIONAL OVERSIGHT PANEL, *supra* note 180, at 43 (citing the transcript of an FDIC board meeting).
[205] GOVERNMENT ACCOUNTABILITY OFFICE, *supra* note 24, at 40.
[206] OFFICE OF THE SPECIAL INSPECTOR GENERAL, *supra* note 182, at 23.
[207] CONGRESSIONAL OVERSIGHT PANEL, *supra* note 180, at 49.
[208] GOVERNMENT ACCOUNTABILITY OFFICE, *supra* note 24, at 40.
[209] *Id.* at 27.

actually saved them from failure. Citigroup and Bank of America are likely in a much stronger position than they would have been absent dramatic government intervention. In fact, Citigroup and Bank of America may only currently exist because of the government.

It is hard to estimate the exact amount of support provided by the government. The GAO estimates that the emergency programs that provided the most direct assistance to bank holding companies offered approximately $2.6 trillion in potential support at their peak.[210] While the ultimate direct cost to taxpayers was nowhere near this astronomical amount, and in some cases was actually profitable,[211] this support not only exposed taxpayers to risk[212] but also helped insulate banks from the consequences of their actions. This protected banks that took unwise risks while harming banks and nonbank competitors that could have otherwise displaced firms facing market discipline. In fact, banks that received government support, especially those considered TBTF, were able to profit at the expense of their less-supported rivals. As the Congressional Oversight Panel for TARP noted, while hundreds of small banks were allowed to fail during the crisis, large banks were not, which meant they were in a position to pick the corpses of the smaller banks and become even larger and more powerful.[213]

While changes to the law have sought to make bailouts less likely,[214] it is unclear whether these efforts will be successful. First, while certain authorities held by regulators have been

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[210] *Id.* at 14–15.
[211] The U.S. government has turned a profit on at least some elements of the bailout for banks. *See, e.g.*, PRO PUBLICA BAILOUT TRACKER, https://projects.propublica.org/bailout/ (showing a significant profit from the Troubled Asset Relief Fund as of December 4th, 2018); FDIC, *supra* note 162, at 57–58.
[212] As Kenneth Rogoff noted to the Congressional Oversight Panel for TARP, part of the cost that taxpayers bore with TARP that needed to be considered part of its price was the *risk* that banks would fail and default, even if those defaults did not end up occurring. CONGRESSIONAL OVERSIGHT PANEL, *supra* note 180, at 58.
[213] CONGRESSIONAL OVERSIGHT PANEL, *supra* note 180, at 183.
[214] *See, e.g.*, GOVERNMENT ACCOUNTABILITY OFFICE, *supra* note 24, at 42–58 (discussing various changes to regulators' authorities post-crisis).

restricted, others remain and some new ones have been granted.[215] Second, it is worth remembering that many of the extraordinary steps taken by regulators to save banks (and therefore preserve their power) were done pursuant to crisis legislation.[216] In a new crisis, it is unclear whether Congress will stick to its stated desire for no new bailouts or if, in the words of former Treasury secretary Timothy F. Geithner, the government will feel the need to "do exceptional things again."[217] As discussed below,[218] there is evidence that the markets are not convinced that the government will not support banks again, which itself may serve to bolster banks' power.

5. IMPLICIT SUBSIDIES

In addition to the direct benefit certain banks obtained from government actions taken with the intent of protecting those banks from market discipline, there is also evidence of an indirect benefit. Some implicit subsidies seem to impact all or most banks, while others benefit only a select few. These subsidies help protect and enhance bank power by allowing them to attract and retain investment and deposits more cheaply than they would absent government support. Implicit subsidies are important for our discussion because they may allow incumbent banks to operate at an advantage relative to nonbanks that may compete on some product lines and allow some banks to maintain a market position they would lose to competition absent the subsidy. Because a decision to use power for business policies that amount to de facto regulation is specific to particular banks, it matters not only that banks have obtained significant support

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[215] *Id.* at 42–58.
[216] For example, the Emergency Economic Stabilization Act created TARP.
[217] OFFICE OF THE SPECIAL INSPECTOR GENERAL, *supra* note 198, at 44.
[218] *See infra* Section I.C.5.

relative to nonbanks but also that particular banks have been subsidized at higher rates than their competitors.

a. Banking-wide implicit subsidies. Banks appear to receive an implicit subsidy from public policy and the perception of investors that banks will be more likely to be protected in the event of economic trouble than firms outside the financial sector. For example, Andrew Atkeson, Adrien d'Avernas, Andrea Eisfeldt, and Pierre-Oliver Weill find that after the financial crisis, approximately half the franchise value of banks in the United States is attributable to the value of explicit or implicit government guarantees.[219] Bryan Kelly, Hanno Lustig, and Stijn Van Nieuwerburgh examined out-of-the-money (OTM) puts[220] for a financial sector stock index contrasted to OTM puts for individual financial firms and found evidence of a sector-wide subsidy amounting to approximately $282 billion.[221] They found no comparable implicit subsidy in other nonfinancial sectors.[222] Priyank Gandhi and Lustig also found evidence that some U.S. commercial banks enjoy a subsidy in that they are able to offer a lower equity return than comparably risky nonbank companies can.[223] Gandhi and Lustig identify the source of this subsidy as the commercial banks' ability to access the Federal Reserve's discount window and benefit from FDIC deposit insurance.[224]

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[219] Andrew G. Atkeson et al., *Government Guarantees and the Valuation of American Banks* 8 (Nat'l Bureau of Econ. Research, Working Paper No. 24706, July 2, 2018), https://www.nber.org/papers/w24706.
[220] An out-of-the-money put is a put with a strike price below the market value of the underlying asset. *See Out of the Money (OTM) Definition and Example* (Apr. 18, 2019), https://www.investopedia.com/terms/o/outofthemoney.asp.
[221] Bryan Kelly et al., *Too-Systemic-to-Fail: What Option Markets Imply About Sector-Wide Government Guarantees*, 106 AM. ECON. REV. 1278, 1280 (2016).
[222] *Id.* at 1308.
[223] Priyank Gandhi & Hanno Lustig, *Size Anomalies in U.S. Bank Stock Returns*, 70 J. FIN. 733, 735 (2015).
[224] *Id.* at 735–36. However, the authors also note that small banks suffer an implicit tax because of perceived financial sector risk.

b. Too-big-to-fail subsidies. While there is evidence that all or most banks enjoy some implicit subsidy as a result of public policy, banks that are perceived by investors and depositors to be so large or systemically important that the government will not allow them to fail appear to have benefited even more. These TBTF banks have been able to attract and retain customers more easily and obtain funding more cheaply than they would have absent the implicit guarantee that the government would save them.[225] This places them at an advantage over their nonprotected competitors, granting TBTF banks more market power than they would have absent the expectation, informed by precedent, of government protection if they run into trouble.[226]

Identifying the existence and scope of a TBTF implicit subsidy can be challenging, but evidence indicates that one can exist when there is an expectation among potential investors, creditors, or depositors that a bank will receive government assistance in a time of distress rather than be allowed to fail and enter receivership.

Recent discussion of the TBTF subsidy revolves around the last crisis and the firms that were bailed out. However, it is worth remembering that the concept that a bank could be too big to fail predates the 2008 financial crisis. Previous bailouts helped condition expectations for that crisis and still influence expectations today. An early example of a TBTF subsidy can be found after the government bailout of Continental Illinois National Bank and Trust Company. The Comptroller of the Currency made a statement in September 1984 in testimony before Congress that the 11 largest banks were "too big to fail,"[227] though the Comptroller did not mention

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[225] Nizan Geslevich Packin, *Supersize Them? Large Banks, Taxpayers and the Subsidies That Lay Between*, 35 NW. J. INT'L L. & BUS. 229, 237–38 (2015); GOVERNMENT ACCOUNTABILITY OFFICE, LARGE BANK HOLDING COMPANIES: EXPECTATIONS OF GOVERNMENT SUPPORT 30–33 (GAO-14-621, July 2014).
[226] Packin, *supra* note 225, at 237–38.
[227] Maureen O'Hara & Wayne Shaw, *Deposit Insurance and Wealth Effects: The Value of Being "Too Big to Fail,"* 45 J. FIN. 1587, 1587 (Dec. 1990).

exactly which banks he was referring to.[228] Analyzing the aftermath of this announcement, Maureen O'Hara and Wayne Shaw find that banks expected to be covered by the Comptroller's announcement experienced significant increased abnormal stock returns, while banks not expected to be covered suffered negative abnormal returns.[229] Further, for the banks expected to be covered by the Comptroller's announcement, the larger the bank, the higher the abnormal return. However, noncovered banks, particularly the larger banks, experienced more negative abnormal returns.[230] O'Hara and Shaw also find that for banks expected to be covered by the Comptroller's announcement, the less solvent the bank was, the higher the abnormal return—implying that the value of the implicit subsidy is higher the less solvent an institution is.[231]

