

A Comparative Communication Discourse Analysis
Examination of the Economic Crisis of 1929 and the Mortgage Crisis of 2008
Through the Analysis of Mainstream and Alternative Media Discourses

by
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ABSTRACT

The economic crisis in 2008 triggered a global financial shockwave that left many wondering about the origins of the crisis. Similarly, in the early twentieth century, Wall Street faced catastrophic losses that set the stage for the Great Depression, which resulted in a decade of economic depression, leaving millions of people out of work. Using discourse analysis to understand how economic crisis is framed through the mainstream press, this research project analyzed the stock market crash of 1929-1932 and the mortgage-backed financial crisis of 2007-2009 through the lens of two mainstream publications, *The New York Times* and *The Wall Street Journal*. Comparative analysis focused on explanations for the causes of the crises, attributions of blame, culprits, and proposed solutions emerging in news coverage of the 1929 panic and the 2007-2009 financial crises. Mainstream media accounts of the 2007-2009 crisis are then compared with ‘alternative media’ accounts of crisis causes, culprits, and solutions. These comparative analyses are contextualized historically within economic paradigms of thought, beginning with the classical economists led by Adam Smith and transitioning to the Chicago School.

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CHAPTER ONE

OVERVIEW OF THE PROJECT

The financial crises of 1929 and 2008 shook the entire global economy. Yet, the causes of these crises, the agents involved, and the solutions remain contested in academic scholarship and public discourse. Therefore, the purpose of this thesis is to analyze mainstream media framing of the two financial crises' causes, culprits, and solutions by analyzing and comparing news coverage of each crisis provided by *The New York Times* and *The Wall Street Journal*. The limits of mainstream news media frames of the 2007-2009 crisis are revealed by comparison with alternative problem-solution frames for the crisis found in alternative media. Through these comparative analyses, this thesis extends knowledge of how media help set public and government agendas and policy orientations by shaping public interpretations of critical issues.

This project ultimately adopts a critical orientation to mainstream media's role in shaping representations of, responsibility for, and reform of financial misconduct. Careful analysis of *The New York Times* coverage of causes and culprits of the 1929 crisis suggests that press coverage of criminal misdeeds and Pecora Commission findings played a role in building support for strong regulatory action, leading to passage of the Glass-Steagall Act of 1933. In contrast, analysis of media coverage of the 2008 crisis by *The New York Times* and *The Wall Street Journal* indicates that stories de-emphasized criminal acts and problem-solution frames, thereby undercutting critical demands for a strong regulatory response by the U.S. government, although both newspapers acknowledged that repeal of Glass-Steagall was one of the major contributions to the

2008 meltdown. Consequently, the United States government had little mainstream media opposition to its unprecedented bailouts of financial institutions using taxpayer money (Crawford, 2011) and has faced relatively little public pressure for massive regulatory reforms, such as breaking up the large banks and prosecuting financial wrongdoings as criminal offenses.

This thesis's expanded analysis of the contemporary media environment suggests audiences wanting more critical coverage of 2008 crisis causes and culprits must turn to the alternative press, including the Internet blogosphere. Content analysis of popular alternative media reveals greater willingness than the mainstream press to investigate criminal wrongdoings and to call for strong regulatory action. The alternative media are especially more willing to interview interviewees and to report on their activist activities.

Project Background

The 1929 crisis resulted in the 1932 Pecora Commission investigation and subsequent prosecution of high-level banking executives like Charles Mitchell of National City Bank, considered the second-largest bank in the United States. These events paved the way for passage of the 1933 Glass-Steagall Act, which imposed a stringent regulatory framework on the nation's banks. The repeal of the Glass-Steagall Act in 1999 by the Clinton Administration with the Gramm-Leach-Bliley Act in 1999 was instrumental in the creation of the subprime-loans bubble, which turned out to be the driving force behind the financial panic of 2007-2009. Until its repeal, the Glass-Steagall Act prevented many of the irresponsible banking practices that eventually contributed to

the stock market crash that began in late 2007. For example, the banking system set up by Glass-Steagall discouraged risky loans. According to Frank Shostak, the year before the repeal of Glass-Steagall in 1999, subprime loans were approximately 10 percent of all mortgage lending (Shasta, 2010). However, post-repeal of the Glass-Steagall Act, by 2005, the percentage doubled as it was approaching twenty-one percent.

Yet, the 2007-2009 financial meltdown has not yet resulted in any criminal prosecution of high-level banking executives, nor has it resulted in the re-instatement of Glass-Steagall. Moreover, no new regulatory frame with the scope of Glass-Steagall has been implemented. The data from this thesis suggest that the lack of regulatory response may be partly a function of media framings of the 2007-2009 crisis in relation to “complexity” and “systemic risk,” in comparison to the theme of “criminality” that emerges in media coverage of the 1932 Pecora Commission findings. Thus, the themes emerging from media framing of financial crises may shape public demands for justice and government legislative and executive responses.

The mainstream media reports analyzed in this project were taken from *The New York Times* in 1929 and the early 1930s and *The Wall Street Journal*, and *The New York Times* for the contemporary crisis from 2007-2009. Coverage by *The New York Times* in 1929-1932 is compared with coverage of the 2007-2009 crisis by both *The New York Times* and *The Wall Street Journal*. Content analysis reveals that in 1929 the media were more likely to represent financial misdeeds as criminal behavior, but were less likely to promote regulations as the solution to the crisis until the Pecora Commission findings were publicized. *The New York Times* then adopted a more proactive regulatory stance. In contrast, during the 2008 crisis, the mainstream media quietly recommended re-

establishment of the Glass-Steagall Act, but were less likely to represent the causes of the crisis as criminal in nature. In 2008, both *The New York Times* and *The Wall Street Journal* were more likely to blame the complexity of the system, than the criminality of the industry.

The tepid and technically-detailed accounts of causes and culprits of the 2007-2009 crisis found in *The New York Times* and *The Wall Street Journal* are then compared with the more highly-charged and accusatory accounts and themes found in alternative media. Discourse analysis of news reports and interviews found on popular financial blogs and sites reveals a greater willingness to assign blame and demand strict regulatory response in alternative media accounts. Moreover, the alternative media accounts evidenced greater engagement with the criminal aspects of the financial risk instruments (e.g., derivatives) at the heart of the 2007-2009 meltdown.

The methodology for these analyses is based on qualitative research using discourse analysis of media accounts describing, comparing, and contrasting the two historic crises that occurred in 1929 and 2008. Discourse analysis is a qualitative method that examines what can be spoken about and how and what cannot be spoken about (Hjort, 2005). Themes emerge from careful readings of articles in a “grounded fashion.” Themes are not counted but rather are interpreted by focusing on the semantics of their language, the use of metaphor and symbolism, and their implicit worldviews. Textual data from original sources are used to illustrate and document the interpretive argument made by the critic.

The New York Times and *The Wall Street Journal* were analyzed due their prominent reputation throughout the world. The stories were accessed and analyzed

digitally using uploaded versions of *The New York Times* and *The Wall Street Journal* available through university databases, including ABI/Inform and LexisNexis. Searches using multiple sources and databases provided a well-rounded investigation of the communication issues and the media reports, as well as enabling insight into the government actions that affected the American economic landscape. Alternative media were found using Internet searches and by examining popular online financial websites, such as Zero Hedge. Sites were selected based on their high ranking within Google search results for searches such as “financial crisis” and “causes.”

Background of the Great Depression and the Great Recession

President Herbert Hoover traveled to the industrial state of Michigan to acknowledge the progress of America, especially to business people and scientists (Foner, 2005). On October 21, 1929, President Hoover stated, “We gain constantly in better standards of living, more stability of employment . . . and decreased suffering.” Despite the positive rhetoric from President Hoover, three days later, Wall Street experienced the stock market crash of 1929. It was the most catastrophic financial crash in the history of the United States. As panic set in, more than \$10 billion in market value, which is equivalent to over ten times that amount in today’s money, vanished in a span of five hours (Foner, 2005). Undoubtedly, the economic panic collapsed global financial activities.

Even though the stock market crash in 1929 was not the first financial panic in the United States, the Great Depression became a worldwide economic collapse by all

Western world establishments. At the end of the “Roaring Twenties,” the United States became the main source that triggered the Great Depression, resulting in extreme downturn in outputs, unemployment, and acute deflation on a global scale (Romer, 2003). Still considered as the worst economic crash in history, multiple factors such as diminished consumer demand, misled governmental policies, and financial fraud all contributed to the Great Depression, which endured for more than a decade (Romer, 2003). Four years after the crash, the market hit its trough (lowest point of a business cycle) as the world’s industrial production dropped approximately 67% in just four years after Black Tuesday, skyrocketing unemployment rates in the United States to 13 million people (Chamber et al., 1983).

In 1933, the newly appointed President Franklin Delano Roosevelt made efforts to regain the public’s confidence. The situation was so out of control that banking activities were suspended in majority of the states, meaning the public could not gain access to their bank accounts (Foner, 2005). In June 1933, the United States Congress passed the Banking Act of 1933, otherwise known as the Glass-Steagall Act. The main architects, Senator Carter Glass from Virginia and Representative Henry Steagall from Alabama, drafted the bill. The Glass-Steagall Act of 1933 created a separation between commercial and investment banks in the financial sector (Sherman, 2009). Without much choice, banks were forced to pick between acting as a commercial bank, mainly composed of holding deposits and making loans, or as an investment bank, which conducted securities transactions (Crawford, 2011). This was an emergency response to the crisis as approximately 5,000 banks during the Great Depression collapsed (Glass-Steagall act, 1933). The act provided strict regulations, forcing national banks to the Federal Reserve

System that prohibited bank sales of securities. Along with the banking legislation, the Glass-Steagall Act created the Federal Deposit Insurance Corporation (Glass-Steagall act, 1933), which insures bank deposits with a pool of money appropriated from banks (Crawford, 2011). In other words, the FDIC insured bank deposits of commercial banks in return for insurance protection as the Federal Reserve Bank's control over commercial banks tightened (Crawford, 2011).

Despite harsh criticisms from the banks, the Glass-Steagall Act regained the public's trust in the American financial system. Its main goal was to lay a new foundation to bring stability to the American economic system, particularly the banks. After the implementation of the Glass-Steagall Act, banks experienced occasional failures, but the depositors mostly walked away unscathed (Foner, 2005). Confidence in the stock and bond markets slowly recovered, eventually regaining trust and confidence. Not only the investors in the United States recovered, but also the international market took notice of the economic recovery as the U.S. financial system recovered (Crawford, 2011).

However, over time the Federal Reserve reconstructed certain portions of the Glass-Steagall Act by allowing banks to earn revenues from securities transactions. From the 1980s to 1996, the percentage increased from 5% to 25% of banks earning their revenues from securities transactions (Frank, 2010). In 1999, the final process of repealing the Glass-Steagall Act took place when the United States House of Representatives and Senate in an overwhelming fashion voted to abolish the firewall that separated the commercial banks from the investment banks. The U.S. Senate voted 90 to 8 and the House voted 362 to 57 as all of Congress was in favor of repealing Glass-Steagall (LaBaton, 1999). In its place, Congress was in favor of passing the Gramm-

Leach-Bliley Act of 1999 that rescinded the Glass-Steagall Act's control on banks and securities (Obama takes on banks with new glass-Steagall act, 2010). On November 1999, President Bill Clinton approved the Gramm-Leach-Bliley Act by signing the bill into law. Feeling obsolete, the legislation no longer deemed appreciate: "Glass-Steagall was no longer appropriate to the economy in which we live. It worked pretty well for the industrial economy, but the world is very different" (Frank, 2010).

Since the crisis of 2008, some critics have suggested revisiting the idea of reviving the Glass-Steagall Act or implementing a similar plan that introduces new regulations for the banking industry to avoid excessive speculation (10 years later, looking at repeal of Glass-Steagall, no date). In 2010, former Chairman of the Federal Reserve Board, Paul Volcker, introduced what is perceived to be the modern-day Glass-Steagall Act. Instead of re-approving of the old policies from the 1930s that separated the commercial and investment banks, the Volcker Rule, on paper, prohibits banks from proprietary trading, running hedge funds, and making private equity investments or using money to make bets on the financial market (Sweet Jr. & Christiansen, no date).

However, Wall Street and the United States financial landscape have immensely changed since the implementation of the Glass-Steagall Act. The Volcker Rule of regulating the banks has led to some modifications to the current market system; however, the new regulations fail to account for illegal trading activities through the electronic processors and computers that allow for market manipulation. Financial activities such as re-hypothecation, quote stuffing, credit default swaps, high frequency trading, and naked short selling, etc. significantly manipulate the global markets. These financial practices are rarely communicated to the public. The analysis of the alternative media accounts

reveal the limitations of the Volcker proposal and similar regulatory frameworks because of failures to address problems in the financial operations that are rarely mentioned in the mainstream media accounts, although widely recognized and discussed in alternative media accounts. Therefore, this project not only investigates the contemporary culture of Wall Street, but it advocates for regulating mischievous and often fraudulent trading practices that occur in secrecy. The communication messages pertaining illegal trading in the United States financial system is essentially absent for the public to acknowledge.

Overview of the Upcoming Chapters

Chapter 2 details some of the historical economic landmarks in chronological order to help the reader understand the history involving governmental regulations. Adam Smith and other classical economists from England and France radically shifted from the state's economic system of mercantilism to laissez-faire economics that advocated for the utmost economic freedom. This philosophy of laissez-faire carried on in the United States during the 1800's with the booming industry of the railroad expansion pre and post Civil War. By the late nineteenth century, small to medium sized businesses in the United States experienced heavy consolidations, thus giving birth to modern corporations with little to no regulations. This style of laissez-faire economics brought financial prosperity during the "Roaring Twenties," but it also paved a path toward the biggest economic collapse in financial history. In response to combating the problems, the newly appointed Roosevelt Administration implemented legislations such as the Glass-Steagall Act that downsized the banks. With the Western economies adopting the economic philosophy of

John Maynard Keynes, the Keynesian revolution became the hegemonic solution to economic instability.

Chapter 3 is a continuation of the economic history starting in the 1970's with the rise of Chicago School of Economics led by Milton Friedman and George Stigler. This particular school of thought revived the old economic philosophy of laissez-faire, classical economics. This marked the end of the Keynesian Revolution predicated on aggregate demand because the United States suffered from stagflation (experiencing inflation and high employment levels simultaneously). In addition, the Glass-Steagall Act that was passed in 1933 began to lose its powers through constant reinterpretations and eventually was overturned in 1999. Arguably, the repeal was one of the factors that contributed to the crisis in 2007-2009 when the mortgage bubble imploded, setting off the second worst economic crash since the Great Depression. The final section in this chapter addresses some of the post-recession financial frauds that recently took place such as the LIBOR scandal involving the major banks around the world.

Chapter 4 identifies the critical themes through the methodology of discourse analysis examining the mainstream news publications *The New York Times* and *The Wall Street Journal* published during the Great Depression (1929) and the Great Recession (2008). The three themes identified through discourse analysis of article headlines and text include: (1) the individuals that are painted as “the financial heroes” and “responsible agents” during economic chaos; (2) the difference in how the prosecutors conducted the investigation and prosecution of financial crimes during the Great Depression and the current crisis; (3) the regulatory banking act implemented during the Great Depression

and its comparison with the bailouts for financial institutions, such as TARP, during the 2007-2009 crisis.

Chapter 5 recaps the previous chapters and discusses the overall implications for our society, particularly by addressing what the Glass-Steagall Act has meant to the U.S. financial system. The second half of the concluding chapter analyzes the alternative media discourses involving the post-recession problems that still linger today such as high frequency trading (HFT), derivatives market, and quantitative easing (QE). Due to the trivialization of these problems by the mainstream media, only the alternative press offer fresh perspectives on the economic crisis.

CHAPTER TWO
HISTORICAL BACKGROUND (1776 To 1946)

*I will tell you a secret. Economics are supposed to be dry as dust, dismal fellows.
This is quite wrong, the reverse of the truth.*

-Paul A. Samuelson

A typical perception of advocacy is generalized in forms of essays or speeches, but advocacy also embodies itself in the realm of political and economic legislations. Legislative advocacy includes lobbying, ballot initiatives, legislative campaigns, etc. Economic legislative advocacy is an extremely powerful tool for shaping domestic and international financial policies. To understand the history of economic regulations and repeals, Chapters Two and Three will attempt to explain the history of market regulations. Chapter Two will begin by examining the history of the market and government regulations, starting in the seventeenth century with the father of classical economics, Adam Smith (1723-1790), and continuing in Chapter Three by outlining four major historical periods:

- (1) Mercantilism and Laissez-faire (1776-1929)
- (2) Overturning laissez-faire and the installment of the Glass-Steagall Act (1929-1946)
- (3) De-regulation of the Glass-Steagall Act and other banking laws (1999-2000)
- (4) Present crisis (2007-2009)

The chapter begins by explaining how the idea of an independent marketplace emerged. It addresses the regulatory impulse of government, particularly in relation to the growth of the modern corporations during the nineteenth century. It then examines how economic crises prompted governmental regulations, especially in financial markets because of their disruptive effects on the aggregate economy. It looks at the creation of quasi-independent regulatory agencies, such as the Federal Reserve that was set in place to reduce systemic risks, while still permitting industries' autonomy. The chapter particularly emphasizes regulatory infrastructures, focusing on the Glass-Steagall Act (1933), which was passed to mitigate the systemic economic risks caused by the powerful banking industry.

Mercantilism and Laissez-faire Economics

By pursuing his own interest, he frequently promotes that of the society more effectually than when he really intends to promote it.

-Adam Smith

The celebrated work of Dr. Adam Smith can only be considered as an assemblage of the soundest principles of political economy, supported by luminous illustrations.