The 2008 financial crisis and its aftermath also indicate that TBTF banks have enjoyed an implicit subsidy because of government actions and statements conditioning the market to expect that large banks will be saved by the government if they are at risk of failure. For example, looking at money market deposit accounts from 2005 to 2010, Stefan Jacewitz and Jonathan Pogach find evidence that large banks were able to pay lower rates (between approximately 35 and 40 basis points) on uninsured money market deposit accounts than their smaller peers during the crisis because the large banks were perceived to be less risky.[232] The rate advantage enjoyed by big banks disappeared after a change in the law extended FDIC insurance in money market deposit accounts, replacing an apparent implicit government guarantee for accounts at some

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[228] *Id.* at 1591.
[229] *Id.* at 1593.
[230] *Id.* at 1595–96.
[231] *Id.* at 1596.
[232] Stefan Jacewitz & Jonathan Pogach, *Deposit Rate Advantages at the Largest Banks*, 53 J. FIN. SERV. REV. 1, 2, 33 (2018).

banks with an explicit guarantee at all banks.[233] Given the importance of deposits as a funding mechanism for banks,[234] such a differential could provide significant savings for TBTF banks.[235]

There is significant evidence from the capital markets that TBTF banks recently enjoyed an implicit subsidy from the government. Looking at debt markets from 1990 to 2012, Viral Acharya, Deniz Anginer, and A. Joseph Warburton find that being a large financial firm, especially a bank, is associated both with being able to pay less to issue debt and with less risk sensitivity on the part of investors.[236] Acharya, Anginer, and Warburton estimate that large financial firms (including banks) received an average of $30 billion a year between 1990 and 2012 in implicit subsidies, with subsidies exceeding $100 billion a year during the financial crisis.[237]

Other scholars also find evidence for an implicit government subsidy to TBTF banks of approximately $121.29 billion and posit that, absent this TBTF subsidy, banks would not have issued approximately $91.6 billion of corporate debt in 2008 and 2009.[238] This finding is based on the spread between credit default swap premiums and stock-market-implied credit default swap premiums: during the crisis, financial firms exhibited an average pricing error of 183 basis points while banks exhibited a mean pricing error of 350 basis points.[239] Meanwhile, nonfinancial firms showed much lower spreads.[240]

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[233] *Id.* at 3.
[234] "[At the end of 2006] deposits represented 61 percent of total assets for banks larger than $200 billion and 68 percent for the rest of the [banking] industry. . . ." *Id.* at 2.
[235] Jacewitz and Pogach estimate the observed advantage in 2007 to be approximately $7.1 billion total. They also note that if TBTF banks enjoyed a comparable discount across all uninsured liabilities and equity, the advantage would equal about $17 billion. *Id.* at 28.
[236] Viral Acharya et al., The End of Market Discipline? Investor Expectations of Implicit Government Guarantees 2, 19 (May 2016) (unpublished manuscript), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1961656.
[237] *Id.* at 19.
[238] Frederic A. Schweikard & Zoe Tsesmelidakis, The Impact of Government Interventions on CDS and Equity Markets 32–33 (June 2012) (unpublished manuscript), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1943546.
[239] *Id.* at 13.
[240] *Id.*

According to one study, an implicit TBTF guarantee allowed large banks to pay artificially low rates on corporate debt issued between 2007 and 2010, resulting in a subsidy of $129.2 billion to TBTF bank shareholders (who benefited from additional return on equity) and $236.1 billion to TBTF bank debtholders (who benefited from reduced default risk thanks to the implicit guarantee that the government would prevent a default).[241] The implicit government guarantee also allowed large banks to continue to offer short-term debt when other firms were forced into issuing relatively more expensive long-term debt.[242]

Implicit government insurance against failure lowers the expected equity return of the 10 largest commercial banks by almost 2 percent compared to a portfolio of stocks with similar risk, resulting in an average savings of $2.76 billion per bank per year.[243] Conversely, small banks pay more to investors to compensate for risk than large banks do,[244] even though small banks have outperformed large banks on several criteria during the past two recessions.[245] Gandhi and Lustig conceptualize the implied government guarantee as granting potential shareholders OTM puts on large banks but not on small ones, lowering the risk of holding large bank equity and allowing large banks to offer equity relatively cheaply.[246]

Kelly, Lustig, and Van Nieuwerburgh examine OTM puts for a financial sector stock index contrasted to OTM puts for individual financial firms and find evidence of a sector-wide subsidy amounting to approximately $282 billion.[247] They also analyze puts for individual firms and find that puts on the largest 10 percent of banks were significantly cheaper than on smaller

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[241] Zoe Tsesmelidakis & Robert Merton, The Value of Implicit Guarantees 2 (July 2013) (unpublished manuscript), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2231317.
[242] *Id.*
[243] Gandhi & Lustig, *supra* note 223, at 735.
[244] *Id.* at 735, 739.
[245] *Id.* at 752.
[246] *Id.* at 735, 753.
[247] Kelly et al., *supra* note 221, at 1280.

banks during the financial crisis, even though there was little or no difference in prices before the crisis.[248] They find that the difference in price related to firm size only appeared in the financial sector.[249] They also find evidence that risk-adjusted credit default swap rates were lower during the crisis for large financial firms than for small financial firms, and that this discrepancy only existed in the financial sector.[250]

The GAO also examined whether large bank holding companies (BHCs) benefited from an implicit government backstop that subsidized their ability to obtain capital or assets.[251] The GAO assessed the state of the literature and noted that most studies found that large BHCs were able to obtain funding more cheaply than small BHCs during the financial crisis, but it also noted that previous studies were subject to limitations that may limit the validity of their results.[252] The GAO also interviewed regulators and market participants. Officials from the Financial Stability Oversight Council noted that, while the market perception that some banks might not be allowed to fail had diminished, it still existed.[253]

The GAO then used 42 different econometric models to examine funding costs of large and small BHCs from 2006 to 2013. While the results did indicate that large BHCs were able to obtain funding more cheaply during the financial crisis than smaller BHCs, providing some evidence for a TBTF subsidy, the models also provided some evidence that that advantage had diminished and may have disappeared in the wake of the crisis.[254] However, the GAO also found that among "systemically important" financial institutions (defined as those with $50

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[248] *Id.* at 1312.
[249] *Id.*
[250] *Id.* at 1313.
[251] GOVERNMENT ACCOUNTABILITY OFFICE, *supra* note 225.
[252] *Id.* at 40.
[253] *Id.* at 38.
[254] *Id.* at 48–51.

billion or more in assets) the larger BHCs tended to have lower funding rates,[255] and that risky large BHCs were able to acquire funding more cheaply than comparably risky small BHCs.[256] The GAO also found that its models predicted that large BHCs would be able to find funding more cheaply than small BHCs if the credit risk environment were comparable to the environment during the crisis.[257]

As the GAO notes, it is possible that being TBTF has become a disadvantage as new government regulation has dampened expectations that the government will bail out TBTF banks and has imposed new costs on large institutions.[258] However, it is also possible that the subsidy has gone into stasis rather than going away. As discussed above, the GAO noted in its models that large BHCs were able to obtain funding more cheaply in a credit risk environment similar to that of the financial crisis.[259] Atkeson, d'Avernas, Eisfeldt, and Weill's work also indicates that while the raw value of government guarantees has diminished significantly, it has not disappeared and makes up about half of banks' excess franchise value, indicating that there is still an expectation of government bailouts.[260]

Even if the TBTF subsidy has diminished or expired, its existence may have contributed to banks' market power. Opportunities to access capital more cheaply, or access more capital than would otherwise be possible, or obtain or retain customers that could otherwise have gone

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[255] *Id.* at 52.
[256] *Id.* at 53.
[257] *Id.* at 54.
[258] *Id.* at 24–30 (discussing regulatory changes that lower market expectations of a bailout in the future), 36 (discussing the Federal Reserve Capital Surcharge, expected to partially offset TBTF advantage). *See also* STEVE STRONGIN ET AL., MEASURING THE TBTF EFFECT ON BOND PRICING (Goldman Sachs Glob. Markets Inst., May 2013) (finding that there was a minor TBTF advantage for large banks during the crisis but that large banks face higher funding costs after the crisis); Aditi Kumar & John Lester, *Do Deposit Rates Show Evidence of Too Big to Fail Effects?* (Oliver Wyman, Mar. 2014) (extending the analysis done by Jacewitz and Pogach (*see supra* note 232 and accompanying text) to include 2010–2012 and finding that the cost advantage shrinks dramatically and is likely attributable to non-TBTF factors).
[259] *See* GOVERNMENT ACCOUNTABILITY OFFICE, *supra* note 225, and accompanying text.
[260] Atkeson et al., *supra* note 219, at 4–5.

to a competitor can provide lasting benefits to firms because firms can build on this success. These benefits can also reduce competition that would otherwise emerge and threaten the power of favored firms. Therefore, even if the TBTF subsidy is currently dormant or absent, we cannot discount its effect on the market power some banks currently enjoy.

Some have argued that TBTF banks enjoy economies of scale that benefit society as a whole by providing more effective and efficient access to financial services.[261] From this perspective, the implicit benefit TBTF banks enjoyed and may still enjoy is arguably justified.[262] However, even if this is true, it only holds if the subsidized TBTF banks actually *provide services* to the public. If a subsidized bank withholds services to enforce its view of good social policy, rather than fulfilling its role of intermediating credit, processing payments, or providing deposit services, it will have captured the TBTF subsidy without providing the services that nominally justify it.

II. Why Banks Acting as De Facto Regulators Is Potentially Problematic

Having discussed some of the ways the government grants certain important forms of privilege to banks, frequently at the expense of nonbank competitors or by favoring some banks over others, we will now discuss some of the reasons why it may be inappropriate for banks to try to impose de facto regulation. One reason is that public policy granted banks privileges for reasons that are different from, and frequently inconsistent with, the idea of banks withholding service in order to limit legal behavior downstream. Additionally, allowing banks to serve as regulators risks banks abusing their important and, in many ways, government-granted position.[263]

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[261] Packin, *supra* note 225, at 255.
[262] *Id.*
[263] It could also be argued that banks are unlikely to be competent at regulation or embrace the procedural safeguards policymakers generally impose on government regulation. However, an examination of this question is beyond the scope of this paper.

A. Banks That Withhold Service May Be Acting Inconsistently with the Reasons They Are Empowered by Public Policy

As discussed above, banks enjoy protection from competition and from the consequences of their actions. Banks also are able to take advantage of government-provided infrastructure and services that are denied to their nonbank rivals. While these powers reflect a series of political decisions and were created over time instead of as one coherent whole, the "regime of privilege" banks enjoy is generally justified by supporters as appropriate because banks are considered both special and essential to a functioning economy. It is worth considering whether the idea of banks assuming the role of de facto regulators is consistent with the purposes underlying the granting of their advantages. If a bank's actions are inconsistent with how the advantages are justified, this calls into question whether the public is actually benefiting from the bargain it struck with banks, and whether banks should continue to enjoy their advantages.

1. CHARTERS

As discussed above, the government's ability to restrict access to bank charters (and all the advantages that come with a charter) is a significant source of banks' market power and distinguishes banks from many other firms, including other financial services firms.[264] Most states and the federal government evaluate charter applications on public-benefit grounds.[265] It is therefore worth evaluating why the government is supposed to grant or withhold bank charters, and whether banks' use of that power for de facto regulatory purposes is consistent with these justifications.

[264] *See supra* Section I.A.1.
[265] *See supra* Section I.A.1.a.

Banks have always been controversial in the United States.[266] Their supporters consider them useful, if not essential, to furthering economic development,[267] but banks have also been feared as a threat to equality, virtue, economic stability, and even the republican form of government (because they potentially grant a narrow clique of people too much power over the economy).[268] Banks are seen as posing unique risks to the economy, both through their failure and through malfeasance.[269]

Moreover, limiting access to the business of banking via chartering has served as a source of direct and indirect revenue for states (including through outright graft).[270] All this has resulted in a regulatory environment that has traditionally limited access to banking via charters and has frequently imposed conditions beyond mere competence on those who wish to obtain a charter.[271]

Currently, when the OCC evaluates whether to grant a charter, its policy is to consider, inter alia, whether the proposed bank will "provide fair access to financial services by helping to meet the credit needs of its *entire* community"[272] and whether it will promote "fair treatment of customers including *efficiency* and *better service*."[273] The OCC may also consider the

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[266] *See* Mehrsa Baradaran, *Banking and the Social Contract*, 89 NOTRE DAME L. REV. 1283, 1287–90 (2013) (discussing early controversies surrounding banks).
[267] *Id.* at 1289–90; HOWARD BODENHORN, A HISTORY OF BANKING IN ANTEBELLUM AMERICA 15 (2000).
[268] Baradaran, *supra* note 266, at 1288, 1296–97; HOWARD BODENHORN, STATE BANKING IN EARLY AMERICA: A NEW ECONOMIC HISTORY 78 (2003); Sylvan Lane, *Bernie Sanders Introduces Bill to Break Up Big Banks*, THE HILL (Oct. 2018), https://thehill.com/policy/finance/409785-bernie-sanders-introduces-bill-to-break-up-big-banks.
[269] Baradaran, *supra* note 266, at 1313–14; BODENHORN, *supra* note 268, at 155. *But see* Daniel R. Fishchel et al., *The Regulation of Banks and Bank Holding Companies*, 73 VA. L. REV. 301, 306–12 (1987) (disputing certain arguments that banks are inherently different from other firms).
[270] Richard Sylla et al., *Banks and State Public Finance in the New Republic: The United States, 1790–1860*, 47 J. ECON. HIST. 391–403 (June 1987); BODENHORN, *supra* note 268, at 16–17; John Joseph Wallis, *Answering Mary Shirley's Question, or What Can the World Bank Learn from American History?*, *in* POLITICAL INSTITUTIONS AND FINANCIAL DEVELOPMENT 101 (Stephen Haber et al. eds., 2007).
[271] *See, e.g.*, Peltzman, *supra* note 43; Ladenson & Bombara, *supra* note 43; Kenneth E. Scott, *In Quest of Reason: The Licensing Decisions of Federal Banking Agencies*, 42 CHICAGO L. REV. 235, 284 (Winter 1974); Krishnamurthy, *supra* note 43, at 842.
[272] 12 C.F.R. § 5.20(f)(1)(ii) (2015) (emphasis added).
[273] *Id.* § 5.20(f)(1)(iv) (emphasis added).

factors relevant to the FDIC's determination about whether to grant deposit insurance.[274] These factors include whether the bank will serve the "*convenience* and *needs* of the community."[275] In evaluating whether to allow bank mergers, the OCC also looks at what impact the merger would have on competition and whether it would provide "expanded or less costly services to the community."[276]

Most states cite similar criteria for evaluating bank charters. For example, California requires a bank to prove to the satisfaction of the state banking commissioner that the "public convenience and advantage will be promoted by the establishment of the proposed bank."[277] Illinois requires that the Commissioner of Banks and Real Estate must find that "the convenience and needs of the area sought to be served by the proposed bank will be promoted."[278] Ohio requires that "the convenience and needs of the public will be served by the proposed bank."[279] For most states, there is some requirement that the bank will serve the needs of the public.

The public-needs requirement reflects the fact that banks are meant to be intermediaries that help the public meet its needs. Those needs are determined by the public, not the banks. Banks are downstream from the public expressing its preferences through the market (what do people want to buy and sell) and the political and regulatory process (what should and should not be legal). Banks making lending decisions on the basis of whether the loan will be profitable and paid back reflects the bank assessing the market desires of the public. In this way banks are serving as intermediaries to efficiently allocate credit and other services to meet the public's needs. However, when a bank chooses to withhold services in order to limit or deny access to a legal good or

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[274] *Id.* § 5.20(f)(2)(iii).
[275] 12 U.S.C. § 1816(7) (2019) (emphasis added).
[276] 12 C.F.R. § 5.33(ii)(a), (c) (2019).
[277] CAL. FIN. CODE § 1023(a) (2019).
[278] 205 ILL. COMP. STAT. 5/10(a)(5) (2019).
[279] OHIO REV. CODE ANN. 1113.03(C)(2) (2019).

service, the bank is seeking to impose its will on the public rather than responding to the public's desires and convenience. In fact, if a bank refuses to serve lawful businesses it disfavors (when service would be consistent with safety, soundness, and profitability considerations), this could inconvenience the public and frustrate their desires. Such a situation could arguably be inconsistent with the criteria according to which the bank was granted its charter.

2. FDIC INSURANCE

The FDIC was founded under the Banking Act of 1933.[280] The Banking Act was intended "to provide for the safer and more effective use of the assets of banks, to regulate interbank control, to prevent undue diversion of funds into speculative operations, and for other purposes."[281] U.S. banking history leading up to 1933 helps illuminate the intent behind this Act. Congress passed the Banking Act of 1933 in the aftermath of the stock market crash of 1929 and the bank runs of the early 1930s. These bank runs resulted in a number of bank failures because banking institutions were not able to supply the massive cash payouts that their depositors demanded. Depositors lost around $1.3 billion between the years 1929 and 1933.[282] Many argued that the government needed to act in order to provide security that depositors' funds would be there when they decided to access them. Such assertions led to the Banking Act and the formation of the FDIC.

The FDIC was created to prevent bank runs, and the bank failures that resulted from them, from occurring in the future. It would accomplish this by insuring depository accounts up to a specified amount. Not only would depositors have a guaranteed payout in the event of a bank run, but the promise of this payout would deter bank runs to begin with.

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[280] 48 Stat. 162 (1933).
[281] *Id.*
[282] FDIC, *Historical Timeline*, https://www.fdic.gov/about/history/timeline/1930s.html (last visited Aug. 17, 2019).

It is clear that the FDIC was formed to increase the stability of banking institutions and to protect depositors. The legislative history of the Banking Act supports this. When explaining the justifications for the Act, a senate report specifically noted that "within the past few years, the insolvency of banks has been a major cause of distress and business difficulty in all parts of the country."[283] It stated that the goal in creating the FDIC was to provide for the "protection of depositors and limitation of their losses through a bank deposit insurance corporation."[284] Nowhere in the Banking Act or its legislative history was it posited that the FDIC was created to empower banks to be moral arbiters or de facto policymakers. The purpose of FDIC insurance is to provide more stability and trust within the financial sector, not to give banks the ability to impose their regulatory preferences on the market.