-Jean-Baptiste Say

After the Treaty of Westphalia in 1648, Europe's national authorities predominantly functioned under the establishment of mercantilism (Cohn, 2012). However, the rise of classical economics most notably led by a Scottish social philosopher, Adam Smith, fundamentally reconfigured the realm of political economy

during the 18th and 19th centuries. Rejecting the old mercantilist principles of protectionism, state monopolies, and colonialism, Smith heavily supported a drastic overhaul in favor of free trade, limited government, balanced budgets, the gold standard, and laissez-faire economics (Skousen, 2005). In other words, Smith advocated for the utmost economic freedom for capitalists. Smith's most famous work, *An Inquiry into the Nature and Causes of the Wealth of Nations*, published in 1776, declared economic independence against protectionism and state interventionism. In a laissez-faire economy, the government's responsibility is considerably restricted only to protect private property and construct an atmosphere suitable to the operation of the market system (McConnell and Brue, 2008). Laissez-faire translates to "let it be," that is, it prevents the government from intruding with the free market system. The notion is that governmental interference will only lead to further impediments pertained to the efficiency of the market.

Popularized by the French during the late 17th and early 18 century, the origin of laissez-faire literally translates from French to English as, "let-fair." However, laissez-faire is commonly interpreted as "hands-off" or "let it be." Orthodox liberalism or classical liberalism predates many of the well-known 18th century Western philosophers and economists such as Smith, Say, Bastiat, Ricardo, Malthus, Mill, etc. English philosopher John Locke (1632-1704) reasoned that the "state's primary tenet is to preserve people's lives, liberty, and Estates, by the general names property" (Locke, 1964). Even though Locke predated Adam Smith by a few decades, Smith is considered as the father of classical economics, due to his extensive written works that heavily advocated for laissez-faire policies and resistance against state-operated mercantilism. According to Smith, the division of labor, interdependence, and unregulated economies

would benefit by efficiently producing goods and trading with other states (Cohn, 2012). Although Smith deeply preferred the government stepping aside from the market, he did not completely discount the government's responsibilities. It is crucial for the state to possess the ability to retaliate against other states when engaged in times of national conflicts, protect individuals from injustice(s), and provide public goods that the private sector would not be able to provide on their own (Wyatt-Walter, 1996; Smith, 1776, p. 180). In addition, the Government must enforce contracts, maintain state security against opposing nations, and supply public goods and services (Nadesan, 2010).

To resist the hegemonic forces of mercantilism, Smith sought to fight against the state by condemning the oppressive method of mercantilist economics. The mercantilists shrewdly operated by conjoining the bond between economics and politics, projecting both wealth and power as indispensable objectives to the state. The European mercantilists possessed the ability, power, and wealth to strengthen their military powers against enemies abroad. These powers operated under government-authorized monopolies domestically and abroad, imposing military forces on inferior nations to seize prized natural commodities such as gold, silver, opium, etc. (Skousen, 2005). Mercantile states mainly increased exports and decreased imports of manufacturing goods as they prevented other states from industrially prospering. Therefore, colonialism became the key tenet to a successfully operated mercantile state because colonies such as India for the British East Company supplied Great Britain (metropole) with raw materials to serve as resource markets for its manufactures (Cohn, 2012).

In addition, Adam Smith criticized high tariffs and trade regulations as a counterproductive formula to economic growth. Instead, he advocated for a drastic

solution to counter the oppressive forces suggesting free movement of labor, capital, money, national trade, and goods. For example, by expanding trade between Britain and France and other nations that provided valuable commodities: “If a foreign country can supply us with a commodity cheaper than we ourselves can make it, better buy it from them” (Smith, 1776; 1965). Some contended his economic ideas were too radical, but Smith continued to advocate for the dismantling of state regulations regarding prices, employment, and trades that would lead to universal economic opulence, which extends to the lowest ranks of society (Smith, 1776; 1965). Milton Friedman praised Smith stating, “Adam Smith was a radical and revolutionary in his time, just as those of us who preach laissez-faire are in our time” (Friedman, 1978, p. 7).

The Wealth of Nations forever changed modern day economics over the next centuries by dismantling the hegemonic economic forces of state-run mercantilism. Adam Smith, who coined the term, “The Invisible Hand” argues that, individuals who chase their own interest will create a self-regulating and highly prosperous society. In a passage Smith states, “The private interests and passions of individuals naturally dispose them to turn their stock towards the employments, which in ordinary cases are most advantageous to the society” (Smith, 1776; pg. 1079). The core concept of Smith’s notion of the market explains the outcome of a certain kind of behavior in a particular, social framework resulting in definite and foreseeable outcomes (Heilbroner, 1992). The drive of individual self-interest in a cutthroat environment not only results in competition, but also the provision of those goods and services society desires. According to Smith, self-interest is a force that guides people to whatever work society is willing to pay. Smith states, “It is not from the benevolence of the butcher, the brewer, or the baker that we

expect our dinner, but from their regard to their own interest. We address ourselves, not to their humanity, but to their self-love, and never talk to them of our necessities, but of their advantages” (p. 24).

Smith’s notions of economic liberty forever changed future generations’ by disassembling oppressive mercantilist policies. “The Invisible Hand” became the trademark of Smith’s model of economic liberty. He argued that if individuals were left to their own devices, chasing after their own self-interest, people would produce a self-regulating system and a highly prosperous society (Skousen, 2005). Former Chicago School of Economics Professor George Stigler calls Smith’s invisible-hand doctrine the crown jewel of economics: “Smith had one overwhelmingly important triumph. He put into the center of economics the systematic analysis of the behavior of individuals pursuing their self-interests under conditions of competition (Stigler, 1976; p. 1201). In *The Wealth of Nations*, Adam Smith spurned mercantilist ideals of economic control headed by the state in favor of the “invisible hand” that advocates for peoples’ self-interest in labor.

The Rise and Fall of Classical Liberalism

Unlike contemporary liberalism that is prevalent in the Western world that advocates for government intervention in the financial sector to stimulate growth, classical liberalism in the mid-18th century aligned with what is equivalent to contemporary conservatism, emphasizing the significance of free market and limited government intervention in the market economy. The classical economists had essentially disrupted and dethroned the sovereignty over the state’s economic operations. Sir Dudley

North, an advocate for economic liberty stated, “Peace, Industry and Freedom that bring Trade and Wealth and nothing else” (Davies, 1952, p. 284; Nadesan, 2010).

Despite crediting Adam Smith with coining the concept of laissez-faire, the foundation of this term originated in France during late seventeenth century. John Maynard Keynes noted in 1926 that the idea of economic freedom was first codified in 1751 by Marquis D’Argenson (Nadesan, 2010). Keynes described Marquis’s idea of laissez-faire or economic freedom as follows: “The Marquis was the first man to be passionate on the economic advantages of governments leaving trade alone, to govern better, he said, one must be governed less.” Keynes further highlights the attraction of market economy in the 17th and 18th centuries through the transition from public advantage to private interest by stating, “The individualism of the political philosophers pointed to laissez-faire. The divine or scientific harmony (as the case might be) between private interest and public advantage pointed to laissez-faire” (Keynes, 1926).

During the eighteenth century, French philosophers, Jean-Baptiste Say and Frederic Bastiat, who predicated their studies on open trade and free entrepreneurial economy (Skousen, 2005), mainly led the economic school of laissez-faire in France. Known as the French version of Adam Smith, Jean-Baptiste Say developed his own law of markets, which became the cornerstone of classical macroeconomics. Say’s law states, “supply creates its own demand” that focuses on saving, capital investments, and entrepreneurship (Skousen, 2005). An admirer of Smith’s self-directing economic system of competition, liberty, and minimal government interference, Say contributed to classical economics in four areas:

(1) Belief in testing theories with facts and observation; (2) A subjective utility theory rather than a labor theory of value; (3) An appreciation of the vital role of the entrepreneur; (4) Say's law of market forms the foundation of classical macro model of business fluctuations and economic growth. (Skousen, 2009, p. 52)

Say's classical model of "supply creates its own demand" became the economic norm of market activity until the arrival of British economist John Maynard Keynes in the 20th century.

Frederic Bastiat firmly believed in free trade and laissez-faire policies. One of Bastiat's profound works was debunking the popular fallacy of stimulating the economy through the destruction of war. Bastiat's "Broken Window" fallacy notes: it's true destruction leads to spending; however, that money could be used for something far more productive according to the individual's need. Bastiat explained:

The window having been broken, the glass industry gets six francs' worth of encouragement; that is what is seen. If the window had not been broken, the shoe industry (or some other) would have received six francs' worth of encouragement; that is what is not seen. (Bastiat 1995; p. 2)

In Bastiat's most critical thesis, *The Law* (1850), he established a proper social organization appropriately suited for people that preserves life, liberty, property and justice (Skousen, 2005). Bastiat further states, "If everyone enjoyed the unrestricted use of his faculties and the free disposition of the fruits of labor, social progress would be ceaseless, uninterrupted and unailing" (Bastiat, 1850; 1998, p. 5).

Adam Smith was not the only British classical economist during the late eighteenth century, as Thomas Malthus and David Ricardo also maintained the classical economic ideologies by advocating free market, limited government, and gold-backed currency. However, the economists that succeeded Adam Smith took a different route

from his principles as they left a black eye on the face of Smith's economic philosophies. Instead of carrying on Smith's positive views of wealth creation, harmony of interest and universal opulence, his British heirs failed to communicate Smith's economic ideologies (Skousen, 2005). For example, David Ricardo (1772-1823) further fortified the stance on free-trade defense by claiming that two nations could profit both ways through comparative advantage. Ricardo states that even if a nation did not possess absolute advantage in manufacturing goods, they are still able to concentrate on products based on relative advantage (Cohn, 2012). Smith, on the other hand, did not recognize free trade as a unilateral or unconditional policy. In unjust trade restrictions, a state should have the right to retaliate, thereby, progressively implementing free trade policies for domestic industries and labor groups in order to adjust to international competition (Cohn, 2012). Other than the division of labor explained in *The Wealth of Nations*, classical economists failed to produce and expound upon a sound theoretical framework on Smith's vision of universal opulence. Another inconsistency in Smith's work included the important concept of the diamond-water paradox that separates production in use and the production in exchange:

What are the rules, which men naturally observe in exchanging goods for money or for one another, I shall now proceed to examine. These rules determine what is called the relative or exchangeable value of goods. The word value, it is to be observed has two different meanings and sometimes expresses the utility of some particular object and sometimes the power of purchasing other goods, which the possession of that object conveys. The one may be called "value in use," the other, "value in exchange." The things that have the greatest value in use have frequently little or no value in exchange; on the contrary, those that have the greatest value in exchange have frequently little or no value in use. Nothing is more useful than water, but it will purchase scarce anything can be had in exchange for it. A diamond, on the contrary, has scarce any use-value, but a very great quantity of other goods may frequently be had in exchange for it.

(Smith, 1776; 1965 p. 46-47)

Smith is comparing and contrasting a precious commodity like water to an impractical product such as diamonds; yet, such stones are highly valued in the marketplace. This only provided ammunition to the socialists by painting the picture of capitalists generating massive profits over providing practical services. Despite Smith's combination of economic freedom and limited government paving a path toward universal wealth, the father of classical economics failed to expand on a reliable theoretical framework that details how consumers and producers work through the profit-and-loss system in order to achieve the ultimate goal of "universal opulence" (Skousen, 2005).

The laissez-faire logic of limited government became popular in the western world throughout majority of the eighteenth and nineteenth centuries (Nadesan, 2010). However, too many mixed theories and doctrines by individual classical economists after Smith only provided the opposition with powerful incentives to label them as individuals with a conflict of interest by pushing profits ahead of the overall wellness of society. In Adam Smith's perfect world, every individual stood to gain as the division of labor expanded to all ranks of society; however, in the eyes of David Ricardo, only one group of people are stood to gain (Heilbroner, 1987). Ricardo argued that the workers are subjected to subsistence due to spending majority of their earnings on family. Adam Smith believed that the landlords, workers, and capitalists would collectively come together to reap the benefits. Contrary to Smith, Ricardo viewed the three-way triangle between the landlords, workers, and capitalists as a "class conflict" model of who gets the biggest piece of the pie. If the landlords receive the majority of the wealth, the capitalists

and workers stand to receive only a small fraction of the remaining wealth (Skousen, 2009).

Inspired by Ricardo, the famous Prussian (German) economist and philosopher, Karl Marx was greatly influenced by David Ricardo, heralding him as his intellectual mentor. According to Murray Rothbard (1980), classical economics came to a halt, thus leaving the Western world of economics at the hand of the Marxists. The failure of Smith's successors seemed to have negative consequences as Thomas Carlyle, an English critic, labeled economics as a "dismal science." The French decided to head towards a different route as they embraced socialism over Say's and Bastiat's free market ideology. The Prussians were facing similar circumstances by rejecting the ideology of classical economics as the theoretical analysis came to be regarded with "deep distrust," as noted by Friedrich Hayek (Hayek, 1976). By end of the eighteenth century and beginning of the nineteenth century, first industrial revolution propelled the states' economies into a new direction of prosperity as the multitude of agricultural-based economies shifted toward industrial production.

Nineteenth-Century United States Business Boom

The history of modern corporations traces back to the early seventeenth century, when Queen Elizabeth I of England instituted the British East India Company. Unlike the contemporary era of large corporations, the crown financed large operations such as expeditions in the Fourteenth century. According to Lee Drutman, the monarchs kept a close eye on these corporations and if they became discontent with the overall lack of results, the crown quickly rescinded their charters. For example, prior to the American

Revolution during the late eighteenth century, the Massachusetts Bay Company fully supervised the American Colonies. This section will mainly address the rise of corporations in the United States during pre-and post-Civil War. The United States in the early nineteenth-century mostly engaged in agricultural production, while large corporations sanctioned by the state government provided transportation such as canals and newly formed railways (Nadesan, 2010).

The early nineteenth-century railroad tycoons became the original founding fathers of the modern day corporations (Bakan, 2004). Due to massive amounts of capital investments and finances to fund nationwide manufacturing projects, railroad operations required corporate forms of finances. According to Chandler (1965), the creation of railways helped launch the rise of private American corporations, but it also played a critical role in advancing the American financial system such as the capital markets and the stock exchanges (Pontecorvo, 1958). Railroad manufacturing commenced during the nineteenth century in the United States then boomed after the United States Civil War from 1865 to 1885. When the railroad industry expanded into the scene, it had the same effect on corporations (Bowman, 2009). Initially, railroads were subsidized by newly established towns in the West to attract visitors from the East and Mid-West to stimulate the local towns (Nadesan, 2010). For example, to attract tourism, local towns created artistic portraits that contained a lavish scenery of the nature with a train heading toward a rail station; within the middle of the portrait, it would read, “Don’t miss the train.” Local towns promoted bogus portraits to influence outsiders for visits and the quickest method was by implementing the railroad system as a catalyst to entice tourism.

With a booming railroad industry in sight, it was only a matter of time before corporations fully seized control. In the mid-to-late nineteenth century, railway stocks enabled middle-class Americans to invest in corporations. According to *The Economist*, “everyone was in the stocks now. Needy clerks, poor tradesman’s apprentices, discarded services men and bankrupts all have entered the ranks of the ranks of the great monied interest” (Bakan, 2004, p. 11). No matter how much people had invested in a company, individuals were held liable without limit for the company’s debts (Bakan, 2004). Investors’ possessions were at stake because their personal assets such as savings and homes would evaporate if the company turned out to be unsuccessful. In other words, individual investors jeopardized all their wealth by simply owning shares in a company. To counter these financial risks, politicians and business leaders advocated regulatory legislations by limiting the liability of shareholders to the amounts the customers had invested (Bakan, 2004). Those that supported limited liability believed it was imperative to entice middle-class investors. In spite of the outcome of the company, if an individual purchased \$100 of shares, they should be protected from liability regardless of the success or failure of the company (Bakan, 2004, p. 11).

However, limited liability posed moral hazards because it permitted the shareholders to escape unharmed from corporate collapse, thus leaving the investors without any sense of responsibility for the fate of the company. The critics of limited liability claimed shareholders could potentially be apathetic or disinterested in the company’s fortunes (Bakan, 2004). A member of the English Parliament stated, “The first and most natural principle of commercial legislation that every man was bound to pay the debts he had contracted, therefore, it enables the investors to undertake in trades

with a limited chance of loss, but an unlimited chance of gain” (Weiss, 1986). Regardless of the praises and the criticisms, limited liability was established in both English and American corporate laws in the mid to latter half of the nineteenth-century.

According to Bakan (2004), limited liability removed the risks of investment in stocks and paved a path for the multitude to dive into the stock markets. However, publicly traded companies during the nineteenth century in the United States were uncommon as companies were often family-owned businesses and regularly traded on a smaller scale of person-to-person circumstances. Unlike the contemporary era of stock market exchanges engaging in business trading, the nineteenth-century United States did not rely on the stock markets until the early twentieth century when corporations became fixtures of the United States economic landscape (Horwitz, 1987). In 1887, the U.S. Congress enacted the Interstate Commerce Law that gave the U.S. government full authority to regulate interstate railroad rates (Dodd, 1936; Nadesan, 2011). By the late nineteenth-century, corporations in the United States experienced drastic modifications.

In 1890, New Jersey and Delaware revolutionized corporate structures, as they became the pioneers of discarding corporate regulations that limited controls on mergers and acquisitions, along with terminating corporate laws that prohibited from owning stocks in other companies (Bakan, 2004; Nadesan, 2011). New Jersey and Delaware’s actions created a ripple effect that pressured other states to stay competitive in the business world. That same year, the U.S. Congress signed the Sherman Anti-Trust Act, which was originally intended for substantial federal surveillance over corporations, business transactions and regulating competition in the free market economy (Dodd,

1936). Despite its original intentions of economic regulations, The Sherman Anti-Trust Act led numerous corporations to consume one another, thus undercutting competition.