3. LENDING AND MONEY TRANSMISSION

Banks' advantages with regard to lending and money transmission licensing result from a combination of federal authority for national banks that prevents states from imposing licensing requirements[285] and state comity regarding each other's institutions that are subject to bank regulation at the state and federal level.[286]

Banks' ability to export laws governing interest while making loans arose out of Congress's desire to protect national banks from hostile state regulation.[287] Congress later expanded this power to state-chartered banks in the spirit of competitive equity.[288] Denying nonbanks similar power is justified by its supporters on the grounds that while state usury laws

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[283] S. REP. NO. 73-99, at 11 (1933).
[284] *Id.*
[285] 12 U.S.C. 24 (Seventh) (2019) authorizes national banks to lend and transmit money.
[286] *See supra* Sections I.B.1 and I.B.2; Tu, *supra* note 86, at 89.
[287] *See supra* Section I.B.1.
[288] *See supra* Section I.B.1.

protect consumers, they are unnecessary for banks, which are subject to an "alternative federal regulatory regime."[289]

It is questionable whether granting these advantages to banks and not to their nonbank competitors is justified.[290] However, even if we accept the proffered justifications, there are no indicia that banks enjoy these advantages because of a desire at the state or federal level that banks use their power to regulate markets rather than to facilitate markets in meeting the desires of customers for lawful products and services.

4. PAYMENTS SYSTEM

The Federal Reserve's entry into the payments system was justified as a way to improve efficiency and lower costs by providing an alternative to the somewhat cumbersome system of correspondent banking and private clearinghouses previously used by banks.[291] Proponents asserted that the beneficiaries of the improved system were not just banks but also American industry and consumers, who could obtain the payments services they sought from banks at a better quality and with reduced risk of a breakdown in the payments system in the event of a banking panic.[292] However, a somewhat more cynical, though not incompatible, explanation is that the Fed took on the role of providing payments services to banks in order to embed itself in

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[289] Adam J. Levitin, *'Madden Fix' Bills Are a Recipe for Predatory Lending*, AM. BANKER, Aug. 28, 2017, https://www.americanbanker.com/opinion/madden-fix-bills-are-a-recipe-for-predatory-lending.

[290] *See generally* Knight, *supra* note 85; *see also* Brian Knight, *Credit Markets Need Legislative Guidance After Madden Decision*, AM. BANKER, Sept. 14, 2017, https://www.americanbanker.com/opinion/credit-markets-need-legislative-guidance-after-madden-decision.

[291] Pierre Jay, *The Federal Reserve System, State Banks and Par Collections*, 99 ANNALS AM. ACAD. POL. & SOC. SCI. 82–83 (Jan. 1922); James N. Duprey & Clarence W. Nelson, *A Visible Hand: The Fed's Involvement in the Check Payments System*, 18, 20–21, 23 (1986).

[292] Jay, *supra* note 291, at 83, 86.

the U.S. banking system, making it more essential and therefore less politically vulnerable, and providing it with a source of revenue.[293]

In either case, it does not appear that the Fed intended to grant banks access to valuable infrastructure to allow banks to engage in de facto regulation by withholding services from Americans. Rather, the Fed's stated intent in providing banks with access to a government-administered payments system was to improve the quality of banks' facilitation of payments. Accordingly, banks' refusal to provide payments services in order to act as de facto regulators is at best unrelated to the purpose for which the payments system was created and at worst fundamentally inconsistent with the reason the Fed provides the service.

5. BAILOUTS

Bank bailouts not only save banks from failure, they may also allow recipient banks to improve their market power and (at least in the case of large banks) raise money more easily because investors anticipate future bailouts.[294] Bailouts are generally justified by regulators and policymakers as necessary to prevent collateral damage to the economy. This damage may be panic, or it may be a breakdown in the intermediating function for credit and payments that banks provide. Further, allowing the existence of banks that are so large they are "too big to fail" is sometimes justified on the grounds that there are economies of scale to banking, and therefore the benefit of having large banks provide more value to banking consumers than small banks outweighs the detriment of large banks' somewhat higher risk profile.[295]

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[293] Edward J. Stevens, *The Founders' Intentions: Sources of the Payment Services Franchise of the Federal Reserve Banks* 25–26 (Fed. Reserve Fin. Servs. Working Paper 0396, 1996).
[294] *See supra* Section I.C.4.
[295] *See supra* Section I.C.1.

These justifications all relate to the essential role banks play to enable a functioning market, including by providing credit and facilitating payments. This reasoning is especially true for TBTF banks, whose higher risk profile is justified as the unavoidable side effect of what makes TBTF banks more efficient and better at providing services. If banks refuse to provide services to customers engaged in lawful commerce in order to try to force a change in consumer or firm behavior, their refusal denies potential customers the benefit of these economies of scale for legal but disfavored activities. In other words, banks' refusal to provide services to lawful businesses removes at least some of the benefit banks are supposed to provide in exchange for insulation from market discipline and from the consequences of their actions. Further, it protects the market power of the banks that have been bailed out or have benefited from the subsidy that can come from expected bailouts. This harms the banks' competitors, which would otherwise benefit from the failure of specific banks. It also harms the frustrated customers who could potentially have been served by these competitors. While some of this harm may be attenuated, it seems clear that banks are not bailed out in order to deny Americans banking services.

The central issue is not whether supporting banks and insulating them from the market is a legitimate goal of public policy.[296] The point is that neither Congress nor federal regulators have empowered banks to coerce the public into avoiding specific, lawful behaviors deemed "bad" or "undesirable" by the banks themselves. Instead, banks are intended to support consumers, lawful commerce, and economic development. When banks use the powers they are granted to leverage refusal of service as a tool to coerce changes in otherwise lawful behavior, this is inconsistent with the justifications for the grants of those powers and with the banks' role as financial intermediaries.

[296] An analysis of whether this is so is beyond the scope of this paper.

While the specific purposes for the powers granted to banks differ, they all relate to general themes of making banks safer and more effective facilitators of lawful commerce. The use of these powers to coerce is at best irrelevant and at worst contradictory to these themes. This means that corrective action may be justified without regard for whether banks are successful in their use of power. It does not matter whether a specific bank has sufficient market power to de facto regulate a market: the mere attempt is contrary to the purpose and spirit of the power the bank was granted. Therefore, it may be reasonable for the government to take steps to prevent that power's misuse.

B. Banks' Role and Position May Raise Unique Concerns

Banks provide essential services to the economy. As discussed above,[297] they are also considered "different" from most other types of businesses and are regulated accordingly. This regulatory approach creates an environment in which the market for certain services that are extremely important, if not essential, to modern life (e.g., credit, payments services, and the safekeeping of wealth[298]) is distorted by regulation, and select providers of these services (banks) are given unique support. There is also the concern that the market for banks is consolidating, owing to both natural and regulatory forces. This should give us pause when we consider banks strategically withholding services to de facto regulate others, because customers may not be able to rely on a fully competitive market to protect them.

The juxtaposition of the importance of banking services, especially credit, with the power of banks and the government-granted privilege they enjoy has been a subject of significant

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[297] *See supra* Section I.A.1.

[298] It is important to note that access to these services is important not only directly but also indirectly. A person may wish to avoid credit and pay only cash for goods and services he or she wishes to buy, but if the provider of those goods cannot access credit, payments, or savings, it will be much harder for the provider to maintain a market presence.

concern in the past. Proposals about how to address this concern have been a recurrent feature of the debate surrounding the regulation of banking services. Past and current arguments may help illustrate the potential risks of banks seeking to act as regulators.

1. THE MARKET FOR BANKING SERVICES MAY NOT BE FULLY COMPETITIVE

While the United States has a large number of banks relative to many other countries,[299] it is going through a period of significant consolidation. The number of banks has declined from more than 13,000 in 1992 to just over 5000 at the end of 2018.[300] The share of assets held by the ten largest banks (by assets) has also increased markedly, from 27.2 percent in 1984 to 58.3 percent in 2016.[301]

The level of concentration within the U.S. banking market is debated. Using a common measure of market concentration, the Herfindahl-Hirschman Index (HHI),[302] U.S. banking regulators consider a market moderately concentrated if it scores between 1000 and 1800 and highly concentrated if it scores at or above 1800.[303] The Bank Policy Institute, an industry-affiliated research institute, estimated that the HHI of the national market as a whole was 617 for

[299] For example, there are only 88 banks in Canada and 41 in the United Kingdom. *See* Canadian Bankers Association, *Focus: Fast Facts About the Canadian Banking System* (Mar. 13, 2019), https://cba.ca/fast-facts-the-canadian-banking-system; European Banking Resources, *Banks in Country United Kingdom*, https://www.ecbs.org/banks/united-kingdom/ (last visited Aug. 17, 2019).

[300] Stephen Matteo Miller et al., *The Recent Decline in the Number of Banks*, THE BRIDGE (Mercatus Ctr. at George Mason Univ.), June 11, 2019, https://www.mercatus.org/bridge/commentary/recent-decline-number-banks.

[301] Dean Corbae & Pablo D'Erasmo, *Capital Requirements in a Quantitative Model of Banking Industry Dynamics* 1 (Nat'l Bureau of Econ. Research, Working Paper No. 25424, Jan. 2019).

[302] The Herfindahl-Hirschman Index is calculated by squaring the market share of each competing firm in a relevant market and then adding the resulting numbers. A market with perfect competition will have a total approaching 0 and a complete monopoly will have total of 10,000. *See* DEPARTMENT OF JUSTICE, HERFINDAHL-HIRSCHMAN INDEX (Jul. 31 2018), https://www.justice.gov/atr/herfindahl-hirschman-index.

[303] 12 C.F.R. § 265.11(c)(11)(v); *The ABCs of HHI: Competition and Community Banks*, FEDERAL RESERVE BANK OF ST. LOUIS (June 11, 2018), https://www.stlouisfed.org/on-the-economy/2018/june/hhi-competition-community-banks.

assets as of the third quarter of 2018.[304] Conversely, Andrew P. Meyer of the Federal Reserve Bank of St. Louis looked at proxy banking markets at the county or metropolitan statistical area level and found that the mean HHI was as high as 3468 in 2017, with 78.8 percent of markets considered "highly concentrated." Concentration was much higher in rural markets than in urban markets: 88.8 percent of rural markets were considered highly concentrated, compared to a maximum of 29 percent of urban markets.[305] Meyer also found that concentration levels on average were increasing since around 2009, though the increase was much more muted for urban markets than for rural ones.[306]

Other estimates of bank market concentration fall somewhere in between these two extremes. Wilko Bolt and David Humphrey find that the average HHI for a sample of 2644 U.S. banks was 1165 over the 2008–2010 period, though they also find that HHI is not a good predictor of competition.[307] Bolt and Humphrey find that other measures of competition in the banking market show a relatively but not perfectly competitive market.[308] Using data ranging from 1984 to 2016, Dean Corbae and Pablo D'Erasmo find evidence of imperfect competition in the banking market, including a much lower Rosse-Panzar *H* statistic than that found by Bolt and Humphrey (.4 vs .79) and markups that exceed 50 percent.[309] While increased concentration of

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[304] Greg Baer, *The Banking Industry Is Unconcentrated, and Will Remain So After the BB&T/SunTrust Merger*, BANK POLICY INST. (Feb. 15, 2019), https://bpi.com/the-bbt-corp-and-suntrust-banks-merger-will-not-raise-the-concentration-of-the-banking-industry/.
[305] Andrew P. Meyer, *Market Concentration and Its Impact on Community Banks*, FEDERAL RESERVE BANK OF ST. LOUIS (Apr. 12, 2018), https://www.stlouisfed.org/publications/regional-economist/first-quarter-2018/concentration-community-banks.
[306] *Id.*
[307] Wilko Bolt & David Humphrey, *Assessing Bank Competition for Consumer Loans* 4, 19–20 (De Nederlandsche Bank Working Paper No. 457, Jan. 2015).
[308] *Id.*
[309] Corbae & D'Erasmo, *supra* note 301, at 6; Bolt & Humphrey, *supra* note 307, at 5–6.

market power can be natural,[310] it can also be the result of government action, as evidenced by the impact of TARP on the banking market.[311]

There is evidence that, in at least some markets, concentration provides banks with market power that can result in higher costs and more onerous loan terms.[312] This seems to indicate that the market for banking is at least sometimes not highly competitive. It also seems to indicate that if certain banks remove themselves from the market for a possible customer, this may grant the remaining banks more market power and potentially the ability to extract rents, harming potential customers even if these customers are still able to obtain banking services.

2. BANKS' UNIQUE ROLE AND POSITION MAY WARRANT ADDITIONAL DUTIES AND LIMITATIONS

The importance of the services banks provide, combined with concern that banks, and those who run them, will use their power to de facto regulate others, has given rise to calls to impose unique duties on banks as a type of common carrier or public utility.[313] These calls might be excessive,

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[310] *See, e.g.*, Stephen Matteo Miller et al., *On the Historical Rise and (Recent) Decline in the Number of Banks*, THE BRIDGE (Mercatus Ctr. at George Mason Univ.), June 18, 2019, https://www.mercatus.org/bridge/commentary/historical-rise-and-recent-decline-number-banks.

[311] *See supra* Section I.C.4.

[312] *See, e.g.*, Iftekhar Hasan et al., *Bank Market Power and Loan Contracts: Empirical Evidence*, 46 ECON. NOTES REV. BANKING, FIN. & MONETARY ECON. 649–76 (2017) (finding that banks with greater market power will exercise that market power to charge higher prices and impose more onerous terms on borrowers seeking syndicated loans); Yili Lian, *Bank Competition and the Cost of Bank Loans*, 51 REV. QUANT. FIN. & ACCT. 253–82 (2017) (finding that banks with market power are able to charge business borrowers higher interest and impose more onerous terms than banks in more competitive markets, especially with regard to borrowers who are non-investment-grade businesses or financially constrained); Biao Mi & Liang Han, *Banking Market Concentration and Syndicated Loan Prices*, REV. QUANT. FIN. AND ACCT. (2018) (finding that higher concentration for banking in both the borrower and lead arranger's market was positively associated with higher loan prices); Julapa Jagtiani & Catharine Lemieux, *Fintech Lending: Financial Inclusion, Risk Pricing, and Alternative Information* (Federal Reserve Bank of Philadelphia, Working Paper No. 17-17, 2017) (finding that banks are able to charge higher rates for credit cards in banking markets with high concentration) (Note: this study defined "high concentration" as a market with an HHI over 2500 rather than using the legal definition for banks of 1800.).

[313] For example, the Supreme Court in *Noble State Bank v. Haskell* acknowledged that banks were so essential to successful commerce that they were subject to enhanced regulation by the state, in an era when government regulation of private business was much more suspect than it is today. 219 U.S. 104, 111–112 (1911).

but they indicate a recognition that banks are important and that the market for banking services may not provide full protection to potential customers. A significant reason for this concern may be the fact that public policy grants banks important privileges and some protection from market forces. Therefore, even if public utility status is not justified for banks, the insights from these discussions are useful as we consider whether banks should be able to use their power for the purposes of regulating the behavior of others.

Modern advocates of treating banks as public utilities continue to point to banks' importance as a justification.[314] However, they also point to the support that banks receive from the government and the distorted market that is created as a result.[315] To these scholars, banks' critical role in facilitating economic activity and ability to utilize and benefit from government support should render them something like a "public-private joint venture," in the words of Alan M. White.[316] This public-private joint venture would entail affirmative obligations to provide services universally and at rates limited by what the public considers fair.[317] if banks are considered public utilities, the debate about whether banks can act as regulators is at an end—because public utilities cannot refuse service, except for failure to pay and a few other narrowly tailored exceptions.[318]

Turning banks into public utilities would be an extreme move. However, without supporting making banks public utilities, we acknowledge the importance of banking services and the role that government-granted privilege plays within this sector. This importance has been

[314] *See, e.g.*, Baradaran, *supra* note 266, at 1312–14; K. Sabeel Rahman, *The New Utilities: Private Power, Social Infrastructure, and the Revival of the Public Utility Concept*, 39 CARDOZO L. REV. 1621, 1658–60 (2018); Alan M. White, *Banks as Utilities*, 90 TULANE L. REV. 1241, 1270–72 (2016).
[315] Baradaran, *supra* note 266, at 1314–23; Rahman, *supra* note 314, at 1658; White, *supra* note 314, at 1269.
[316] White, *supra* note 314, at 1269.
[317] *Id.* at 1271–72.
[318] *The Duty of a Public Utility to Render Adequate Service: Its Scope and Enforcement*, 62 COLUM. L. REV. 312, 323–26 (1962).

one of the justifications for laws that limit the discretion enjoyed by banks as they make decisions about whether to provide services, though their discretion is limited to a significantly lesser degree than it would be if they were designated public utilities.