Although the concept was sound for the U.S. economy, The Sherman Anti-Trust Act restructured corporate ownership, which inevitably prompted market consolidations (Roy, 1997). Intermediate-sized companies utilized pools, which inevitably lead to monopoly because the competing companies agree to fix prices and divide regions among members, so that only one company operates in each area (Nadesan, 2011). With many of the regulations on mergers and acquisitions repealed, vast numbers of small and mid-sized companies morphed into large corporations. For example, the landscape of American corporations witnessed drastic consolidation of 1,800 companies to 157 from 1898 to 1904, thus corporations consolidated thousands, if not hundreds of thousands of shareholders (Marchand, 1998). This model failed to produce a figure that is capable of making managerial decisions; instead, the logjam of shareholders watered down the power to act jointly in the decision making process. With the dispersion of power, it was paramount for the lawmakers to find individuals, groups, or someone else to seize the rights to a corporation within the financial market (Marchand, 1998).

In the case *Santa Clara v. Southern Pacific Railroads* in 1886, the United States Supreme Court ruled corporations as “persons” under law that was protected by the Fourteenth Amendment. The Supreme Court ruling embodies corporations free from discrimination, speech, due process, and equal protection of the laws (Bakan, 2004). In 1911, a law professor reminisced over the phenomenon of the court rulings saying, “no imaginary or fictitious, but real, not artificial but natural” (Horwitz, 1987). By end of the nineteenth-century to the beginning of the twentieth-century, the United States economic

and financial system underwent a revolution from individual enterprises to mega corporations, thus initiating the era of corporatism. Businesses at the end of the nineteenth century organized into corporate forms through consolidations, limited liabilities, and legal persons (Hansmann & Kraakman, 2000-2001). The five-core feature that shaped the corporations today, are:

- (1) Full legal personality, including well defined authority to bind the firm to contracts and to bond those contracts assets that are the property of the firm, as distinct from the firm's owners;
 - (2) Limited liability for owners and managers;
 - (3) Shared ownership by investors of capital;
 - (4) Delegated management under a board structure; and
 - (5) Transferable shares.
- (Hansmann & Kraakman, 2000-2001, p. 440)

At the beginning of the twentieth century, corporations accounted for approximately sixty percent of manufacturing in the United States (Dodd, 1936). According to the *Manual of Statistics* published in 1905, only six steel industries produced half of all manufacturing capital and U.S. Steel was responsible for one-third of all common stocks (Roy, 1997; Nadesan, 2011). Roy (1997) states industrial consolidation occurred due to the exhaustion of railroad securities and anti-trust efforts that generated an economic schism between the small and large businesses. Although the rise of corporations transformed American businesses, the overall public sentiment of fear of these powerfully consolidated companies soon became a reality during the beginning of the twentieth-century. Apparently, public opinion shifted negatively as the multitude recognized the hazards of these corporations hijacking the government and social institutions. During the early twentieth-century, corporations were perceived as gloomy, merciless, impersonal, and amoral monsters of society (Bakan, 2004). The imprisonment of the U.S. financial system through corporate consolidations suddenly became susceptible to civil grievances

and disputes due to rapid growth in size. In the awakening of the public discontent, corporations, business leaders, and media members called for a new strategic plan that still contains significant implications to this day.

One of the largest U.S. corporations in the early twentieth-century, AT&T launched a new style of advertisement to combat the public outrage by instilling corporations with flash-and-blood human traits, similar to the Supreme Court ruling that defined corporations as “human.” By using public relations (PR), AT&T convinced the public to love the company. For several decades, AT&T experienced immense success through its “friend and neighbor” campaign that presented real people for promotion of the company (Bakan, 2004). As a new public relations strategy, employers frequently emerged in corporate advertisements and this style of humanitarian campaign established the blue print for rest of the mega-corporations. Once considered impersonal, amoral and leviathans of society, at the beginning of the twentieth-century, corporations revamped the art of public relations to appear as compassionate and responsible “persons.” This perpetuated the new economic outlook of the twentieth-century that established new promises of corporate responsibility, improved wages, and overall working conditions.

The Downfall of Laissez-Faire Economics

The rise of corporations in the United States gained substantial momentum entering the twentieth-century through excessive leveraging transpired by the banks and securities markets. The banks in the United States and Europe for the most part failed to regulate the states economies until the 1930s, or even post-WWII. In addition, the

government loosened charter restrictions for corporations and created limited liability during the mid to late nineteenth century. The lack of sufficient accounting criteria led investors to acquire securities that solely relied on private rating agencies such as the United States Standard & Poor's (S&P), which still exists today, to offer detailed insights regarding company finances (Nadesan, 2011). Marked by laissez-faire economic practices, the issues listed above paved a path toward destabilization of the American financial system, due to the lack of sovereign control over credit (Ahamed, 2009; Dumenil & Levy, 2001).

Post-WWI from 1914-1918 marked the conclusion of laissez-faire economics in the Western world. According to Nadesan (2011), the Great War provided lucrative outcomes for an alliance or partnership between sectional economic interests and national policy in the name of war profiteering. Even in times of horrid atrocities, the Great War proved to be a lucrative success for several American corporations such as DuPont, which profited millions of dollars from contracts. Furthermore, from the late nineteenth-century to the early twentieth-century, the European expansion over resource-seeking colonial investments in Africa and the Middle East (e.g. oil, railroads, canals, minerals and agricultural products) increased exponentially, while relying on manufacturing and finances in the developed nations (Gabel & Bruner, 2003).

The post-war decade of the "Roaring Twenties" was characterized by prosperity, economic growth, and cheap money that financially propelled economic growth. However, the speedy financial growth and rapid increase of consumption came to a screeching halt due to the threats of overproduction, which inevitably led to the stock market crash of 1929 (Black Tuesday). The American population no longer possessed the

wealth to consume newly produced products such as Henry Ford's Model T's along with other goods (Nadesan, 2011). According to Palmer and Colton (1984), the depression of 1929 caused business expansion that was financed on credit resulted in diminished agricultural crops harvested in Europe. To further note, three years into the depression, world manufacturing sharply plummeted by 67% and unemployment sharply escalated to over 13 million people in the United States (Chambers et al., 1983). The most catastrophic financial crisis to this date did not occur by accident. Presumably, the states failed to comprehend the boom and bust cycles of capitalism as the deregulated market and unsound governmental policies led to the outcome of substantial economic and social fragility (Dumenil & Levy, 2001). In response to the apocalyptic disaster, the United States government granted a legislation that authorized the private Federal Reserve System to become the principle regulator of all banks and it prohibited bank deposits from selling securities (Dodd, 1936; Nadesan, 2011).

Woodrow Wilson would ultimately have unhappy thoughts about the Federal Reserve Banking System he signed into law in 1913:

"I am a most unhappy man I have unwittingly ruined my country. A great industrial nation is controlled by its system of credit. Our system of credit is concentrated. The growth of the nation. Therefore, and all our activities are in the hands of a few men. We have come to be one of the worst ruled, one of the most completely controlled and dominated governments in the civilized world. No longer a government by free opinion, no longer a government by conviction and the vote of the majority, but a government by the opinion and duress of a small group of dominant men."

-Woodrow Wilson

The United States Congress in the early twentieth-century was determined to create an efficient banking system in the awakening financial crisis of 1907 or widely

known as, the Panic of 1907. One of Fed's crucial objectives is to regulate the nation's overall money supply through a satellite of privately operated regional banks (Greider, 1987). There are 12 Federal Reserve banks scattered regionally across the nation, whose policies are to be directed by the Fed's Board of Governors (McConnell & Brue, 2008). Since its inception, the president of the United States appoints the chairman of the Federal Reserve. Prior to its creation, rapid flooding of money triggered excess inflation; conversely, shortage of liquidity impeded national economic growth. Since no single entity controlled the national money supply along with creating and implementing national banking policies, two United States Congressman, Carter Glass, and Robert Owen drafted the Federal Reserve Act of 1913 and signed into law by President Woodrow Wilson on December 23, 1913 (McConnell & Brue, 2008).

Although the Federal Reserve System sounds innocuous and necessary to supervise the American financial system, on July 31, 2012, a local journalist, Ben Swann from Fox 19 Cincinnati, provided a new angle on the Federal Reserve. Popularized by Ron Paul's audit the Federal Reserve (H.R. 459) legislation in July 2012, the report provided an alternative outlook on the Fed. In an in-depth investigation of the Federal Reserve, Swann stated, Federal Reserve Act of 1913 was drafted under great secrecy in a meeting involving powerful individuals and families such as J.P. Morgan, William Rockefeller, the Rothschilds, and two other families at a location called Jekyll Island. These five families represented one-fourth of all the wealth in the world. Next, Swann presented what he perceives as five critical objectives of the Federal Reserve:

- (1) stop competition from newer banks, especially the banks in the Western region of the United States;
- (2) to obtain a franchise to create money out of nothing (not backed by a physical commodity) for the

purpose of lending; (3) to get control of all reserves of other banks, so that reckless banks would not be over run; (4) to shift the losses from the banks to the taxpayers; (5) to convince Congress that the purpose was to protect the public. (Swann, 2012)

If the government needs money, the United States Treasury prints the required amount, but the treasury does not have the authorization to release the newly printed money. This is where the Federal Reserve comes into play by taking newly printed money and supplying it to other banks, and then the regional banks loan it to the public to pay interest. The interest people pay goes back to the U.S. Treasury, thus completing the cycle (Swann, 2012). The Federal Reserve Bank is not responsible to the president, congress and most importantly, the American people. Although, the evidence is not clear, Swann's critique raises questions and issues that deem relevance for the Federal Reserve's role in the financial crisis, which will be discussed later in this thesis.

Overturning Laissez-faire

There is no cause to worry. The high tide of prosperity will continue.

-Andrew W. Mellon

Gentleman, a depression is for capitalism like a good, cold douche.

-Joseph Schumpeter

Although the stock market crash in 1929 became the triggering mechanism for the Great Depression, the United States economy actually began to trend downward years prior to the crash (Kangas, 1997). Three Republican presidents reigned office during the

economic “boom” of the 1920s: Warren G. Harding (1920-1923), Calvin Coolidge (1923-1929), and Herbert Hoover (1929-1933). Their central economic philosophy of laissez-faire operated with little to no government interference or installing of regulatory legislations. This was the belief that the markets always corrected automatically and that government must not interfere with the self-correcting operations. Financial regulations were gashed dramatically, monopolies were allowed to form and inequality of wealth occurred (McElvaine, 1984; 1993). The Republican presidents abolished government regulations, anti-trust laws and the top tax rate was cut from 73 to 25 percent as the top one percent owned approximately 40 percent of the nation’s wealth (Kangas, 1997).

The Great Depression

During the 1920s laissez-faire economic system, manufacturing, services, and finances gained record highs as the stock market sharply increased. The United States economic growth was mainly predicated on two industries: construction and automobile manufacturing. As the 1920s progressed, even the merchandise sales of the well performing industries decelerated prior to the crash (Kangas, 1997). The NYSE prices failed to reflect market pains, including reduced demand for houses, automobiles, and other durable goods. Over-investment and speculation in stocks inflated the prices that contributed to what was considered a “robust” economy. In October of 1929, massive sell-offs of stocks triggered a serious pandemonium at the New York Stock Exchange (NYSE) that spread like wildfire across the globe. In fact, the market did not hit its trough (lowest point of a business cycle) until 1932. When the U.S. economy hit its lowest point, a quarter of the working population was unemployed. The United States banking system

was in life support as 11,000 banks failed, or were given the orders to merge with other banks issued by the newly elected Roosevelt administration. The drastic cuts in the banking system resulted in a 40% decrease from 25,000 to 14,000 banks and the governors of several states had to shut down its state banks (Foner, 2005). By far, The Great Depression was the most traumatic economic event in the United States during the twentieth century. It occurred at a time of great advances in technology and living standards, as economic fallout was inconceivable. The Great Depression of 1929 did not occur by accident. The crisis was an accumulation of massive fraud that built up over the years and there was only one brave soul to conduct an investigation against the hegemonic giants of the financial industry.

Legal Proceedings

During President Hoover's last year in office, the U.S. Senate committee summoned a series of judicial hearings over banking and currency to investigate the transactions that destabilized the U.S. financial system. The initial attempt was unsuccessful because the hearings only managed to produce weak testimonies and they failed to reveal Wall Street's phony financial practices (Crawford, 2011). However, the overall dynamics of the legal proceedings radically shifted a year later. The new outlook on tackling the main causes of the Great Depression was led by Ferdinand Pecora, a Manhattan prosecutor, who proceeded as an advocate for public transparency. Rarely mentioned as a key figure in unearthing fraud, cronyism and reckless use of depositors' funds, Bill Moyers described Pecora as a "savvy immigrant from Sicily that proved the undoing of Wall Street banking world gone berserk with greed and fraud" (Moyers,

2009). The hunt for the lawbreakers responsible for the crisis began on April of 1932 by the Senate Committee on Banking and Currency (Galbraith, 2009). The primary goal was to investigate the fraudulent operations of the stock exchanges. Regarding the trial, Galbraith stated, “Under the later guidance of Ferdinand Pecora, this committee became the scourge of commercial, investment, and private bankers. But this was not foreseen when it was organized” (p. 156).

One by one, Pecora placed the top banking executives on the stand starting with Chase National Bank (JP Morgan Chase) whose president enriched himself by short selling his company’s shares during the economic crash. Pecora then proceeded with his interrogation of Charles Mitchell of the National City Bank (modern day Citibank), exposing fraudulent practices, such as giving bonuses to traders based on sales figures (the riskier the security, the higher the bonuses). This outcome translated to selling off failed loans to Latin American nations through palming off bad loans by packaging them into securities and selling them to unsuspecting investors (Chernow, 2009). The revealing of Mitchell’s fraud was one of the most astonishing moments of the hearings because of his excessive speculation in stocks using the bank’s money. In addition, Mitchell sold stocks of his own bank that he used to secure loans from J.P Morgan (McElvaine, 1993). To worsen the situation, he sold the stocks to his wife for less than the original payment, thereby creating an enormous paper loss and eliminating all tax obligations (McElvaine, 1993). Mitchell stated, “I sold this stock, frankly, for tax purposes.” Pecora’s series of investigations forced Charles Mitchell of National City Bank to resign.

Due to the exposure of financial corruption, the public was enraged over the corporate greed these top executives possessed. Michael Perino stated, “Pecora was a

smart lawyer and he knew that the game plan that he had to follow was to, quite frankly, whip up some popular outrage. If he could get the clamor for reform was in place – Congress essentially fell in line” (Moyers, 2009). Ferdinand Pecora overcame the task of interrogating the financial giants in an era of economic system that heavily favored the mega-bank executives. Through transparency, Pecora sacrificed his entire career to advocate for a greater public interest by exposing the individuals that participated in the greatest economic collapse the U.S. ever experienced, which put millions of people on the unemployment line.

Prior to Pecora’s investigation, the top financial executives were ignorantly commended for their business practices, as the public was completely oblivious to their deceitful methods that eventually led to the financial collapse of 1929. The large banks profitably advocated in circumventing regulatory financial legislations. In effect, unregulated banks traded freely in securities and possessed no interest in discontinuing their profitable, yet fraudulent, business dealings (Crawford, 2011). As a Credit to Pecora, once all the information of immoral financial practices and the inherent conflict of interest became transparent, the public was in an uproar, as the multitude demanded restructuring of these large financial institutions. Pecora not only took Wall Street and the bankers by storm but also helped the public focus on the bigger picture: “the Pecora hearings provided public transparency of the financial fraud that collapsed the American financial system” (Moyers, 2009). Charles Mitchell’s confession during the Pecora Hearings not only created a public outrage, but the exposure of excessive greed surrounding the financial sector became the overwhelming substance of the trial. Other factors addressed included manipulation of stock prices, trading of proprietary holdings,

and unsupportable holding companies. Pecora Commission findings of bank records included giant loans to bank officials and tax evasion (McElvaine, 1993). The remaining faith people had in the financial system evaporated after the newly released indictments.

The public rage at the financial executives yielded a cultural change that led to the installment of economic regulations that provided the necessary protection over the financial sector. The public backlash forced the politicians to enact as they composed and ratified stringent financial legislations. Under FDR's New Deal, the financial crash led to the inception of regulatory reforms and not blindly putting faith in corporations to make the right decisions (Nadesan, 2011).

The Glass-Steagall Act

More than 2000 banks failing in 1931, the United State's banking system was in a state of panic. President Hoover passed the first Glass-Steagall Act in 1932, which attempted to halt deflation and expand the Federal Reserve's ability to offer rediscounts on more types of assets, such as government bonds and commercial paper (Lardner, 2009). The inception of Franklin Delano Roosevelt's presidency in 1933 entered a new age of economic financial reforms. As a part of FDR's New Deal, the Glass-Steagall Act contained two separate pieces of legislations that passed in 1932 and, more notably, in 1933 during the Great Depression. FDR approved the Glass-Steagall Act after the Pecora hearings that aggressively sought economic justice by dragging bank officials in front of the Senate Banking and Currency Committee demanding them to reveal their role in the stock-market crash. The crucial advocacy effort in fighting against the hegemonic forces of the bank-preferred laissez-faire market logic paved a path toward regulating the U.S.

financial system. Roosevelt's approval of the Glass-Steagall Act was one of the first reforms Roosevelt immediately signed into effect. According to *Time* (June, 1933, p. 45):

The Banking Act of 1933 (passed last week by accident because a Presidential blunder kept congress in session four days longer than expected) requires private bankers to give up either banking or their securities business.