For example, the Equal Credit Opportunity Act of 1974 (ECOA)[319] precludes banks and other extenders of credit from denying credit on the basis of certain borrower characteristics such as sex, race, and national origin, as well as whether the borrower obtains income from public assistance or has exercised certain legal rights.[320] ECOA originally only precluded discrimination in credit decisions on the basis of sex and marital status.[321] Shortly thereafter, amendments were proposed to expand the number of criteria that lenders would be prohibited from considering.[322] Motivating the desire to amend the law was a belief that credit was critical and that people were entitled to "fair treatment" from potential creditors.[323] While supporters of amending ECOA did not believe that people had an absolute right to credit,[324] they did believe that decisions should be made on the basis of the creditworthiness of the borrower and not unrelated factors.[325] At least one Senator also felt that "discrimination in the granting of credit by a private-public institution such as a bank is wrong, period,"[326] while a representative of the Department of the Treasury stated that "when discrimination enters into a credit decision it represents a failure of our free

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[319] 15 U.S.C. § 1691 *et seq.* (2019).
[320] *Id.* § 1691(a).
[321] Janet L. Scagnelli, *Consumer Credit Protection—The Equal Credit Opportunity Act Amendments of 1976*, 50 TEMP. L. Q. 388 (1977).
[322] *Id.*
[323] *See, e.g.*, *Hearings on S. 483, S. 1900, S. 1927, S. 1961, and H.R. 5616 Before the Subcommittee on Consumer Affairs of the Senate Comm. on Banking, Housing, and Urban Affairs*, 94th Cong. 1 (1975) (statement of Senator Biden); *id.* at 4 (statement of Senator Brock) ("To deny a credit worthy person the privilege of the service on the arbitrary basis of age is to deny that person the opportunities of a full life."); *S. Rep. 94-589*, 94th Cong. 3 (1976).
[324] *See, e.g.*, *Hearings on S. 483, S. 1900, S. 1927, S. 1961, and H.R. 5616 Before the Subcommittee on Consumer Affairs of the Senate Comm. on Banking, Housing, and Urban Affairs*, at 5 (statement of Senator Brock) (stating that he would not expect a mortgage lender to grant an 85-year-old a 30-year mortgage).
[325] *Id.* at 1 (statement of Senator Biden); *id.* at 6 (statement of Senator Brock).
[326] *Id.* at 6 (statement of Senator Brock).

enterprise system" for which intervention could be warranted.[327] J. Stanley Pottinger, the Assistant Attorney General for the Department of Justice's Civil Rights Division, also noted that prohibiting discrimination could help reduce the risk that banks would be used as a tool for coercion or retribution. Pottinger noted that "if . . . governments or companies were to coerce banks in which they have large deposits into refusing to make loans to . . . businessmen, [amending ECOA] would protect such businessmen by prohibiting such banks from refusing to make loans on the basis of religion or national origin."[328]

The 1976 amendments to ECOA originally included political affiliation as a protected class.[329] Numerous credit providers and government witnesses testified that political affiliation was not a legitimate criterion for determining creditworthiness;[330] the representative of the American Bankers Association said that discriminating on the basis of political affiliation would "run counter to the basic purpose of a financial institution."[331] However, the consensus among

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[327] *Id.* at 347 (statement of Stephen S. Gardner, Deputy Secretary of the Treasury).
[328] *Id.* at 7; *id.* at 332 (statement of J. Stanley Pottinger, Assistant Attorney General, Civil Rights Division, Department of Justice).
[329] S. 1927, 94th Cong. (1975) (statements of Senator Biden and Senator Proxmeier).
[330] *See, e.g.*, *Hearings on S. 483, S. 1900, S. 1927, S. 1961, and H.R. 5616 Before the Subcommittee on Consumer Affairs of the Senate Comm. on Banking, Housing, and Urban Affairs*, at 216–17 (statement of Sheldon Feldman, Assistant Director for Special Statutes, Federal Trade Commission) (supporting barring discrimination on the basis of political affiliation because "the use of such group generalizations denies the applicant the opportunity to be evaluated solely on the basis of his or her personal financial situation"); *id.* at 332–33 (statement of J. Stanley Pottinger); *id.* at 361–62 (statement of John A. Dillon, Executive Vice President, National BankAmericard, Inc.) (noting that political affiliation was not "a relevant factor to consider in evaluating an application for a bank credit card" and that while National BankAmericard was unaware of any example of that happening and therefore opposed the inclusion of the provision, they would be "happy to reconsider this position in the event that the record demonstrates that applicants have been treated arbitrarily because of political affiliation"). *But see id.* at 634 (statement of Max Whitmore, Manager Credit Policy & Control, Standard Oil) (stating that while calling the idea of denying credit solely the basis of the borrower having a political affiliation with beliefs contrary to Standard Oil would be "unconscionable," the law should not prevent credit providers from denying credit "to a potential customer who would use the credit in a manner disadvantageous to the credit grantor or to the United States," specifically in the case of "anti-democratic customers").
[331] *Id.* at 263 (statement of Forrest D. Jones, Executive Vice President, Fidelity Bank, Oklahoma City, on behalf of the American Bankers Association).

witnesses was that discrimination on the basis of political affiliation simply did not happen and that therefore the provision should be removed, which it was.[332]

The ECOA amendments reflect a recognition that access to credit, one of the core banking services, is essential to functioning in a modern economy, and that losing access to it can have a deleterious effect on a business or individual. However, the supporters of amending ECOA also acknowledged that lenders are legitimately profit-seeking firms that operate in a fairly (if not perfectly) competitive market. Therefore, rather than seeking to turn lenders into utilities, the law sought to remove some decision criteria believed to be not legitimately related to creditworthiness and profitability, while otherwise allowing lenders to decide how to allocate their lendable funds to maximize profits and avoid risk.

The debate around both whether banks should be public utilities and what criteria they should be allowed to use when making decisions about whether to provide services reflects real concerns about the need for banking services, the nature of the market for those services, and the role that government-granted privilege plays in that market. These dynamics should perhaps give us pause when banks seek to use their power to influence others to adopt the banks' preferred policies by threating to cut off access to services. Assuming arguendo that the public policy supporting banks is justified by legitimate concerns such as safety and soundness, strengthening the banks' ability to coerce others is still an unintended consequence worth considering. However, addressing this concern does not necessarily require more government control, as will be discussed below.[333]

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[332] *See, e.g.*, *id.* at 263–64 (statement of Forrest D. Jones); *id.* at 361–62 (statement of John A. Dillon); *id.* at 620 (statement of Robert B. Norris, General Counsel, National Consumer Finance Association). *See also* Scagnelli, *supra* note 321, at 388 n.23.
[333] *See infra* Section III.A.

III. How to Address Banks Acting as Regulators

Banks' inclination to use government-granted power to force a change in consumer or firm behavior is potentially problematic. It allows certain institutions to turn insulation from market competition, protection from failure, and government-provided services that were intended to facilitate lawful commerce on their head, denying citizens the benefit of the bargain that has been struck with banks and potentially forcing citizens to "feed the hand that bites them."[334] This results in people being de facto regulated by publicly provided power without the substantive and procedural safeguards and political legitimacy expected from regulation. But if this is a problem, what is the solution? This section suggests some answers.

Before we get to the proposed solutions, we should acknowledge that there is a countervailing value at play—freedom of association. The ability to associate with the causes one believes in, and to avoid associating with those one does not, is an important freedom.[335] This freedom should not be forsaken simply because the people who seek to exercise it have adopted a corporate form.[336]

It should be noted that, owing to the unique nature of banking as a business, it may be tricky to determine the person or people whose preferences for association should be considered relevant. For example, should depositors' preferences matter? And, if so, should they matter only with regard to loans that are funded by depositors? The question is especially tricky if the bank is

[334] This is a paraphrase of a statement found in the obituary of Prof. Norman Stone. Richard J. Evans, *Norman Stone Obituary*, THE GUARDIAN, June 25, 2019, https://www.theguardian.com/books/2019/jun/25/norman-stone-obituary.
[335] Richard A. Epstein, *Public Accommodations Under the Civil Rights Act of 1964: Why Freedom of Association Counts as a Human Right*, 66 STAN. L. REV. 1241, 1247–49 (2014) (discussing the importance of freedom of association in a free society).
[336] Burwell v. Hobby Lobby Stores Inc., 134 S. Ct. 2751, 2768 (2014) (discussing how rights enjoyed by corporations are actually rights enjoyed by the people who own and work for those corporations).

also a publicly traded corporation.[337] Still, freedom of association is meaningful and should, to the greatest extent possible, be respected.

However, as we discussed above,[338] banks and the regime of privilege they enjoy may present a unique situation because of the public policy that distorts the banking market, imposes barriers to entry, provides the advantage of access to government-provided services, and grants banks more market power than they would likely have otherwise. It is this type of distortion that even strong advocates of freedom of association acknowledge can militate toward limiting that freedom.[339]

Further, as discussed below,[340] to the extent that public policy grants banks protection and privilege for the purpose of achieving certain ends, it may be reasonable and appropriate to condition those grants to ensure that the desired ends are actively achieved and not actively obstructed. However, any conditions should be the least onerous required to ensure that the grants of privilege and protection are not misused.

It is with these challenges in mind that we propose some potential solutions to the problem of banks acting as de facto regulators. Our primary goal is to find a solution that allows banks to exercise freedom of association without allowing them to use power that is augmented by public policy to pursue their own regulatory desires. In a perfect world, this would likely

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[337] Should it be the bank's management? Its shareholders (and, if so, all of them or simply a majority)? Its depositors, who provide much of the money the bank uses? *See id.* at 2774 (discussing how to determine whose preferences should hold in assessing questions related to the Religious Freedom Restoration Act and the practical restraints on public companies exercising those preferences).

[338] *See supra* Sections I, II (where we talk about how banks are supported and why it is bad for them to then regulate).

[339] *See* Epstein, *supra* note 335, at 1250–53 (discussing the regulation of common carriers). To be clear, we do not claim that Professor Epstein would agree that banks qualify in this context, we argue simply that he acknowledges that less-than-competitive markets can provide a basis for limiting freedom of association in some cases. *See also* Thomas P. Nachbar, *The Public Network*, 17 COMM. L. CONSPECTUS 67, 93–94 (2008) (discussing how common carrier designations driven by government-granted monopolies or franchises were viewed less skeptically by legal conservatives in the "public interest" era).

[340] *See infra* Section III.C.

involve removing government support for banks entirely, as well as removing barriers to entry for banks. However, we acknowledge that practical and political realities may preclude that, so we include some options that we view as suboptimal but perhaps more feasible.[341] Many of these solutions would likely require congressional or federal regulatory action. However, states are also involved in bank regulation, including in chartering and establishing antidiscrimination requirements, so states can play a role if they choose.

It is important to note what the reforms proposed below would not do. They would not prevent banks from acting as "responsible corporate citizens" or engaging in the political process. They would do nothing to limit banks' ability to advocate for policy change or sponsor causes they believe in using corporate profits, and any attempt to impose such limitations would likely be unconstitutional.[342] Likewise, they would not condition access to government-provided services on banks' endorsement of positions they disagree with, which would also likely be unconstitutional.[343] They would not resort to technicalities or unrelated points of leverage to justify limiting banks' discretion, such as claims that because banks benefit from roads and a police force they are subject to government control.[344] Rather, these reforms would limit the use of government-granted power to prevent it from being used in ways arguably contrary to the reasons the power was granted in the first place. Banks would and should remain free to use persuasive means of advocacy to convince citizens that policies should be changed. However,

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[341] We also note that this section does not touch on how to address a scenario in which a bank obtains outsized market power in a free market. Whether it would be appropriate to infringe on such a bank's freedom of association, and, if so, how, is beyond the scope of this paper.
[342] Citizens United v. Fed. Election Comm'n, 558 U.S. 310 (2010).
[343] Agency for Int'l Dev. v. Alliance for Open Soc'y Int'l, Inc., 570 U.S. 205 (2013) (holding that conditioning a government grant on a requirement that an organization have a policy opposing prostitution "compels as a condition of federal funding the affirmation of a belief that by its nature cannot be confined within the scope of the Government program" and that "[i]n so doing, it violates the First Amendment and cannot be sustained").
[344] Thomas P. Nachbar, *The Public Network*, 17 COMM. L. CONSPECTUS 67, 94 (2008) (discussing how "quid pro quo" theory of common carrier status could lead to any firm that uses roads being swept up).

this would not include withholding services to force a change in consumer or firm behavior based on the banks' policy preferences.

A. Remove, or at Least Minimize, Government-Granted Privilege for Banks

One solution that would resolve the conflict between banks' freedom of association and their arguably inappropriate use of publicly granted power is to remove the publicly granted power. If we strip away the government supports that distort the market and force banks to operate in a free market for banking services, we can be confident that when a bank seeks to influence others, the power it uses was earned by the bank itself by virtue of the quality of its service.[345] This solution may be politically unlikely, but it would resolve the present question in a way that maximizes the values of freedom of association and freedom from inappropriate de facto regulation.

This solution has several advantages, including a freer market, significantly less moral hazard, and no danger that publicly provided power will be turned against the public. However, it is also a dramatic change from current reality, and we acknowledge that the U.S. financial system is the way it is because many people believe the current policy was the best option available to address real concerns.[346] While "you can't get an *ought* from an *is*," we accept that such a drastic change to the current regulatory environment is unlikely to occur and may be undesirable for other reasons. However, there is another path to effectively remove government-granted advantage: dramatically expand access to it.

An advantage held by all competitors is no advantage at all. If we are unwilling to remove the government-granted advantages for banks, we could make it easier for firms that

[345] Whether banks and the services they provide are so essential that banks should be allowed to attempt to de facto regulate even in a free market is beyond the scope of this paper, but it is an important question worthy of further research.
[346] Again, whether current banking policy is optimal is beyond the scope of this paper.

want to compete in the banking services market to obtain the same advantages. Lowering barriers to entry to obtain a bank charter and FDIC insurance to no higher than is absolutely necessary and removing discretion (thereby limiting incumbents' ability to lobby against entry) would help improve competition and weaken any excess market power enjoyed by incumbents.

A complementary path would be to equalize the treatment of banks and their nonbank competitors. For example, nonbank lenders could be granted the ability to lend nationwide on the basis of their home state's laws governing interest and their home state lending license, and nonbank money transmitters could be granted the ability to act nationwide via either a federal money transmission license or forced passporting of their state license.[347] Likewise, the Fed, with congressional assistance, could open the payments system it runs to nonbanks that meet appropriate safety requirements. The United Kingdom[348] and Hong Kong[349] have already opened their payments systems to nonbanks in the interests of competition.

The benefit conveyed by FDIC deposit insurance could also be at least somewhat mitigated by requiring banks to hold a higher capital ratio. This would likely help reduce the risk of a banking crisis and mitigate the risk of failure or the insurance fund needing to be tapped in the event of failure.[350]

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[347] For further discussion of how to equalize the treatment of bank and nonbank lending and money transmission, see Knight, *supra* note 85, at 199–204; *see also* Brian Knight, *Modernizing Financial Technology Regulations to Facilitate a National Market* (Mercatus Ctr. at George Mason Univ., Mercatus on Policy, Aug. 1, 2017), https://www.mercatus.org/publications/financial-markets/modernizing-financial-technology-regulations-facilitate-national.
[348] Ana Nicolaci da Costa, *Britain Will Open Payments System to Non-banks, BoE's Carney Says*, REUTERS, June 17, 2016, https://www.reuters.com/article/uk-britain-boe-fintech-payments-idUKKCN0Z311Z; *TransferWise Becomes First Non-bank to Open Settlement Account with BofE RTGS*, FINEXTRA, Apr. 18, 2019, https://www.finextra.com/newsarticle/31969/transferwise-becomes-first-non-bank-to-open-settlement-account-with-bofe-rtgs.
[349] HONG KONG MONETARY AUTHORITY, FASTER PAYMENT SYSTEM (FPS) (Sept. 28, 2019), https://www.hkma.gov.hk/eng/key-functions/international-financial-centre/infrastructure/faster-payment-system.shtml; J. P. Koning, *Should Central Banks Lock Out Non-bank Payment Providers?*, AIER (Jan. 15, 2019), https://www.aier.org/article/sound-money-project/should-central-banks-lock-out-non-bank-payment-providers.
[350] *See, e.g.*, James R. Barth & Stephen Matteo Miller, *Benefits and Costs of a Higher Bank Leverage Ratio* (Mercatus Ctr. at George Mason Univ., Mercatus Working Paper, 2017), https://www.mercatus.org/publications/benefits-costs-bank-leverage-ratio.

However, this option is not without its problems. These proposals would likely be met by vicious lobbying that could result in suboptimal results. Bailouts likely present the most challenging issue, since bailing out every bank and bank competitor that might fail is neither desirable nor feasible, but access to bailouts has provided real advantage to firms lucky enough to enjoy it. This may be the most intractable problem, which may strengthen the argument that banks likely to receive a bailout need to have their freedom of association curtailed to compensate for the real or perceived likelihood they will receive extraordinary government support in the event of a crisis.

B. Condition Access to Benefits on Political Neutrality (but Also Allow Alternatives)

If uprooting the system or throwing it wide open are not feasible solutions, the question must be what changes can be made within the confines of the current system. The obvious answer is that the government should condition the support it provides on banks forswearing the use of that support as a tool to impose de facto regulation. Banks would not necessarily have to avoid using their market power to try to regulate, but they could not do so using government-provided power. Banks that chose to pursue de facto regulation would need to use private suppliers of services instead of the government.

As a practical matter, this would introduce more complexity than the solutions proposed above because the government would need to define when a bank's actions constitute an attempt to regulate—but this challenge is not insurmountable. This solution would also require changes to the law to make it easier for banks to use private alternatives to government-provided services. Finally, there is a risk that any changes within the current system would be insufficient to address the misuse of government-granted privilege.

Many of the ways in which the government supports banks involve the government as a service provider. For example, the FDIC serves as the banks' insurer and the Fed acts as a provider of payments system services. Those services, or equivalents, could be obtained via the private sector. For example, the Clearing House, a private organization owned by a consortium of large banks, runs several payments systems used by banks that compete and coexist with the Federal Reserve.[351] Likewise, banks could substitute federal deposit insurance for private insurance or alternative risk mitigation schemes such as hedging or maintaining high capital buffers.

To prevent government support from enabling banks to appoint themselves as regulators, the government could condition access to support on a requirement that the bank does not attempt de facto regulation and enforce this requirement through either fines or withdrawal of access to the relevant service. Defining what counts as attempting de facto regulation may prove challenging. It could be defined by prohibiting banks from making decisions on the basis of certain criteria, such as how the decision is likely to shape a downstream market or limit access, directly or indirectly, to certain legal goods or services. It could also be defined by limiting the *scope* of acceptable decision-making criteria. For example, a bank could be required to justify its decision on the basis of profit and loss, repayment risk, and so forth.