The Banking Act of 1933, commonly known as the Glass-Steagall Act, was a pivotal moment for regulating the banking system in the aftermath of the Great Depression. It effectively separated commercial banking practices from investment houses. Under Glass-Steagall, the commercial banks that accepted deposits were barred from engaging in investment banking practices. It also, disallowed the investment banks to principally engage in trading of securities and underwriting and selling securities (Tabarrok, 1998). The new banking legislation gave the banks an option to decide whether to withdraw from the securities business and receive the benefits of federal deposit insurance or bypass the acceptance of deposits and convert to an investment bank. The rules within the Banking Act made a clear distinction, as banks had to decide between enacting as a commercial or as an investment bank (Crawford, 2011). According to Parrish (1992), the passage of Glass-Steagall transferred the control over open market operations such as buying and selling of government securities from the private Federal Reserve System to the Federal Reserve Board in the nation's capital. Insurance funds subsidized by the federal government and banks were set to be administered by a newly formed agency, the Federal Deposit Insurance Corporation (Parrish, 1992). The Banking Act of 1933, enacted on June 16, 1933, established the Federal Deposit Insurance Corporation (FDIC) and controlled speculations, keeping the banks away from the stock market. The

protection from the FDIC guaranteed customer deposits to a certain level in order to calm the widespread panic that resulted in rapid bank collapses (Sherman, 2009).

During that same year, Congress passed the Securities Act of 1933, which required issuers of securities to “file with a federal commission and make available for investors an amount of information about the issuer and the security to be issued which far exceeds in volume and completeness of detail anything required by state law” (Dodd, 1936, p. 54). Failing to comply resulted in exclusion from future sales, criminal penalties, and civil liability to issuers and directors (Nadesan, 2011). The Securities Exchange Act of 1934 lengthened the provisions of the Securities Act of 1933 and transformed these entities into what is widely known today as the Securities Exchange Commission (SEC). A year after, the construction of the Federal Communications Commission (FCC) provided regulatory power over telephone and telegraph corporations such as AT&T (Nadesan, 2011). Therefore, the widespread efforts of regulating the financial markets and securities helped transition the U.S. financial system toward recovery.

The Glass-Steagall Act (P.L. 73-66, 48 STAT, 162) prohibited commercial banks from owning securities, brokerage firms, established a temporary deposit insurance program under the Federal Reserve, and included Regulation Q, which prohibited the practice of paying interest on commercial checking accounts and capped the interest rate on savings accounts (Sherman, 2009). In other words, Regulation Q allowed the Federal Reserve to regulate interest rates in savings accounts. It tightly regulated the interest rates these banks could offer on deposits. It also made exemptions for institutions specializing in mortgage lending, particularly the savings and loans associations. According to Sherman (2009), deposits at these firms received a ¼ of a percent advantage over

consumer deposits as these transactions were unequivocally intended to promote a flow of money into housing. In the 1920s and early 30s, the overall make-up of this bill was overwhelmingly ostracized amongst the American legislators (Benston, 1990). There was minimal congressional support to regulate the American financial system even after the crisis. Just two years after the passage of the Glass-Steagall Act, Carter Glass tried to repeal his own legislation, as he believed it was a mistake and an overreaction; however, he passed on the decision to repeal the Banking Act in 1946 (Benston, 1990).

However, despite personal doubts regarding the implementation of financial regulations, the reforms produced overwhelming results. Glass-Steagall's goal was to revamp the old financial structure, pave a new groundwork based on integrity, and, more importantly, provide financial stability to the banking system. Constant financial crises, or panics were reoccurring events that resulted in devastating consequences dating back to the 1800s, but Glass-Steagall kept the financial panics in check (Lardner, 2009). While individual banks collapsed occasionally, the depositors escaped unharmed. The United States financial system regained its confidence by setting high standards of reliability and transparency. As time passed, trust in stocks and bonds steadily recovered for investors not only in the United States, but also on a global scale (Lardner, 2009).

The U.S. Congress decided to exercise the Glass-Steagall Act in 1956 with the passage of the Bank Holding Company Act, which prohibits companies that own commercial banks from engaging in non-banking activities, particularly insurance (Mitchell, 2010). The policy-makers strongly advocated for barring banks from risky investments in underwriting insurance (Mitchell, 2010). Despite the bankers' complaints

about deposit insurance, the passage of the Glass-Steagall Act immensely strengthened the American private banking system (McElvaine, 1993).

The Main Advocates

It is important to acknowledge the legislative advocates that assembled the Glass-Steagall Act in 1932 and 1933. Who were these people? Standing at an imposing height of 5 feet, 4 inches, the primary force behind the legislation was Senator Carter Glass from Virginia. According to Federal Reserve documents, Glass was responsible for drafting the Federal Reserve Act in 1913, due to the Panic of 1907. Considered as the father of Federal Reserve, Carter Glass acted as an advocate to bring financial stability to the United States economy. Fast-forward to the 1930's, Carter Glass was one of the few critics of the banking culture that indulged in perilous investments. It was imperative for Glass to advocate for the limitation of the banking sector in order for him to push for the notion of regulatory modifications he desired. Although this particular legislation strongly opposed the culture of laissez-faire economics, he had two strong allies on his side. First, what was considered an improbable legislation became a reality once the revelation on National City Bank's corrupt practices were brought to the forefront during the Senate Committee on Banking and Currency's Stock Exchange Practice Hearings (Benston, 1990). Second, a major contributor to Glass's regulatory actions occurred when Representative Henry Steagall decided to support Glass's legislation. Steagall was a member of the House Banking and Currency Committee. He initially possessed very little interest in economic regulations when he first encountered Glass; however, both congressional representatives came to an agreement after Carter Glass promised to

include Henry Steagall's proposal, which allowed bank deposit insurance (Benston, 1990). Overall, these two factors became essential elements that led to the creation of the Glass-Steagall Act. The next section will briefly discuss the economic philosophy of Keynesian economics, which main tenets are derived from aggregate demand in an environment of regulated capitalism.

When All Else Fails, There is Keynes

*Did Keynes create a sense of hope? Oh, unquestionably. There was this breath of hope and optimism, and I came back from Cambridge to find a whole group of people here who had also read *The General Theory*.*

-John Kenneth Galbraith

"I believe myself to be writing a book on economic theory which will largely revolutionize—not I suppose, at once but in the course of the next ten years—the way the world thinks about its economic problems."

"The long run is a misleading guide to current affairs. In the long run we are all dead"

-John Maynard Keynes

One of the most prolific economic minds of the twentieth century, John Maynard Keynes (1883-1946) immensely influenced the realm of political economy, and a great number of people swear by his economic ideology (Hall, 1989). During the Great Depression, laissez-faire economists overvalued the degree of junction between self-interest and public interest. He saw an inherent flaw in the classical model that focused too much on the aggregate supply-side over the aggregate demand curve. Keynes claimed that market-produced equilibrium might occur at a juncture where labor and capital are

underutilized. The economic modification results in unemployment rather than wage cuts, due to labor unions resisting the downward movement of wages; thus, unemployment leads to decrease in demand and deduction in production and investment (Cohn, 2012).

In a passage from his most well known published work, *The General Theory of Employment, Interest, and Money*, Keynes writes, “the central controls necessary to ensure full employment will, of course, involve a large extension of the traditional functions of government” (Keynes, 1936). Keynes advocated for the government to implement fiscal policies to boost demand, supporting government investment through public projects. Contrary to laissez-faire economics, Keynes simply saw that state intervention in the economy would boost aggregate demand based on infrastructure over monetary easing. After WWII, Keynes supported an internationalist solution at the Bretton Woods Conference in summer of 1944, otherwise known as the Financial Conference (Nadesan, 2011). Representing Britain as a postwar negotiator, Keynes heavily advocated for liberal policies of the Labour government and encouraged the United States to provide England with \$3.75 billion in loans due to Britain’s serious fiscal problems (Block, 1977, p. 62-69).

To counter systemic economic disasters, the Bretton Woods Conference also gave birth to the World Bank and the International Monetary Fund (IMF). Originally, Keynes pushed for the development of a global currency, but the members of the conference decided to peg the U.S. dollar as the world’s reserve currency (Gokay, 2005). During the Depression era and WWII, Keynes encouraged states to combat unemployment, and his advocacy effort for national and international economic management contributed largely to contemporary liberal economic thought. From Keynes’s perspective, greater

government intervention would facilitate the efficiency of the market; thus, instead of replacing capitalism, government intervention would help rescue and revitalize economic activities (Arblaster, 1984, p. 292).

Despite Keynesian post-war solutions and FDR's New Deal headlined by the Glass-Steagall Act, all good things must end. One of FDR's pillars that prolonged the greatest run of economic prosperity in the United States faced major challenges when lawmakers started to reinterpret the banking legislation. The firewall that separated commercial banking transactions from the investment houses gradually dissolved to allow buying and selling of stocks, safekeeping securities and switching funds between bank and stock accounts (Mester, 1996). Next, chapter three will continue with the economic history starting with the rise of Neoliberal era during the 1980s and the repeal of the Glass-Steagall Act that enabled the U.S. financial system to experience another round of deregulatory era.

In conclusion, we witnessed several historic landmarks that revolutionized the global economy from Adam Smith's doctrine of laissez-faire to the implementation of regulatory capitalism through John Maynard Keynes' economic philosophy of government interventionism in the early twentieth-century. By drafting and advocating for legislative regulations, the Glass-Steagall Act truly served the interest of protecting the public sector. Will be seen in the next chapter, the Banking Act of 1933 slowly lost its regulatory powers, and even more during the late-1990s. By end of the 20th century, the United States legislative and executive branches completely repealed the Glass-Steagall Act and in its place, implemented the Gramm-Leach-Bliley Act that further deregulated the United States financial system. The interest of protecting the public's money shifted

as the policymakers deceptively advocated on behalf of corporations, financial firms, insurance companies, and securities.

CHAPTER THREE

HISTORICAL BACKGROUND (1970 TO PRESENT)

Chapter Two addressed the history of economics starting with the Classical Liberals in 1776 led by Adam Smith's model of laissez-faire economics. This style of limited government and self-regulation became the hegemonic economic system throughout the Western world. However, the United States abandoned laissez-faire in response to the catastrophic stock market crash in 1929 that resulted in nationwide bank failures. Senators Carter Glass and Henry Steagall assembled what is widely known as the Glass-Steagall Act of 1933 (Banking Act).

This regulatory reform separated the commercial banks from the investment banks. In effect, the Glass-Steagall Act forced the banks to choose between being a commercial bank or an investment house; thus, the legislation created a firewall between the two banking activities. The Glass-Steagall Act of 1933 stated there is an inherent conflict of interest between the commercial banks (the lending side) and the investment banks (taking an ownership position). This bill ended the conflict of interest by separating the two entities. For example, one could be a commercial bank like Bank of America or an investment house like Merrill Lynch, but under Glass-Steagall, a bank could not proceed to take the responsibilities of both banking activities. The Glass-Steagall Act operated as a form of advocacy by regulating the financial industry in order to protect the national economy ranging from customers, investors, and the banks -- from a catastrophic financial meltdown. Chapter Three is a continuation of economic history starting in the

1970s when the United States entered a new era of global economy led by the well-renown Chicago School of Economics.

From 1944 to the late 1970s, the United States economic system operated under the Keynesian model of economics, which emphasized policy efforts to increase aggregate demand. The model holds that demand creates its own supply. Keynes believed that increased demand reduced unemployment and that interventionist government policy could stimulate demand. The majority of the Western states operated under Keynesian interventionist policies post-WWII era through the 1970s. However, the United States entered a new era of global economics led by the Chicago School in the final decades of the twentieth century. The shift began in the late 1960s when Keynesian policies failed to combat the stagflation caused first by the Vietnam War, rising energy prices and increased competition from countries such as Japan, Brazil, Taiwan, South Korea, and Germany. The stagflation was particularly pronounced in 1973 after the Petroleum Exporting Countries (OPEC) announced oil prices would rise substantially. The recession proved costly for support for Keynesian government programs, such as welfare and full-employment policies (Cohn, 2012). Keynesian policies were held responsible for the stagflation, defined as low economic growth and high levels of inflation. As a result, Chicago School critics argued for abandonment of Keynesian economic policies.

The Rise of Neoliberal Economics

Keynes had nothing to offer those of who had sat at the feet of Simons, Mints, Knight, and Viner.

-Milton Friedman

A War can ravage half a continent, but raises no new issues in economic theory.

-George Stigler

There is no center of intellectual ferment like the University of Chicago.

-James Buchanan

The cold war is over and the University of Chicago has won.

-George F. Will

Milton Friedman (1912-2006), one of the central pillars of Chicago School, received numerous honors, including a Nobel Prize in 1976. He was an economics professor at the University of Chicago and served as an economic advisor to President Ronald Reagan in the 1980s. Originally, a Keynesian economist, Friedman broke free to advocate for monetarism (Nadesan, n.d.). Friedman and other monetarists believed that Keynesian economic philosophy of injecting capital via government projects leads to market destabilization. They advocated for control over fiscal policy and discarded the Keynesian method of stimulating aggregate demand, engineered by government spending and infrastructure investment (Nadesan, n.d.). In regard to the dangers of government, Friedman stated: “Government is an instrument through which we can exercise our freedom; yet, by concentrating power in political hands, it is also a threat to freedom” (Friedman, 1962). Influenced by Adam Smith, Friedman stressed the significance of

classical liberalism and the belief that the market preserves and protects liberty. In his book *Capitalism and Freedom* (1962) states, "A state that takes its citizens' freedom through anything more than necessary action is no better than one that seizes their freedom guided by fascist, mercantilist or even a socialist" (Balaam & Dillman, 2011). Thus, Milton Friedman critically opposes state interference with the market economy. In the quote below, Friedman further explained his contempt for interventionist economic policies.

Wherever we find any large element of individual freedom, some measure of progress in the material comforts at the disposal of ordinary citizens, and widespread hope of further progress in the future, there we also find that economic activity is organized mainly through the free market. Wherever the state undertakes to control in detail the economic activities of its citizens, ordinary citizens are in political fetters, have a low standard of living, and have little power to control their own destiny. (Milton Friedman & Rose Friedman, 1980; p. 54-55)

A champion of the free market ideology, Friedman believed in the significance of advocating for economic freedom for the greater good of the general public. The more responsibility and intervention the state bears on society, it hinders economic freedom for the populace. Friedman advocated for radical changes in national economic policies as it brought fresh ideal that deviated from the Keynesian method of regulated capitalism. The next section will discuss the Glass-Steagall Act under the Neoliberal ideology that begun to weaken its regulatory policies.

The Dismantling of the Glass-Steagall Act and Market De-regulation

As economic prosperity declined in the late 1970s and beginning of the 1980s, Friedman's advocacy of orthodox liberalism started to captivate government policies.

The written works of Milton Friedman and Friedrich A. Hayek (one of the famous members from the Austrian School of Economics) tremendously influenced governmental policymakers starting in the 1980s (Cohn, 2011). Academic scholars often coin the term “neoliberalism” to distinguish these twentieth century thinkers from Adam Smith, David Ricardo and other British and French classical economists from the Chicago School of Economics led by Milton Friedman and George Stigler.

During the Twentieth Century, two prominent political leaders strongly advocated for the resurrection of classical economics: known as the “Iron Lady,” British Prime Minister Margaret Thatcher and the United States President Ronald Reagan (Balaam & Dillman, 2011). The revitalization of classical economics was seen as reinvigorating confidence in the American financial system by repudiating modern liberalism. However, Neoliberal policies advocated by Reagan and Thatcher was not well received by government employees, trade unions and welfare recipients (Cohn, 2012). The outcome of the conflict only led to greater pressure for the government to implement classical/orthodox liberal philosophies such as privatization, deregulation, and free trade and foreign investments (Cox, 1987, p.286-288; Lipietz, 1992, p. 30-31). The transition to the return of classical style of economics led to these implementations:

(1) Advancement in technology, communications, and transpiration has enabled Multinational Corporation (MNCs) and international banks to shift their activities and funds around the globe. (2) The IMF and World Bank provide the least developed countries with financing since the 1982 foreign debt crisis, but these conditions include privatization, deregulation, and liberalization of least developed economic nations. (3) The disintegration of USSR, orthodox liberal economics has spread to the former Soviet bloc’s that are in transition of economically recovering. (Cohn, 2012, p. 83)

Instead of increasing government spending that would boost money supply and generate its own demand, the implementation of supply-side economics decreased taxes. As a result, the top income tax rates in the U.S. slashed from 70 percent to 33 percent in a span of six years (1980-1986) (Balaam & Dillman, 2011). Industries such as trucking, telecommunications, and airlines experienced privatization to expand competition. Although the policies created inequality, neoliberals viewed the market as a positive tool for redistribution of wealth; therefore, in theory, economic growth from the top would eventually find its way for all socioeconomic classes. However, in reality, instead of society as a whole benefiting from the economic philosophy of neoliberalism, the prevalence of deregulation plagued the United States economic system.

As time passed, the focus on the United States economy shifted away from Keynesian economics in favor of the neoliberal model. The Glass-Steagall Act maintained its regulatory powers until the 1980s. From the inception of the law signing it into effect in the 1930s, the large corporate banks advocated to abolish the Glass-Steagall Act (Crawford, 2011). During the 1980s and on, an abundance of congressional legislative bills commenced to repeal the Glass-Steagall Act piece by piece. A single bill did not completely abolish the legislation, but through a series of legislative acts, the Banking Act slowly disintegrated, thanks to administrative rulings that crossed over commercial banking activities and investment activities (Sherman, 2009). In 1986, the Federal Reserve reinterpreted sections of the Glass-Steagall Act's constraints and stated banks could earn up to 5 percent of gross revenues in investment banking business (Sherman, 2009; Crawford, 2011). As the decade ended, the Federal Reserve loosened its restrictions by raising the revenues to 10%. The Federal Reserve justified their policy by

stating that Glass-Steagall's ambiguous definition of the phrase "engaged principally" allowed for multiple reinterpretations (Sherman, 2009).

Known as the "Wizard" of the financial industry, Chairman of the Federal Reserve Alan Greenspan who served no fewer than four presidential regimes (1987-2006), advocated for deregulating the American financial sector (PBS Frontline, 2003). During the mid-90's, Greenspan and the Federal Reserve increased the revenues from 10% to 25% for the allowable percentage of investment banking operations holding companies could own (Sherman, 2009). The reinterpretation of Glass-Steagall continued in 1998 when Citicorp and Travelers Insurance Company merged into Citigroup. Under Glass-Steagall, this transaction was illegal, but the Federal Reserve's reinterpretation of the banking regulation assisted the completion of the merger between Citicorp and Travelers Insurance Company (PBS Frontline, 2003). Some believe this was the major blow prior to its complete demise in 1999. Phil Rubinstein of the LaRouche PAC stated:

In order for the merger to occur, the Glass-Steagall Act had to be overturned. With banking regulation completely abolished, you have bank holding companies, which had subsidiaries of commercial banks; however, what this means is they can now take the deposits of commercial banks and siphon them into speculative investment activity, mortgage-backed securities. (Rubinstein, no date)

During the conclusion of the twentieth century, under the supervision of the Clinton Administration, Citicorp transformed into the most prodigious financial service corporation in the world finalizing the merger with Travelers (Sherman, 2009). The unification of these two corporations violated a major financial law; however, Citicorp heavily advocated for two solid years to repeal the Glass-Steagall Act (Lucus, 2000). *The Wall Street Journal* published an article regarding the merger under the Bank Holding

Act: “The Fed can do what it wants, says Martin Mayer. The Greenspan Fed- strongly supportive of removing the barriers between banking, securities, and insurance” (Wessel and Schroeder, 1998, p. 1-C1). Despite majority of bankers and legislators advocating for consolidation, this merger criminally violated the law:

Under today’s securities laws, proponents of repeal say those abusive practices would be illegal, so Glass-Steagall’s protection is no longer needed. Besides, they argue, the financial-services industry has outgrown the 65-year-old law. The merger plan will face scrutiny by insurance departments in some other states, but unless unexpected opposition emerges among state regulators, the review is likely to be pro forma. In brief states, New York Insurance Superintendent Neil D. Levin also indicated no opposition to the merger. (p.1-C1)

This transaction allowed Citigroup to become the world’s biggest financial company (Sherman, 2009). Many begun to realize the magnitude of the economic shift coming to fruition as the new financial economic era was taking its shape entering the twenty-first century. Through multiple interpretations, the Federal Reserve essentially gutted one of Roosevelt’s regulatory cornerstones, the Glass-Steagall Act. To reiterate, the Banking Act prevented risky and fraudulent banking activities that caused the financial crash of 1929. In the mid-90’s, Alan Greenspan, the Clinton Administration, and the Federal Reserve gave the green light to the regular banks to become deeply involved in investment banking activities, which provoked the conflict of interest in these banks to push for shady financial investments on investors who were ignorant of the consequences (Gupta, 2008).

In 1998, *The New York Times* published an article titled, “Shaping the Colossus” (O’Brien & Treaster, 1999) discussing the benefits of the merger:

The transaction would combine two companies with very different cultures and chief executives. Although Citicorp is much more aggressive

than some of its peers, it still tends to fit the profile of a cautious buttoned-down bank. Travelers, by contrast, are marked by the entrepreneurial style of its chief executives. The new company would vault ahead of other global financial giants, including Bank of Tokyo-Mitsubishi Ltd. And Deutsch Bank A.G., both of which already offer the menu of financial products that Citicorp and Travelers are trying to put together. The size of the deal would easily eclipse the largest merger agreement to date. (O'Brien & Treaster, 1999, section A; p. 1; Column 6)

Despite violating the Glass-Steagall Act, the article further elaborates the future financial implications for the corporations and the customers at stake: "This proposed merger challenged regulators and lawmakers to either end the Banking Act or force the merged company to cut back on its offers to customer (O'Brien & Treaster, 1999, section A; p. 1; Column 6)." To continue the explanation of overcoming the regulatory rigors: "The transaction would have to negotiate a maze of regulations governing the bank industry that were put in place precisely to prevent the creation of the type of company Travelers and Citicorp now aim to put together. Those laws were enacted in response to public concerns about unfettered financial power and the economic consequences when such giants collapse (section A; p. 1; Column 6).

The final blow that completely abolished the Glass-Steagall Act occurred in 1999, when the U.S. Congress decided to pass the Financial Modernization Act or as many called it, the Gramm-Leach-Bliley Act. This legislation passed 90 to 8 in Senate and 362-57 in the House of Representatives, resulting in a majority consensus from the legislative branch (LaBaton, 1999). The Gramm-Leach-Bliley Act (1999) revoked constraints against everything that Glass-Steagall mandated, such as the combination of banks, securities and insurance operations for financial institutions (Sherman, 2009). President Clinton signed the Financial Services Modernization Act of 1999 into law, deregulating

the derivatives market and destroying any remaining vestiges of the Glass-Steagall Act. The abolishment of the regulatory firewall marked a monumental moment of deregulation that shaped the coming future of an economy heavily predicated on the financial sector (Barth, Brumbaugh Jr., and Wilcox, 2000).

In the early part of the 20th century, we saw how legislative advocacy affected the entire economic system by providing stability through regulations. However, as decades passed it also contained a dark side filled with deceptive ideals to promote reckless policies. As stated earlier, the Federal Reserve's constant reinterpreting of the Banking Act severely weakened its powers, which led to its demise in 1999. The Gramm-Leach-Bliley Act of 106th United States Congress not only repealed the Glass-Steagall Act of 1933, but it consequently opened up the market among banks, securities, and insurance companies (Crawford, 2011). This very practice countered the integrity of the Glass-Steagall Act that prohibited the combination of any one institution from acting as an investment house, a commercial bank, and/or as an insurance company.

The support behind the Gramm-Leach-Bliley Act took its shape through legislative, written and speech advocacy. By knocking down the regulatory barriers created during the Great Depression, it allowed banks, investment firms, and insurance companies to sell each other's products, thereby, providing a one-stop shopping for financial services (Crawford, 2011). Clinton's Secretary of Treasury, Larry Summers, who is one of the prominent advocates of deregulation, expressed his optimistic thoughts upon the passage of the Gramm-Leach-Bliley Act:

Today, Congress voted to update the rules that have governed financial services since the Great Depression and replace them with a system for the 21st century. This historic legislation will better enable American

companies to compete in the new economy (LaBaton, 1999).

Senator Phil Gramm, one of the key contributors to repealing Glass-Steagall stated:

The world changes and we have to change with it. We have a new century coming and we have an opportunity to dominate the same way we dominated this century. Glass-Steagall, in the midst of the Great Depression, came at a time when the thinking was that the government was the answer. In this era of economic prosperity, we have decided that freedom is the answer (LaBaton, 1999).

Judging by the quotes above, the common themes of future progress and modernization truly resonated in the public sphere. The policy-makers completely bypassed any concerns of repeating another historical meltdown similar to the Great Depression. These legislative advocates framed and communicated in ways that deceptively advocated for the betterment of the American financial system. The same legislative advocates struck fear in the public by communicating that a regulatory firewall only impeded the progress of the United States financial markets from maintaining its global leadership position. Even though the rhetoric of sustaining the success of the U.S. financial system resonated with the public, the deregulatory legislation only intended to advocate on behalf of the financial industry. The Gramm-Leach-Bliley Act only benefited the financial investors, the top corporate executives, firms and the wealthy hedge funds. The legislation completely neglected the rank and file investors, derivatives market, the American people, and 401k due to the loosened restrictions of securitization.

Senator Phil Gramm, one of the authors of the Gramm-Leach-Bliley Act famously repealed the Glass-Steagall Act, included a stipulation that exempted over-the-counter derivatives like credit-default swaps from regulation by the Commodity Futures Trading Commission (CFTC). In other words, the Commodity Futures Modernization Act was not

liable of credit-default swaps from regulators. This legislation pertains to the contemporary crisis because credit-default swaps crumbled AIG, which the United States taxpayers approximately paid over \$180 billion in bailout money (Dealbook, 2009). What took about fifty years to rebuild and prosper for the overall health of the United States economy, the system was on a verge of obliteration within the first decade of the twenty-first century.

The Present Crisis

Virtually nobody foresaw the Great depression of the 1930s, or the crisis, which affected Japan and Southeast Asia in the early and late 1990s. In fact, each downturn was preceded by a period of non-inflationary growth exuberant enough to lead many commentators to suggest that a “new era” had arrived.

-Bank of International Settlements, June 2007

“If stupidity got us into this mess, then why can’t it get us out?”

-Will Rogers

For approximately a half a century, our nation was able to experience the benefits of legislation that truly advocated for public policy by protecting the national wealth through a series of financial regulations. Many consider the Glass-Steagall Act to be the cornerstone of the financial regulation that brought stability to the American banking system; however, from the 1980s to present, regulated capitalisms shifted in favor of promoting economic deregulation. For example, in 1972, James Tobin proposed an international uniform tax on all spot conversions of one currency into another,

proportional to the size of the transaction (Tobin, 1978). At the tax rate of only one percent, Tobin thought his proposed plan would be enough to discourage temporary speculative capital flows and produce revenues in least developed countries to combat poverty. The pros of Tobin's idea were that it would decrease the potential damage of the global economic crisis and provide impoverished nations with capital; however, the orthodox liberal economists believed it was an unnecessary change because the financial sector was in perfect shape (Eichengreen, 1999, p. 88-90; Michalos, 1997).

Former Federal Reserve Chairman, Alan Greenspan loosened the monetary policy in the early 2000s to promote the well-being of the financial sector of job growth and investments. According to Nadesan (n.d.), financial de-regulation broadened the retail banking and credit opportunities. The loose regulations allowed two major housing institutions, Fannie Mae and Freddie Mac, to initiate a massive purchase of subprime loans. According to a presentation titled, "The End of Growth?" by Satyajit Das, our global economic system operates under "Botox Economics" by flooding in cheap, easy money, and government debt (Das, 2012). The low interest rates set by Greenspan, which intended to expand the economy destroyed the construction in the fields of residential and commercial real estates (Nadesan, n.d.).

Similar to the Great Depression of 1929, the catastrophic economic crisis that unfolded in late 2007 to 2009 did not occur by accident. The contemporary financial collapse commenced with the explosion of the subprime mortgage crisis in the United States housing market that consequently sent the world in a global credit crunch, which ultimately led to macro and micro financial collapses. During the late twentieth and early twenty-first century, the United States housing market drastically soared as a large

portion of the American people invested in the hype of mortgage-generating financial security. Significant portions of mortgage financing was backed by subprime mortgages; subprime borrowers include those who did not qualify for market interest rates for the reasons of credit history, size of down payment, lack of income level, and/or employment prospect (Cohn, 2012).

James K. Galbraith, the son of John K. Galbraith (1908-2006) explains that in the early 2000s, the Bush Administration bypassed all ideas of mortgage regulations as “liars’ loans,” “no-doc loans,” and “neutron loans” were bundled together, rated AAA, securitized, and then circulated until the crashing prices demolished the financial system (Galbraith, 2009). Richard Cohen of the *Washington Post* painted a clear scenario of the housing manipulation through the example of Marvene Halterman of Avondale, Arizona:

At age 61, after 13 years of uninterrupted unemployment and at least as many years of living on welfare, she got a mortgage. She got it even though at one time she had 23 people living in the house (576 square feet, one bath) and some ramshackle outbuildings. She got it for \$103,000, an amount that far exceeded the value of the house. The place has since been condemned. Halterman’s house was never exactly a showcase – the city had since cited her for all the junk (clothes, tires, etc.) on her lawn. Nonetheless, a local financial institution with the cover-your-wallet name of Integrity Funding LLC gave her a mortgage, valuing the house at about twice what a nearby and comparable property. Integrity Funding then sold the loan to Well Fargo & Co., which sold it to HSBC Holdings PLC, which then packaged it with thousands of other risky mortgages and offered the indigestible porridge to investors. Standards & Poor’s and Moody’s Investors Services took a look at it, as they are supposed to do, and pronounced it AAA. (Galbraith, 2009)

As one can see, this is just one example of the financial fraud enabled by the government that took advantage of credulous people taking out mortgages that never had a chance of paying down in reality. The government created an illusion of assuring lenders that housing prices would always rise; therefore, the bad loans could always be refinanced

(Galbraith, 2009). Consequently, numerous subprime borrowers that failed to pay higher rates faced the option of defaulting on their loans, and ultimately owed more than the value of their homes due to declining prices (Cohn, 2012). Unfortunately, what was once considered a lucrative dream turned into a living nightmare as millions of Americans faced foreclosures and evictions from their home.

Even prior to the “economic doomsday,” there was one major warning signal in March of 2008 when one of the top investment firms Bear Stearns filed for bankruptcy, admitting to losing over than \$50 billion from subprime mortgages. The final triggering point occurred on September 15, 2008, when Lehman Brothers, one of the top investment banks in the United States, filed for Chapter 11 bankruptcy. As panic set in, the entire system contracted as if the collapse of Lehman were an anchor dragging down the entire financial system. During that same month, the Federal Reserve of New York intervened and authorized the lending to AIG of \$85 billion in bailouts money. To worsen the outcome, AIG neglected to back the financial derivatives; therefore, when the subprime meltdown occurred, it suffocated AIG’s ability to pay in credit default swaps to their counterparties until the intervention of the New York Fed’s credit line that lent a hand to AIG in more bailout money surpassing over \$182 billion (Nadesan, n.d.; Teitelbaum & Son, 2009).

According to Charles Ferguson’s documentary, *Inside Job* the world’s largest insurance company, AIG sold massive quantities of derivatives called credit default swaps. This particular type of derivative operates similar to an insurance policy. The collapse of collateralized debt obligations (CDO) comprised of pooled mortgages, car loans, student loans and other debt-triggered payouts of credit default swaps (CDS). It was

AIG's job to keep their promise on credit default swaps by paying back the investors for their losses (Ferguson et al., 2010). The investment banks paid rating agencies to evaluate the collateralized debt obligations (CDO), and many of them were undeservedly awarded AAA ratings, which is the highest possible investment grade. Lenders did not care whether a borrower could repay, so they made even more risky loans. For the investment banks, the more CDOs they sold, the higher profit these firms generated. However, in a bizarre fashion, unlike insurance, speculators possessed the purchasing power to buy credit default swaps from AIG in order to bet against the CDOs that they did not own (Ferguson et al., 2010). AIG failed to save enough capital for emergencies to pay counterparties in case of an economic panic; instead, the company excessively paid its employees large bonuses once the contract transactions were completed, thereby encouraging risk-taking actions.

Unlike the Great Depression, the current crisis profoundly failed to fix, let alone even attempt to prosecute the central figures involved in today's financial fraud. Not a single financial executive served time in prison, which prompts the question, where is our Pecora Commission? Instead of prosecuting guilty individuals, the government created moral hazards that hooked the taxpayers to bailout failing institutions such as AIG by forfeiting over \$180 billion. NYU economist Nouriel Roubini states the bailouts of these financial institutions such as Freddie, Fannie, AIG, large banks and other institutions and corporations added an additional seven trillion dollars to public debt (Fallows, 90; Nadesan, n.d.). The government bailout efforts in response to the 2008 crisis was such an atrocity that economist Michael Hudson argues, "This is the largest and most inequitable transfer of wealth since the land giveaways to the railroad barons during the Civil War

era” (Hudson, 2008). To worsen the outcome, *Bloomberg* reported in August 2011 that current Chairman of the Fed Ben Bernanke gave the green light to lend the mega-banks \$1.2 trillion of taxpayers’ money to “save” the U.S. economic system from falling into an economic depression (Keoun & Kuntz, 2011).

It has been nearly five years since the post-mortem of the Great Recession of 2008. Unfortunately, the volatility of the financial industry has gotten much worse. In short, from the financial institutions, to the government, to the public and private sectors, they have collectively failed to learn the lessons of the past two decades. The financial giants and Wall Street have circumvented all the laws and rules such as the Volcker Rule proposed by the former Fed Chairman, Paul Volcker. The Volcker Rule bans banks from taking risky speculative trading with federally insured money. The Volcker Rule was launched in July of 2012, but the final provisions are significantly weaker than the original proposal due to the feud between legislators, regulators, and bank lobbyists. In an interview with a financial expert Satyajit Das on a New Zealand news station, he discussed the powerful influence of bank lobbyists resisting regulatory solutions (Tarrant, 2012):

I will give you one example. In the United States there is a rule called the Volcker Rule, which is designed to prevent the banks from trading with their own money. But the problem is the rule has been watered down and made so complex, it is 270 pages long and its got loopholes everywhere. I had a lovely conversation with a lawyer who said he would be embarrassed if he could not get one of his clients to get through one of the loopholes. Essentially, we are not making any progress. There is a lot of activity, but have yet to see much achievement. (Tarrant, 2012)

The Volcker Rule does not necessarily separate banking activities; instead, it mainly prohibits proprietary trading of dealing in securities and other financial instruments,

rather than on behalf of the customers (Sweet Jr. & Christiansen, no date). It also imposes additional capital requirements on shadow banks (unregulated activities by regulatory institutions) engaged in proprietary trading. According to the definition on Investopedia, the shadow banking system came under heavy fire during the subprime meltdown in 2008 because it managed to escape regulations due to not accepting traditional bank deposits. The consequence led to employing higher market, credit, and liquidity risks, and failed to provide capital requirements to compensate with those risks. Lastly, the Volcker Rule restricts banks' ownership stakes in hedge funds and private equity funds (Mitchell, 2010). The Volcker Rule's ability to limit the power of these mega-banks sounds nice on paper, but the effectiveness of the banking provisions of separating commercial banking from risky securities will most likely to be circumvented by the powerful banking lobbyists.