Conditioning access to government support looks more like current antidiscrimination laws that apply to credit providers, such as ECOA,[352] than like the duty-to-serve requirement that comes with being a public utility.[353] Antidiscrimination law does not prevent a bank from denying service to a customer; it simply limits the criteria the bank can use to determine whether

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[351] *See* The Clearing House, *Payments Systems*, https://www.theclearinghouse.org/payment-systems (last visited Aug. 17, 2019).
[352] *See, e.g.*, 15 U.S.C. § 1691 *et seq.* (2019); *see also supra* Section II.B.2.
[353] *See supra* Section II.B.2.

it will deny service by excluding protected classes from the scope of legitimate variables.[354] This is not a proposal to make banks public utilities and require them to offer services universally. Banks under this regime would be allowed to deny credit or other services on the basis of traditional business considerations, including profit maximization and loss minimization. Banks would be able to refuse to serve customers they find politically distasteful, but not on the basis of that distaste. This is important, because—as discussed above—it is essential that banks exercise discretion when providing services, both to protect the safety and soundness of the system and, in the case of credit, to allocate capital to its most productive ends *as indicated by the market*. However, just as it is inappropriate for banks to take notice of protected-class categories like sex and race, it may be inappropriate for them to view service provision decisions as a tool of de facto regulation.

This conditioning of access to government services would constitute a significant restriction on banks' autonomy, but they could escape the requirement by opting to use private services instead. A piece of legislation in this vein has been introduced by Senators Kevin Cramer (R-ND), John Kennedy (R-LA), and James Inhofe (R-OK). The "Freedom Financing Act"[355] would prohibit banks and credit unions with over $10 billion in total consolidated assets that refuse to do business with lawfully licensed firearms manufacturers, importers, and dealers for "political or reputational considerations" from accessing the Fed's discount window or automated clearing house network.[356] While this bill seeks to sever government-granted power from banks' attempts to de facto regulate, it is too limited to properly address the issue

[354] It should be noted, however, that while antidiscrimination law is meant to eliminate conduct that is bad without regard for whether the government enables it, this provision seeks to remove an unintended and inappropriate use of government power for conduct that is otherwise generally, though not necessarily always, unobjectionable in and of itself.
[355] S. 821, 116th Cong. (2019–2020).
[356] *Id.*

because it applies only to banks that refuse to do business with firearms businesses instead of applying generally.

Although conditioning access to government benefits, while allowing alternatives, is attractive in that it allows for pluralism, it also presents some significant challenges. As discussed above, definitional issues would be tricky, though likely not impossible to overcome. Another challenge would be assessing the adequacy of the alternative services, especially where the alternative services have implications for consumer protection or safety and soundness. For example, ensuring that the deposit insurance equivalent is adequate would require the banks' regulators to do a different type of analysis than they do currently. It is also possible that private mechanisms may be less effective in satisfying the primary purpose that gave rise to the government-granted support in the first place, frustrating the broader intent of the regulation. Conversely, it is possible that the private sector could provide better services than the government.

There are also reasons to doubt that conditioning government benefits would be sufficient. While some government-granted advantages lend themselves to clean exclusion and substitution, others do not. Bank charters still pose a significant barrier to entry and open the door to valuable regulatory benefits[357] separate and apart from the government-provided services, so this option may not be sufficient. Likewise, as described above,[358] the bailout question remains challenging if not intractable. Therefore, it is not clear that conditioning government benefits would sufficiently mitigate the potential abuse of government-granted privilege that banks enjoy.

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[357] *See supra* Section I.A.1.
[358] *See supra* Section II.A.5.

C. Prohibit De Facto Regulatory Considerations from Decision-Making

We now turn to the potential solutions that provide the least amount of space for freedom of association: these options are fairly restrictive and should not be considered lightly. They include conditioning becoming or remaining a bank, or providing banking services, on abstaining from attempting to de facto regulate when considering whether to provide services. This could be done by conditioning the granting or retention of a charter or by regulating specific services such as credit provision or money transmission; such restrictions would be akin to laws that prohibit discrimination in the provision of credit on the basis of protected characteristics.[359] The State of Georgia already does this in the context of firearms by prohibiting banks from denying firearms firms service on the basis of the firms' line of business.[360] Conditioning the granting of a charter on not seeking to de facto regulate would limit the scope of this requirement to chartered banks. Conversely, regulating service provision would likely apply the requirement more broadly, sweeping in market participants that do not receive the same government-provided benefits banks enjoy. Therefore, the justification for conditioning the ability to provide services may be weaker than for conditioning access to a charter.

These solutions have the virtue of simplicity and would address the outstanding concerns posed by the other proposed solutions since they would constitute, in one sense at least, a relatively minor change from the status quo: U.S. law already limits banks' discretion in the criteria they use when deciding whether to provide services. The definitional challenges discussed above would apply but would likely not be insurmountable. This solution would also address the concerns about bailouts because all banks, large and small alike, would be limited in

[359] *See, e.g.*, 15 U.S.C. § 1691 *et seq.*; *see also supra* Section II.B.
[360] GA. CODE ANN. § 10-1-439.2 (2019); *see also* Josh Blackman, *Four Problems with Citi's U.S. Commercial Firearms Policy* (Mar. 23, 2018), http://joshblackman.com/blog/2018/03/23/four-problems-with-citis-u-s-commercial-firearms-policy/.

their conduct. Finally, this bright-line rule could help prevent banks from becoming conduits of coercion. As Assistant Attorney General Pottinger highlighted, there is a risk that parties with leverage over a bank will seek to use banks as a tool to harm interests indirectly that they may not be able harm directly.[361] This has arguably occurred in the infamous "Operation Choke Point" and other recent episodes.[362] This threat is not limited to regulators, however. As Pottinger alluded to, private actors could also pressure banks to cut off services to lawful firms disfavored by those private actors. The countries and firms that Pottinger worried would coerce banks had no direct regulatory control over banks, but they could use the threat of diminished profitability to encourage banks to cut off services. If it is illegitimate to allow banks to become a tool for coercion against legal but disfavored businesses, a bright-line prohibition could help prevent this from occurring.

However, a bright-line prohibition is also the most restrictive and least flexible option. Therefore, it should be considered the last resort. This is true because, as we acknowledged above,[363] this is a case where freedom of association butts up against the idea that banks should not be able to use government-granted privilege to act as de facto regulators. There may be cases where the balance of equities tips toward freedom of association: when (1) the freedom of association interest is very strong (it matters a great deal to the relevant decision makers), clear (it is well defined and articulated), and uniform within the bank, and (2) the government-granted privilege is minimal and has minimal effect. For example, consider a small, closely held bank where all the owners and depositors agree on a certain set of values and where the bank does not

[361] *See supra* Section II.B.2.
[362] *See generally* Julie Andersen Hill, *Regulating Bank Reputation Risk*, GA. L. REV. (forthcoming), https://ssrn.com/abstract=3353847.
[363] *See supra* Section III, the opening paragraph.

receive much government support and has very little government-granted market power within the relevant market.[364]

D. Do (Almost) Nothing

Of course, if one does not believe that banks' receipt of significant government-granted privilege is overly problematic, or if one believes that any cure would be worse than the disease, the logical response would be to do nothing. However, even in this scenario the interests of honesty and transparency seem to indicate that banks should be explicitly allowed to act as de facto regulators. Many of the powers and privileges granted to banks were granted using the justification that banks are necessary to empower consumers and businesses to engage in lawful commerce.[365] If instead policymakers wish to empower banks to serve as de facto regulators, they should make that wish explicit.

IV. Conclusion

Whether banks must be "special" is open to question. However, it is clear that public policy makes banks different from many other industries. Banks enjoy government-granted privileges and protections that help insulate them from market forces and competition. A side effect of this situation is that banks could use that power to restrict commerce beyond their mandates, acting as de facto regulators.

There are reasons to believe that this should give us pause, because—as this paper argues—the ability to act as a de facto regulator is not the reason banks were empowered by law,

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[364] However, it should be noted that even small banks can be powerful in their relevant market. *See, e.g.*, Ruth Simon & Coulter Jones, *Goodbye, George Bailey: Decline of Rural Lending Crimps Small-Town Business*, WALL ST. J., Dec. 25, 2017, https://www.wsj.com/articles/goodbye-george-bailey-decline-of-rural-lending-crimps-small-town-business-1514219515.

[365] *See supra* Section II.A.

and it may be inconsistent with the purpose of that empowerment, which was to the facilitate lawful commerce. Further, banks' importance and the fact that consumers may not be able to participate in a free market, in part because of regulation, become problematic when banks take actions that amount to de facto regulation. Therefore, it may be reasonable to curtail banks' use of publicly granted power to further a de facto regulatory agenda. This paper suggests a nonexhaustive list of potential options for policymakers to consider.