Since the recession of 2008, fraud is still at the heart of the financial sector as companies, banks, and individuals are responsible for losing millions and billions of dollars. Even with the implementation of the Volcker Rule, the sophistication of technological advancements has made regulations fall further into the depths of irrelevance. Known as High Frequency Trading (HFT) or "black box trading," mainly predicated on complex algorithmic systems, computerized trading transactions occur at fractions of a second at speeds that are beyond comprehension. Today, algorithmic trading accumulates over 60% of all trades nationwide at all the exchanges (Casey Report, 2012). HFT is not only a lucrative method of outperforming competitors, but it has drastically changed how traders strategize. According to Michael Hudson (2010), the average time a stock was held involving HFT was only 22 seconds. These powerful

processors are physically placed in close proximity to electronic exchanges (Nadesan, n.d.). The combination of speed and proximity provides an advantage over traders on the exchange floors as the HFT'ers find an insight into the trading prices. As Ellen Brown (2010) noted, it is similar to poker players peeking in a mirror to see their opponents' hands. With a similar advantage, flash orders allow the program traders to preview the incoming orders, so they have the advantage of leaping in front for gaining profits off the top (Brown, 2010). On any given day, the market performance swings one way or the other for better or worse, as long as the market keeps moving, profits are generated for the HFT'ers (Nadesan, n.d.). One of the alternative media sources, *Zero Hedge*, wrote an article regarding the close relationship between the practice of HFT and the former investment bank, Goldman Sachs. A former investment house, which recently converted to a commercial bank, Goldman Sachs is able to generate lucrative profits through Alternative Trading System's (ATS), which is the ability to trade around the clock. In an attempt to compare the corruption of HFT, *Zero Hedge* states:

As the market keeps going up day in and day out, regardless of the deteriorating economic conditions, it is just these HFT's that determine the overall market direction, usually without fundamental or technical reason. Based on a few lines of code, retail investors get suckered into a rising market that has nothing to do with green shoots or some Chinese firms buying a few hundred extra Intel servers: HTFs are merely perpetuating the same Ponzi market mythology last seen in the Madoff case, but on a massively larger scale. (*Zero Hedge*, 2009)

By taking advantage of the afterhours trading, Goldman Sachs on average profited over \$100 million from 116 out of 194 trading days in 2009 (Durden, 2009; Brown, 2010).

Although the media and the regulatory agencies largely ignored HFT, an infamous incident occurred on May 6, 2010, known as the "Flash Crash." The incident started at

approximately 2:41 p.m.; when the traders watched in disbelief a sharp decline of Dow Jones Industrial by nearly a thousand points, only to see it quickly salvage nearly 600 within a matter of minutes (Buchanan, 2012). According to the investigative report by the SEC, it all started when an individual trader working for a mutual fund company requested a substantial order to sell more than 75,000 futures contracts worth nearly \$4.1 billion, which were tied to the S&P 500. It is normal to see significant transactions take hours to fully process, even with an algorithmic computer processing the orders (Goldstein, 2010). However, a major blunder occurred when the computer completely neglected the price, so this little mishap ripped open the market by sending into a spiral. The failure between two parties triggered other traders to sell stocks and funds, which caused many traders to temporarily step aside to assess the situation. Therefore, the limited number of trade partners at the NYSE sped up the sharp decline in the overall performance of the market. However, according to Robert Whitelaw, a finance professor at NYU, contrary from the SEC report, the Flash Crash was an outcome of traders leaving in purchase orders that would never gain any substantial momentum. According to the *New York Times* (2011), the SEC proposed a regulatory law called a consolidated audit trail that would collect data on trades in real time from all the exchange floors.

Another major financial scandal involves the mega-banks in a LIBOR manipulating scandal that occurred during the summer of 2012. According to *The New York Times*, the acronym for LIBOR is London Interbank Offered Rate. Simply put, Libor is the average interest rate at which large international banks such as Barclays in London can borrow from other banks (Times Topics: Libor Barclays Interest Rate

Manipulation Case, 2012). The banking scandal was officially reported late June 2012 and new reports are continuing to arrive since the LIBOR scandal hit public.

When a British financial mega-bank, Barclays, was fined \$450 million for manipulating the Libor rates, the CEO of Barclays Bank, Robert Diamond, resigned in disgrace. Reports indicate that he will not be the last CEO to testify in court because other financial giants such as JPMorgan Chase, Citigroup, HSBC, and others are under heavy investigation. According to Reuters report of the LIBOR scandal:

More than a dozen banks are under investigation by authorities in Europe, Japan and the United States over the suspected rigging of the London interbank offered rates, a key interest rate used in contracts worth trillions of dollars globally. (MacLellan, Tostevin, 2012)

There have been up to 16 banks linked to the manipulation of LIBOR rates in 2008, but only one bank (Barclays) has confessed to criminal misconduct.

During middle of the financial crisis from 2007 to 2009, the mega-banks around the world attempted to appear stable, so these dozen or more banks offered lower than usual borrowing rates (AccountingDegree.net, 2012). The manipulation of LIBOR allows bank balance sheets to appear healthier at the expense of the public. The banks involved were lending money in the market at lower interest rates and in returned collected less profit. The clients that received the payout profits such as the cities, governments and financial institutions, which involve hospitals, fire departments, police departments, school, local libraries and so on all suffered due to insufficient shares of lending profits in a distorted market. One of the prolific financial columnists for the Rolling Stone Magazine, Matt Taibbi concisely stated:

This is the world's biggest banks stealing money that would otherwise have gone toward textbooks and medicine and housing for ordinary

American, and turning the cash into sports cars and bonuses for the already rich. It is equivalent of robbing a charity or a church fund to pay for lap dances. (Taibbi, 2012)

In June 2008, the former Secretary of Treasury and former Secretary of the New York Federal Reserve, Tim Geithner sent a private message to British regulators concerning the potential manipulation of LIBOR. Since the LIBOR manipulation scandal went public, Geithner is under heavy fire for the lack of action concerning the central role LIBOR that plays in the global markets. In an article by *The Wall Street Journal*, Geithner sent a letter to Mervyn King (Bank of England Governor) demanding him to “eliminate incentive to misreport” by banks (Treanor & Rushe, 2012). During the time of the financial crisis, “Fed officials became deeply concerned about the functioning of short-term lending markets in late-2007 to early 2008. One problem was that large banks engaged in the development of short-term loans to fund their operations and their borrowing costs soared” (Paletta & Hilsenrath, 2012). The ongoing investigation in the LIBOR manipulation scandal is examining whether banks purposely provided false lending rates, affecting the interest rates for trillions of dollars in financial banking products. Milliken and Ahmann (2012) reported LIBOR is used for \$550 trillion of interest rate derivatives contracts and influences rates from credit cards to mortgages to student loans. James Rickards of Tangent Capital claimed the monstrosity of the Libor manipulation scandal:

So big I don't think people have got their minds around it. This is the largest financial scandal I have seen in my career. If \$500 trillion of swaps are tied to Libor and the rates are manipulated by 10 basis points over a five-year span, which equates to \$2.5 trillion of fraudulent dealings. The entire situation may get so out of control that Congress may have to intervene to limit the damage because it has great potential to destabilize the global banking system. (Task, 2012)

In an article titled, “A Huge Break in the LIBOR Banking Investigation” written by Matt Taibbi of *Rolling Stone Magazine* breaks down the sheer amount of fraud that is tied to the LIBOR scandal:

This is unbelievable, shocking stuff. A sizeable chunk of the world’s adjustable-rate investment vehicles is pegged to Libor, and here we have evidence that banks were tweaking the rate downward to massage their own derivatives position. The consequences boggle my mind. For instance, almost every city and town in America has investment holdings tied to Libor. If banks were artificially lowering the rates to beef up their trading profiles that means communities all over the world were cheated out of ungodly amounts of money. (Taibbi, 2012)

Since the 1980s, our world has been living under an imperial system based on money and power. Carter Glass managed to draft a legislation that advocated for the restoration of the American financial system. Who is willing to be the next Carter Glass or Ferdinand Pecora? These two individuals in particular knew the implications as they promoted legislative advocacy that paved a road for justice and economic stability. Our nation needs a new direction that reflects the principles of the FDR, Carter Glass, Pecora, and the founders. One must advocate not only against the kleptocratic style of government that allows elites to take advantage of government corruption by extending their personal wealth and political powers, but also the advocates must expose the hidden financial corruptions through new transparent measures.

The Bush and Obama Administrations responses to the economic crisis have been characterized by large bailouts of large financial firms and institutions and failures to prosecute top banking executives. William K. Black, who criminally prosecuted individuals responsible for the Savings and Loans crisis in the late 1980s, slammed the responsible financial culprits for committing fraud by gambling away approximately \$11

trillion in household wealth, eliminating six million jobs and five more million job that would have been available (Nadesan, n.d.). Instead of learning from the past mistakes, the world of economics and finances is more corrupt than ever as it trivializes financial practices such as high frequency trading, tolerates the unregulated derivatives market, enables re-hypothecation, etc. The narrative limits and self-censorship of mainstream media discourses constrain popular understanding of the extent of Wall Street's fraudulent culture. Chapter Four will identify the discursive themes found in mainstream media by analyzing news reports from *The New York Times* and *The Wall Street Journal* representing the Great Depression and the present crisis.

CHAPTER FOUR

DISCOURSE ANALYSIS

By briefly examining the global economic history, Chapters Two and Three provided a condensed historical framework of economic landmarks that took place dating from the seventeenth century up to the contemporary era. Chapter Four will explore the media's role in framing and shaping interpretations of the complicated system of economic, political, social and market forces that rocked the nation in the 1930s and again in 2008. Professor Delli Carpini (2004) from University of Pennsylvania emphasizes the power of the media in shaping public opinion, "As one of several socializing agents, the media provide much of the 'raw material' that make up social and political, attitudes, and schema" (p. 408). The media, I argue, have shaped interpretations of financial crises, thereby influencing government's regulatory responses. The media analysis in Chapter Four compares and contrasts the stock market crash of 1929 and the implosion of the housing bubble in 2008 by looking at articles from two mainstream publications: *The New York Times* and *The Wall Street Journal*.

This chapter identifies three major themes that emerge from analysis of *The New York Times* and *The Wall Street Journal* news accounts. The first major theme concerns the pseudo-heroes (bankers) portrayed in the media discourses during the Great Depression and during the contemporary era. The second theme of this chapter details the criminality aspects of how individuals and institutions are portrayed by the media over time. The third and final theme of this chapter addresses and compares the regulatory

responses during the Great Depression and the 2008 financial crisis. The analysis compares policy responses in relation to these media representations.

The data for this chapter will examine articles from the two most prominent United States newspaper companies: *The New York Times* and *The Wall Street Journal*. These two publications have a long-held reputation of covering historical moments that occurred in the U.S. dating back to the late nineteenth century, so it is feasible to conduct a meticulous investigation of events occurring in two separate timelines dating back to 1929. *The New York Times* and *The Wall Street Journal* ranked first and third in national standing according to the Audit Bureau of Circulations (2012). These two companies not only draw readers from all fifty states, but attract a global audience as well. The data collection will primarily be acquired electronically through academic databases such as Lexis/Nexus, and ABI/INFORM.

The timeline for the Great Depression will be narrowed from 1929 to 1937, and the Great Recession will be narrowed from 2007 to 2009. However, there was one exception in data analyzed when it came to the analysis of the Volcker Rule. The date range had to be expanded from 2007 to 2010 because President Obama first embraced the regulatory act during the beginning of 2010. Articles from *The New York Times* were analyzed from both eras. On the other hand, these databases for *The Wall Street Journal* created complications because the availability of articles at ASU only covered the contemporary era. Searches in these two media outlets used more than one database. Using key word searches to filter through large numbers of articles simplified searches and allowed for scanning of hundreds of headlines, facilitating identification of recurring themes and frames. Detailed searches helped narrow down the articles, but ambiguous

searches such as “AIG” resulted in hundreds of articles. For example, using ProQuest, I would select *The New York Times* and type key words such as “Glass-Steagall Act” during the 1932 to 1937 selecting news, editorials, and articles. Other examples of key words include: Banking Act, The Great Depression Headlines, Glass-Steagall bill, banking regulation, stock exchange crash/collapse, economic crash, banking fraud, Pecora commission, Federal Reserve, Carter Glass bill, Henry Steagall bill, criminal bankers, National City Bank fraud, Charles Mitchell banking fraud, financial speculation, AIG bailouts, banking bailouts, Fannie Mae and Freddie Mac bailouts, housing speculation, Bear Stearns purchase, Banks acquisitions, Bank mergers, Wachovia and Wells Fargo, financial institutions, bailouts, etc.

Chapter Four will utilize APA 6th edition formatting style using block quotations of excerpts from the primary data sources to illustrate and document critical analysis. Discourse analysis will be the methodology employed to identify and analyze recurring ideas and themes in the data. According to Hepburn and Potter (2007), discourse analysis examines the text through analyzing and transcribing written texts, deciphering the arguments, metaphors, and themes within the text. Discourse analysis is an outlook on the complexity of human language and its essential connection to the fundamental issues in social sciences (Wood & Kroger, 2000). The ultimate goal of analyzing language is to seek the in-depth significance of the text(s) that is important to society.

Theme One: High Praises, Heroes and Lies during the Great Depression

The first major theme has been named “high praises, heroes, and lies” because the analysis of Depression era coverage revealed a striking shift in tone in newspaper accounts of the key players in the financial industry and in representation of the industry as a whole. Prior to the Pecora Commission in the 1930s, *The New York Times* provided optimistic headlines and articles regarding heavy losses around the time of “Black Tuesday” in the stock market. To combat the negative discourses, the publication framed the bankers as a voice of reason, deceiving the public concerning long-term problems. However, as the Pecora Commission findings were reported *The New York Times* tone changed and “lies” appeared as a dominant theme. The heroes of finance were revealed to have been duplicitous.

Analysis of media accounts revealed that the financial industry during the “Roaring Twenties” possessed “celebrity” status (Senate.gov, no date). President Hoover praised the financial industry at an investment banking convention stating:

Your work is of double value. On the one hand, it helps to prevent our reservoir of capital from being drained into unsound and unprofitable ventures. On the other hand, it is important to secure a greater participation of the public in its enterprises, which are essentially sound and profitable. Such widespread participation tends to the dissemination of knowledge of the needs and achievements of industry. Such knowledge cannot fall to be helpful in furthering a mutual understanding between business and the public in general. (Bankers see an era of long prosperity, 1925, p. 4)

The praises for the financial industry came at a time during the peak years of economic prosperity during the “Roaring Twenties.” However, the discourse started to shift from

“Bankers See Era of Long Prosperity” in 1925 to “5 Bankers Called in Market Inquiry” in the early 30s.

As revealed here, the bankers were represented as valuable to the society. By end of the 1920s, a major theme arose from *The New York Times* article’s trivializing the deep-rooted problem of the economic crisis. During any crisis, the publication’s job is to inform the audience using facts such as numbers, dates, statistics, and the events that led to the outcome(s), but also possess the ability to formulate civic sentiments. Below, there are four major headlines from *The New York Times* that trivialized the market’s horrid performances around the time of “Black Tuesday.” During the developing stages of the market crash from October 25 to 30, a series of daily headlines emerged that promised optimistic conditions despite record losses. The major headlines from the paper states:

WORST STOCK CRASH STEMMED BY BANKS; 12,849,650-SHARES DAY SWAMPS MARKET; LEADERS CONFER, FIND CONDITIONS SOUND (*The New York Times*, 1929, Oct. 25)
STOCKS GAIN AS MARKET IS STEADIED BANKERS PLEDGE CONTINUED SUPPORT; HOOVER SAYS BUSINESS BASIS IS SOUND (*The New York Times*, 1929, Oct. 26)
STOCK PRICES SLUMP \$14,000,000,000 IN NATION-WIDE STAMPEDE TO UNLOAD; BANKERS TO SUPPORT MARKET TODAY (*The New York Times*, 1929, Oct. 29)
STOCKS COLLAPSE IN 16,410,030-SHARE DAYS BUT RALLY AT CLOSE CHEERS BROKERS; BANKERS OPTIMISTIC, TO CONTINUE AID (*The New York Times*, 1929, Oct. 30)

The headlines above disguises the core issues with false hopes of future recovery and exhibits the desperation by the mainstream press to avoid a financial panic that extends from Wall Street to Main Street. All four of these headlines are carbon copies as they commence the article by utilizing negative discourses, “Stock Prices Virtually Collapsed,” “Hurricane of Liquidation,” “Chaos in Wall Street,” and “Overwhelmed by Selling

Orders,” then proceeding to end with a positive outlook such as, “Business Basis is Sound,” “Bankers Support the Market” and “Sound Conditions.” The narratives of the article essentially takes the readers through the major transactions that occurred in the previous day ranging from massive sell-offs to causes of the market decline, and the uncertain economic outlook. Some articles ended on an optimistic note. For example, “The New York and out-of-town commodity markets also experienced a recovery of good spirits, which in many cases were translated into gains in prices for the day” (Stock prices slump, 1929). While others were pessimistic, “Failure aboard had diverted a tremendous volume of selling to the United States, and under these influences the market continued to sag until it literally crumpled of its own weight” (Stocks collapse, 1929).

Contrary to the reckless bankers during the Great Depression, Ferdinand Pecora, a Manhattan prosecutor investigated Wall Street’s phony banking and stock brokerage practices under the United States Senate Committee on Banking and Currency.

According to Jacobi (2009), Wall Street sold roughly \$25 billion of rubbish stocks investors during the economic boom; however, Pecora’s investigation was able to stop more than a billion dollars from falling into the hands of the financial crooks. Pecora’s investigation revealed the fraudulent culture behind Wall Street as they accumulated their wealth on predatory financial practices:

The old regime of unlimited license may be said to have definitely come to an end. The testimony had brought to light a shocking corruption in our banking system. A widespread repudiation of old-fashioned standards of honest and fair dealing in the creation and sale of securities and merciless exploitation of the vicious possibilities of intricate corporate chicanery. The public had been deeply aroused by the spectacle of cynical disregard of fiduciary duty on the part of many of its most respected leaders of directors, who conveniently subordinated their official obligations to an avid pursuit of personal gain; of great banks, which combined the

functions of a bank with those of a stock jobber, of supposedly impartial public markets for the sale of securities, actually operated as private clubs for the individuals benefit for their members. (Jacobi, 2009)

To change the landscape of the United States financial system, Ferdinand Pecora's investigative report candidly exposed the financial executives that indulged themselves in pursuit of personal profits. The abuse of power and wealth among the Wall Street bankers empowered the public to advocate for systemic changes based on regulatory structures. Overall, Pecora's audacity to confront these bankers for financial fraud helped emerge Pecora as a hero during the Great Depression.

Theme One: High Praises, Heroes and Lies during the Present Crisis

Lies were not a dominant theme in *The New York Times* and *Wall Street Journal* coverage of the 2007-2009 crises. Instead of emphasizing duplicity, the news reports emphasized complexity and systemic risks. Heroic government figures were featured in these reports as technocratic saviors of the system. Three agents stood out as the saviors of our financial system: Tim Geithner, Ben Bernanke, and Hank Paulson. According to media accounts, with hard work and persistence from these men, the global economic system avoided a "financial Armageddon." The executives of the financial firms implicated in causing the crisis were not represented as criminals, but rather were represented as risk-seekers who handed over their companies to dangerous quantitative analysts.

During the contemporary era, bankers may not have received the highest praises; however, powerful policymakers and central bankers in Washington such as Tim

Geithner (New York Fed), Hank Paulson (Secretary of Treasury), and Ben Bernanke (Chairman of Fed) received some of the highest praises for their heroic efforts during the 2008 economic turmoil. After the collapse of investment bank, Lehman Brothers, Treasury Secretary Hank Paulson organized a \$700 billion bailout plan to “rescue” the financial sector from a complete annihilation.

The \$700 billion financial rescue that Congress votes on today must surely rank as the least popular legislation in modern times. And yet it deserve a pass because in reality it is an attempt to shield middle America from further harm caused by the mistakes of Wall Street and Washington. Treasury Secretary Hank Paulson’s plan should do some good, and if executed properly shouldn’t cost taxpayers anything close to its \$700 billion showroom price. (A main street rescue, 2008)

Although, the article stated, “it shouldn’t cost taxpayers anything,” large bulk of the bailout money came from the taxpayers to relieve the troubled financial institutions. The American International Group Inc (AIG), one of the world’s largest financial institutions devised a bailout plan with the chairman of the New York Fed, Tim Geithner:

Mr. Geithner was the driving force behind the government takeover of insurance giant AIG –that has had to be rescued with more taxpayer capital. The most frustrating part of the AIG episode has been the New York Fed’s lack of transparency, both about the nature of the “systemic risk” that required the takeover and why it was superior to bankruptcy. (Secretary of bailouts, 2008)

The totality of “rescuing” AIG approximately reached \$150 to \$180 billion of taxpayers’ money. The article begs the question, “why was AIG the exception over other financial institutions such as Lehman Brothers that went under?” The lack of transparency by Geithner and the New York Fed displayed that they were willing to inject large sums of capital to keep AIG afloat over other financial institutions that failed. Geithner’s financial

decisions gained considerable attraction as he left the New York Fed to succeed Hank Paulson as the new United States Secretary of Treasury under President Obama:

Mr. Geithner gained respect among Wall Street chiefs over the past year for his hands-on role in the credit crisis. For instance, he was instrumental in engineering the government-assisted rescue of Bear Stearns. Mr. Geithner was one of the first officials to warn about a financial instrument, known as a credit-default swap. (Weisman, Solomon & Hilsenrath, 2008)

However, Tim Geithner was not alone in the grand scheme of “rescuing” the American financial system from utter chaos as Fed Chairman Ben Bernanke received high praises for his efforts. Originally selected by George W. Bush as Fed Chairman in 2006, Bernanke looked to maintain his status as world’s top central banker:

As central bankers and economists from around the world gather on Thursday for the Fed’s annual retreat in Jackson Hole, Wyo., most are likely to welcome Mr. Bernanke as conquering hero. In Washington and on Wall Street, it would be a surprise if President Obama did not nominate Mr. Bernanke for a second term. (Andrews, 2009)

In 2009, newly elected President Obama decided to nominate Ben Bernanke to a second term as chairman of the Federal Reserve. Despite the positive reputation on these central bankers, few politicians became skeptical of their financial achievements regarding the crisis:

Senator Christopher J. Dodd, Democrat of Connecticut and chairman of the Senate Banking, Housing and Urban Affairs Committee, said in an interview that he would use forthcoming Congressional hearings to press Mr. Bernanke and Mr. Paulson to defend their decision to rescue AIG, and to prod the administration to do more to address the problems in the housing market. Mr. Dodd said twice pressed for assurance that the administration and the Fed had the legal authority for the bailout of AIG and Mr. Bernanke and Paulson said that they believed the Fed could aid any company posing systemic risk to the economy. (Dash & Ross-Sorkin, 2008)

Senator Dodd's inquiry on the central bankers that bailed out the financial sector using 700 billion dollars of taxpayers' money raised legal skepticisms, particularly on AIG. However, Senator Dodd's questioning became a non-issue once Bernanke and Paulson justified the bailouts by using Fed's monetary policy. This also communicated that the Fed can justify any type of monetary policy in a time of an economic downturn. In addition, one of the notorious Wall Street bankers, Jamie Dimon of JPMorgan Chase received high praises for his role during the financial crisis:

Heroic figures have been a rarity amid the evils and embarrassments of the current economic crisis. Duff McDonald claims to have found one in the form of the chairman and chief executive of JPMorgan Chase. Mr. McDonald described the defining events in Mr. Dimon's life and career that led him to become such a powerful force during the financial crisis. Mr. Dimon was "quite literally the only chief of a major bank to have properly prepared for the hundred-year storm that hit Wall Street. (Hurt, 2009)

As one of Wall Street's top investment banker, JPMorgan's Jamie Dimon holds an impregnable reputation as the investment bank grew larger during the financial crisis in 2008.

During a time of crisis, the populace seeks a hero to escape from heavy turbulence despite the repercussions. Media publications possess the discourse to manipulate or misinform the public that changes the entire complexion of the news story. The next section will examine the second major theme of criminality during the Great Depression (1929) and the Great Recession (2008).

Theme Two: Investigations during the Great Depression and the Great Recession

Once the stock market crashed in 1929, the federal authorities searched for answers to why the stock market collapsed during an era of economic boom. The U.S. Senate Banking Committee assembled a legal team led by Ferdinand Pecora to investigate criminal transaction involving the financiers. Earlier accounts tend to offer high praise to the financiers for economic opulence during the 1920s; however, the discourse shifted as disclosures of financial fraud became rampant in the newspapers. During the 1930s, *The New York Times* extensively covered the financial allegations involving Charles Mitchell of National City Bank, the second largest bank at the time for speculation and reckless securities. The widespread reporting made an example out of Charles Mitchell as one of the key figures responsible for the Great Depression.

However, newspaper publications during the current crisis reluctantly mention the high-level banking executives that may have been responsible for the crisis. Instead of an assemblage of federal prosecutors similar to the Pecora Commission in 1932, the contemporary articles communicate a lack of resources, staff, and urgency to hunt down the individuals responsible for the current economic crisis.

To expose the underlying causes of the financial crisis that triggered a shockwave of enormous losses from the banks to public and private sectors, the United States Congress called for an investigation. In 1932, the Senate passed Resolution 84, which was an investigative committee created by the United States Congress Banking and Currency to inquire individuals that participated in financial fraud. The investigation was originally formulated under a Republican-dominated Senate Committee; however, after a

year of little progress, the committee decided to employ an assistant district attorney named Ferdinand Pecora (Moyers, 2009).

Criminality during the Great Depression (1929)

In 1933, The New York Times published various articles regarding National City Bank and their involvement relating to the sales of insurance and securities. The article claimed six members of National City Bank were scheduled to be subpoenaed including the chairman, Charles Mitchell. The article described Mitchell's testimony regarding his involvement in the manipulation of Anaconda Copper Company (5 bankers called in market inquiry, p. 26). The New York Times covered the investigation and reported on findings. One article is particularly noteworthy for its critical discussion of investigative findings, "National City Sold Bank Stock Short During 1929 Boom." The article cites testimony by National City Company's President Hugh B. Baker that the company sold 1,359,000 shares of National City Bank's stock prior to the crash. The outlined three major actions caused by the National City:

- (1) Assuming the successful outcome of the proposed merger of the Farmers Loan and Trust Company with the National City Bank, the National City company sold short, at least 'technically,' on a large number of shares of the bank's stock and borrowed 30,000 shares from Charles E. Mitchell chairman of the boards of both National City institutions.
- (2) The National City Company gave the brokerage firm of Dominick & Dominick a gratuitous option on 32,000 shares of National City Bank stock at prices substantially below those prevailing at the time of the agreement, which yielded a profit of \$354,088 to the brokerage firm.
- (3) Hugh B. Baker borrowed \$75,000 in the form of 1,500 shares of National City Bank stock from the bank's purchasing plan and turned it over to a brother to support the position of the latter's partnership in a brokerage house which had been imperiled by the stock market collapse. (National city sold bank stock short during 1929 boom, 1933, p. 1)

The excerpts above described some of the monetary transactions committed by the National City Bank during the time of “Black Tuesday” that provided the federal prosecutors with evidence of their shady business dealings.

Known as one of the notorious bankers of the early twentieth century, the legal battle between Charles Mitchell of The National City Bank and prosecutor Ferdinand Pecora steadily revealed the financial corruption that contributed to the economic downturn. An article by *The New York Times* published on May 3, 1934, titled, “Mitchell Denies Income Tax Fraud (1934, p. 11)” detailed his alleged crimes starting with 8,500 shares of Anaconda Copper stock purchased at \$116.31 a share in 1930, but sold at \$27 and similar actions occurred when Mitchell subsequently repurchased the stock. Mitchell confessed that he organized the sale to write off the loss against his income tax and that John D. Ryan, a member of the National City Bank board, arranged the sale for him. Mitchell denied his awareness of John Ryan’s decision of repurchasing the stock for him (p. 11). In another article by *The New York Times* titled, “Mitchell Pictured as ‘Ruined’ Patriot” (1933, p. 1), it reported the details of the speculation behind Mitchell’s resignation as the chairman of the National City Bank and the National City Company.

Lawyers for the government and for the defense delivered their opening addresses to the jury before Federal Judge Henry W. Goddard at Mr. Mitchell’s trial on the charge of evading payment of \$850,000 Federal income taxes for 1929 and 1930. (Mitchell pictured as ruined patriot, 1933, p. 1)

United States Attorney, George Z. Medalle accused Mitchell of deliberately defrauding the government and shifted the burden of his own taxes by the selling fraudulent stocks to his wife and friends and failed to report a large payment to the management fund of the National City Company. (p. 1).

The investigation disclosed Mitchell's devastating losses after the stock market crash in 1929 involving his personal income ranging from 25 to 30 million. Mitchell offered all of his property as collateral for a \$12 million loan he received from J.P. Morgan & co., which was downsized to \$6 million. This was enacted in response to salvage what was left of National City Bank (Mitchell pictured as ruined patriot, 1933, p. 1). However, Max D. Steuer, a counsel for the defense not only justified Mitchell's business transactions, but also painted the banker as a righteous man who is suffering from the effects of the financial depression as Steuer stated:

Mrs. Mitchell could have sold at a profit while she owned the stock, except that Mr. Mitchell believed the stock would go higher and wanted her to hold it order to 'make her fortunes.' He repurchased the stock in a natural desire to protect his wife from loss. (Mitchell pictured as ruined patriot, 1933, p. 1)

Aside from portraying Charles Mitchell as a noble executive who based his decisions on an immense false impression, Mitchell blamed the federal government for waiting approximately four years to prosecute him. In defense of Mitchell, Steuer claimed: "Somebody must be made a victim when mob psychology is in control. Who is to be made the victim, some underling? No, we need some big fish, so it's Mitchell" (Mitchell pictured as ruined patriot, 1933, p. 1).

Clearly, the tactic behind this particular discourse discredits the criticisms behind the banker's involvement in the stock market crash. Steuer further added:

Every man is honest and decent who used every possible legal means of reducing the total tax he may be called upon to pay. It is a recognized, absolutely legal, proper, and moral practice from every point of view. Mr. Mitchell has not, does not, and will not ever deny that his purpose in making the sale was to fix a loss on that day to deduct from his income tax (Mitchell pictured as ruined patriot, 1933, p. 1).

Nevertheless, the plea and justification of Mitchell's actions from the defense counsel fails to hold in court as evidence showed his shady financial transactions between National City and JPMorgan & Co.:

Charles Mitchell pledged with J.P. Morgan & Co., of 30,000 shares of National City Bank stock, which he owned outright against a credit of \$12,000,000, out of which the Morgan firm paid for the first 28,300 shares of National City Bank stock purchased on that date, keeping the purchased stock as collateral. Mr. Steuter denied that Mr. Mitchell took the stock at the low price, saying that he took the first 28,300 shares regardless of price. The stock was bought at an average of \$367, and Morgan's paid out \$10,600,000. When Mr. Mitchell sold the 18,300 shares to establish a tax loss, he sold to his wife in order to avoid throwing it into the market. (Mitchell pictured as ruined patriot, 1933, p. 1)

Steuer continued to validate Mitchell's actions by uttering the nationwide economic "doomsday" scenario: "If he had sold it in the regular way through a broker, the effect might have been disastrous, creating a nation-wide havoc" (Mitchell pictured as ruined patriot, 1933, p. 1).

Despite the justification from Steuer's client, the prosecution fired back at Mitchell by expressing:

Mr. Mitchell was placing everything he had at the risk of the situation, because he had absolute confidence in the United States and in the National City Bank and in the security market. The fact remains that he put up his fortune as a sacrifice for the institution he headed. (Mitchell pictured as ruined patriot, 1933, p. 1)

Even though Mitchell appeared to be oblivious of his own company's financial transactions, it is tough for anyone justify Mitchell's dishonest financial dealings that greatly destabilized the stock market.

In a published article titled, "Mitchell Penalty on Tax Demanded" (1934, p. 20), the formerly disgraced president of the National City Bank, Charles Mitchell, came under heavy fire for tax fraud:

Notwithstanding his acquittal on criminal charges of income tax fraud, Charles E. Mitchell, must pay the government \$1,275,644 in taxes in penalties for 1929 and 1930, as it was argued yesterday with the Board of Tax Appeals in Washington. The government's lawyers undertook to show that although Mr. Mitchell had an income of about \$3,500,000 in 1929, he paid no income tax for that year and that in 1930, with an income of more than 750,000, he also failed to pay any tax. (Mitchell penalty on tax demanded 1934, p. 20)

In addition to Mitchell's unpaid taxes, the prosecutor's investigation of Mitchell's stock that he sold to his wife turned out to be an illegal transaction.

The sales of 18,000 shares of National City Bank stock, which Mr. Mitchell alleges he sold to his wife in December, 1929 was a sham sale and that former bank president's act in claiming a tax deduction of \$2,827,305 as a loss resulting from the sale constituted fraud with intent to evade payment of taxes. (Mitchell penalty on tax demanded, 1934, p. 20)

To continue, Mitchell reached insolvency approximating an excess of \$3.5 million as he repurchased the stock from his wife at the original price of \$212. The prosecution team unleashed more damning evidence against Mitchell pertained to the sale of 8,500 shares of Anaconda Copper to W.D. Thornton on Dec. 26, 1930, at a loss of \$758,918.25 making the sale fraudulent. Mr. Mitchell's failure to include his income tax return of \$666.666.67 from the National City's management fund in July 1929 also constituted fraud. (Mitchell penalty on tax demanded, 1934, p. 20)

About a year later, *The New York Times* released an article titled, "Mitchell Guilty, Tax Board Rules" (1934, p. 1) indicated the Board of Tax Appeals in a civil suit ruled that Mitchell must pay in 1.1 million in penalties and taxes (Mitchell Guilty, Tax Board

Rules, 1934, p. 1). Despite his criminal charges of failing to pay his income taxes in 1933, “The tax board held that this did not bar it from finding fraud in the civil proceeding before the board. Conviction of fraud in a civil suit imposes a penalty equal to 50 percent of the deficient tax” (Mitchell Guilty, Tax Board Rules, 1934, p. 1). To simplify the financial fraud involving Charles Mitchell and The National City Bank, the article briefly formulated six parts explaining the ruling:

1. Mr. Mitchell was guilty of fraud in claiming in his 1929 tax return a \$2,872,305.50 loss on 18,300 shares of stock sold to his wife and later repurchased. The Board upheld the government’s argument that this was not a bona fide sale.
2. Mr. Mitchell was guilty of fraud in failing to include in his 1929 income \$666.666.67 received from the National City Company’s management fund, notwithstanding the fact that he subsequently signed a receipt acknowledging the money to be an overpayment subject to later repayment. These two omissions made his 1929 return “fraudulent with intent to evade tax” the board held.
3. Mr. Mitchell’s 1930 income tax return was also made fraudulent by his failure to include \$54,900 in dividends received on the National City Bank stock sold to Mrs. Mitchell in 1929.
4. Mr. Mitchell actually sustained a loss of \$758,918.25 in 1930 on the sale of 8,500 shares of Anaconda Copper Mining stock to W. D. Thornton. This was the only point decided in Mrs. Mitchell’s favor.
5. That acquittal of Mr. Mitchell by a jury in New York in 1933 on criminal charges of income tax evasion did not prevent the finding of fraud and assessment of penalties by the board in civil proceedings.
6. That collection of the deficient taxes and penalties was not blocked by the statute of limitations, since fraud was involved. (Mitchell guilty tax board rules, 1934, p. 1).

Despite the damning evident against Charles Mitchell’s failure to pay taxes, Mitchell escaped unscathed and ultimately led to his acquittal of tax evasion.

On June 24, 1933, in an article titled, “Press Tax Inquiry for Evasion Data” (1933), it explained that Charles Mitchell of National City Bank was acquitted of tax

evasion, but the Senate Banking and Currency Subcommittee was determined to act on persistence on those who escaped charges of financial fraud:

Congress has not been relieved of any responsibility because Mr. Mitchell escaped jail. Unwholesome income tax practices are encountered during the further conduct of the investigation, they will be disclosed. If they have the color of fraud, I have no doubt they will be prosecuted. But in any event, neither the absence of prosecution, nor an astute criminal defense, will deter Congress from taking legislative action to make our income tax laws equally applicable to – and equally enforceable against – all our people without regard to their wealth or the source from which their income is derived. (Press tax inquiry for evasion data, 1933)

It was unbelievable that Mitchell was acquitted for his crimes, but the prosecutors remained optimistic, as they felt obligated to the public:

The authority given the committee by the Senate to examine income-tax returns has been of, great value to our investigators in checking the reliability of evidence obtained in other quarters. When unwholesome or unethical practices were discovered, we owed a public duty to expose them and to call them to the attention of Congress for such remedial action as might be deemed appropriate. (Press tax inquiry for evasion data, 1933)

In another scandal pertained to the National City Bank, former U.S. Attorney, Charles H.

Tuttle decided to press charges involving fraud and misallocation of bank's funds:

The officers and directors not only issued false and misleading financial statements to conceal their abuse of office, but employed funds of the bank to make loans to corporations of which they were directors. The officers and directors of the bank used the assets of the bank wrongfully for their own private profit. (Tuttle lays fraud to bank officials, 1934, p. 2).

The unearthing of financial fraud involving Charles Mitchell and The National City Bank proved to be complex as it contained multiple layers of fraud from tax evasions to the selling of fraudulent stocks to misallocation of bank's capital. Regardless of the prosecutions concrete investigation, the committee was in a desperate need of a lawyer

who not only possessed great knowledge, but also exuded great attributes of a stoic attitude, bravado, and gravitas against the bankers.

An article published by *The New York Times*, “The Man Who Will Question Morgan” (1933, p. 2) portrayed the New York prosecutor, Ferdinand Pecora as a maverick that possessed the might to resist the banking hegemony that corrupted the American financial system.

It will be the first time in twenty years that the affairs of J.P. Morgan & Co. have been the subject of public inquiry. Within a week, he subpoenaed Charles Mitchell, chairman of the board of the National City Bank, and later wrung him admission, which caused him to resign and to face trial on the charge of evading income tax payments amounting to \$858,000 in 1929 and 1930. He also probed into the Insull securities crash and questioned Richard Whitney, president of the New York Stock Exchange, at the length upon the practice of the Exchange. Mr. Pecora has been delving into the affairs of the Morgan Company and other among the sixteen important private banking firms whose seventy-one partners hold 996 directorships in the major part of the economic structure of the country. These firms he has defined as private bankers who make their own rules and are not subject to examination at the hand of any public authority. (The man who will question Morgan, 1933, p. 2)

Prior to the Great Depression, the banking hegemony in the United States grew so powerful that it was inconceivable for anyone to picture these men in front of a Senate Banking Committee publically confessing to financial crimes that destabilized the American economic system.

Even though the Pecora Commission demanded financial justice that captivated the public, other cases of banking frauds involving the stock market crash became prevalent after 1932. For instance, some of the headlines read: “Banking Fraud Charged” (1932, p. 2), “Detroit Banker Accused Of Fraud” (1933, p. 7), “Gets 4 To 8 Years in

Banking Fraud” (1933, p. 13), “Bernardino’s Guilty of Banking Fraud” (1934, p. 22), and “Ex-bankers Guilty in Detroit Fraud” (1935, p. 21).

The sheer number of criminal and civil violations during the Great Depression completely defrauded the national and local banking systems in the United States. Despite news reports on financial fraud on an annual basis, the Pecora Commission scrutinized the banking hegemony that led to the investigation of the financial manipulations that took place before and after the stock market crash of 1929. By making an example out of Charles Mitchell of National City Bank, the allegations of financial fraud enraged the public, which ultimately forced the U.S. Congress to draft and implement regulatory acts. For example, the Glass-Steagall banking legislation was drafted in an effort to separate commercial banking from investment banking. Within the Glass-Steagall Act, the Federal Deposit Insurance Corporation (FDIC) provided guaranteed safety of deposits in member banks. The criminal prosecutions created a ripple effect of regulatory agencies that provided financial stability. Unlike the Great Depression, the second half of this theme focuses on the contemporary crisis that failed to assemble a meaningful committee to investigate Wall Street’s role during the contemporary financial crisis. Similar to the early twentieth century, the banking hegemony deemed to be untouchable in the 2000s.

Criminality during the Contemporary Crisis (2007-2009)

The second part of this theme covers the contemporary crisis involving the discourse of criminality. Unlike the Great Depression, the prosecutors in the twenty-first century failed to criminally prosecute the top banking executives for their financial criminality. When the investment bank Lehman Brother filed for Chapter 11 bankruptcy on September 15, 2008, it sent a financial shockwave throughout the global economic system. Similar to the Great Depression, corporations, firms and individuals must be held accountable for the atrocities of criminal exploitation. Instead of holding these entities responsible for insurmountable losses, the discourse drastically shifted from crime to normal growth of “risk.” In an article written by Morse (2008), prior to its final demise in 2008, Lehman Brothers lost approximately \$350 million when employees of a large Japanese trading company allegedly exercised forged documents and an imposter to boost capital for business. The alleged fraud seems to be one of the substantial cases in Lehman’s history:

The New York based investment bank entered into with a medical consultancy owned by Tokyo-based pharmaceutical company LTT Bio-Pharma Co. last year. The alleged fraud is unusual for its size and because the victim is one of Wall Street’s most venerated institutions. The episode of alleged fraud appears to involve early investors making money as they were paid from funds provided by subsequent ones. As far back as three years ago, other investment banks had entered into smaller agreements with the LTT Bio-Pharma subsidiary, but received their principal and interest. (Morse, 2008, p. 1)

Shortly after the collapse of Lehman Brothers in 2008, *The New York Times* published an article expressing the prosecutions courage of “bumping elbows” at the grand level of the Justice Department:

In the investigation of the collapse of Lehman Brothers, United States attorney in three different jurisdictions – Manhattan, Brooklyn and New Jersey – have issued nearly two dozen subpoenas. Recipients include the chief executive, Richard S. Fuld Jr., and other top executives as well as Wall Street banks that provide research coverage on Lehman, like Merrill Lynch, and funds that invested in it. (Segal, 2009; Weiser & White, 2008)

The discourse of prosecuting financial criminals is assuring to the public, but when these New York prosecutors failed to send Rich Fuld Jr. (CEO of Lehman Brother) to prison for financial fraud, they essentially failed to bring economic justice. Perhaps this may indicate the lack of legal accountability:

The Department of Justice is missing important staff members. Former members of the Justice Department say that prosecutors and regulators are reluctant to act while the markets are in such disarray for fear of further unnerving investors and the public. (Segal, 2009)

This is just one example of a government agency that failed to sufficiently organize evidence in order to bring economic justice. The CEO of Lehman Brothers, Rich Fuld Jr., was able to escape without criminal charges despite losing billions of dollars in investors' money.

The New York Times featured a story on American International Group (AIG), one of the largest global financial institutions that inflicted self-harm based on failed derivatives, and poor financial risk-taking. An article written by Spitzer, Partnoy and Black (2009) posed simple, yet critical, investigative questions such as who knew what, and when? Who benefited, and by exactly how much? Would AIG's counterparties have failed without taxpayer support? The authors do not accurately have the answers to these questions; however, suggested where such answers could be found:

But we know where the answers are. They are in the trove of e-mail messages still backed up on AIG servers, as well as in the key internal accounting documents and financial models generated by AIG during the

past decade. Before releasing its regulatory clutches, the government should insist that the company immediately make these materials public. (Spitzer, Partnoy & Black, 2009)

By evading to releasing the e-mails, investigators are prohibited from inquiring about AIG's trade partners and counterparties from the large investment and commercial banks. In addition, the e-mails may explain how much information the board of directors knew prior to the economic doomsday:

Why haven't the Treasury and the Federal Reserve already made sure the public could see this information? Do they want to protect AIG, or do they worry about shining too much sunlight on their own performance leading up to and during the crisis? (Spitzer, Partnoy & Black, 2009)

Nonetheless, why would the chairman of the Fed play such large role in protecting AIG?

In a response to AIG and its troubles, Ben Bernanke stated, "AIG's 'irresponsible bets' had made him 'more angry' than anything else in regards to the financial crisis" (Nocera, 2009). AIG was represented as irresponsible risk-takers, rather than criminal fraudsters. The conflict of interest by Bernanke displays that the central bankers are willing to protect AIG at all costs, as Tim Geithner bailed out the insurance company at the staggering rate of \$150 to \$180 billion. The paradox in Bernanke's statement is quite evident in lacking real condemnation of individuals like Joe J. Cassano, former head of AIG's financial division who cashed out his money in retirement.

During the Great Depression, the United States Senate Banking and Currency Committee assembled an investigation team led by Ferdinand Pecora to investigate the origins of the Great Depression. In another article published by *The New York Times* titled, "Where is Our Ferdinand Pecora?" written by Chernow (2009, A25) advocated the

United States Congress to refer back to the Pecora Commission as an inspiration to compose a contemporary investigation for financial crimes.

The moment calls for nothing less than a sweeping inquest into the twin housing and stock market crash to create both the intellectual context and the political constituency for change. Our current stock market slump and housing bust can seem like natural calamities without identifiable culprits, creating free-floating anger in the land. The new Congress has a change to lead the nation, step by step, through all the machinations that led to the present debacle and to shape wise legislation to prevent a recurrence. (Chernow, 2009, p. A25)

The latest financial crisis has caused infuriating public sentiments as our policymakers are urgently seeking for answers, so it is logical for our financial and political leaders to assemble an investigative committee similar to the Great Depression. However, the current system is so out of control that it may dilute or bypass any criminal investigations. In an article published by *The Wall Street Journal* by Davis (2008), “The World Bank’s in-house watchdog said the bank’s effort to set-up anticorruption commission and ethics codes to combat graft in developing nations has been largely a flop.” In another article by the same publication written by Rappaport in 2009, took a survey of 500 certified examiners. The overwhelming majority witnessed a rise in internal financial fraud in the past year (Rappaport, 2009, p. 4-C):

The greatest increase comes from employees embezzling money from their firms, which includes all types of theft including pocketing money and altering inventory accounting. Fraud committed against companies by unrelated third parties or vendors also increased sharply, doctoring financial statement and corruption have increased more than 10% in the past year. (Rappaport, 2009, p. 4-C)

As the financial system gets destabilized, increase in fraud trickles down to the lowest ranks of society as people engage in pocketing money to falsifying inventory. As a result, the expansion of fraud increases revenue loses for organizations:

In a weak economy, the window for committing fraud opens up. U.S. organizations on average lost 7% of their annual revenue to fraud last year – or \$994 billion based on 2008 U.S. gross-domestic-product estimates – according to the association’s 2008 Report to the Nation on Occupational Fraud & Abuse. That is up from 5% in 2006, the last time the association published the report. Even as finagling goes up, most companies are cutting back costs and aren’t planning to add resources to prevent it. Most of the examiners responded that the companies they for also are cutting back staff, which often leads to a higher incidents of fraud. (Rappaport, 2009, p. 4-C)

For example, according to a report from *The Wall Street Journal* titled, “Mortgage Fraud Jumped 42% in Year” (2009, p. 6-D):

The most common mortgage-fraud cases include misrepresenting income, employment history, debt, and assets. Mortgage fraud has represented about \$1 billion in losses over the past decade as reported incidents comes as lenders raise credit standards to curb rising foreclosures. Many banks have been criticized for their offering up of mortgages without asking for thorough documentation. Critics charge the industry with being too lax in qualifying risky borrowers during the boom, which fueled an overheated housing market. (Mortgage Fraud Jumped 42% in Year” (Mortgage fraud jumped 42% in year, 2009, p. 6-D)

Despite a low wave of prosecutions, some of the published stories from the heralded *New York Times* and *Wall Street Journal* provided articles on the federal government cracking down on financial crimes that positioned the United States economy under heavy turmoil.

Here are few examples:

Federal prosecutors in Manhattan have charged four New Yorkers with conspiring to obtain more than \$10 million in fraudulent home mortgage loans in a plan that relied on former prisoners living in a halfway house to pose as home buyers. Most of the mortgages, which were subprime loans provided to borrowers considered high credit risks, are now in default or in foreclosure. (Weiser, 2009)

It is encouraging to see criminals sentenced to prison for financial fraud, but targeting the “smaller” guys won’t affect the financial industry as long as the banking titans are protected from serious prosecutions. Although in a report by McKinnon (2009, 1-C)

stated a group of U.S. Senators issued a court order from large banks such as Goldman Sachs and Deutsche Bank:

A Senate panel has subpoenaed financial institutions, including Goldman Sachs Group Inc. and Deutsche Bank AG, seeking evidence of fraud in last year's mortgage-market meltdown, according to people familiar with the situation. The congressional investigation appears to focus on whether international communication, such as email, show bankers had private doubts about whether mortgage-related securities there were putting together were financially sound as their public pronouncement suggested. Collapsing values for many of those securities played a big role in precipitating last year's financial crisis. (McKinnon, 2009, 1-C)

The Senate deserves a credit for taking action, however, if Charles Mitchell of National City Bank avoided charges of tax evasion back in the 1930s, these large bank officials are well capable of escaping from legal charges as well. At worst, these mega banks pay their way out of trouble.

Even the FBI decided to investigate and hunt down individuals and organizations that diabolically utilized financial instruments to gain record profits:

The Federal Bureau of Investigation has opened criminal inquiries into 14 companies as part of an investigation of the subprime-mortgage crisis. The probe is focusing on accounting fraud, securitization of loans and insider trading, among other areas. The FBI wouldn't identify the companies under investigation but said it is looking into allegations of fraud in various stages of the mortgage process, from companies that bundled the loan into securities to the banks that ended up holding them. FBI officials say the bureau is working with the SEC, which has opened more than three dozen investigations in the subprime-mortgage business of companies involved in the underwriting and securitization of loans. The probes are complicated because of the sophisticated financial vehicles used to propel the mortgage-business boom in recent years. (Perez & Scannell, 2008, p. 3-A)

However, the FBI is confronted with serious problem of experiencing a shortage of detectives, particularly in the department of white-collar crimes:

The number of mortgage fraud cases has grown so fast that government agencies that investigate and prosecute them cannot keep up, lenders and law enforcement officials have said. Reports of suspected mortgage fraud have doubled since 2005 and increased eightfold since 2002. Banks filed 47, 717 reports this year, up from 21,994 two years ago. In 2002, banks filed 5,623 reports. Law enforcements agencies say they are overwhelmed, especially because investigating and prosecuting fraud can be complex and time consuming. (Leland, 2007)

The excerpts above mostly involve mid-level individuals that committed financial fraud. During the Great Depression, the U.S. Senate assembled a commission led by Ferdinand Pecora in an attempt to criminally prosecute the well-known bankers such as Charles Mitchell of National City for financial fraud, which paved a path toward regulatory acts. In contrast to the current crisis, U.S. Senate Banking Committee and the prosecutors essentially failed to set a precedent on criminally charging the big banking executives for their role in the mortgage crisis. Although we are seeing some legal measures by the prosecutors and the FBI, impediments ranging from legal barriers to a lack of sufficient resources equates to a lack of prosecution. The next theme will discuss the regulatory policy responses during the Great Depression in contrast to the contemporary economic downturn.

Theme Three: Policy Responses during the Great Depression and the Great Recession

This final section compares policy responses during the Great Depression, which implemented regulatory acts in response to the catastrophic bank failures and financial corruption. On the contrary, the current economic crisis led to monetary policies like Troubled Asset Relief Program (TARP) that bailed out the large financial institutions,

such as banking and insurance for their malinvestments using taxpayers' money. The former Chairman of the Fed, Paul Volcker, introduced a new regulatory act that bans proprietary trading, which prohibits financial firms such as banks from trading bonds, commodities, currencies, derivatives and stocks with the company's own capital to generate large sums of profit. Proprietary trading may lead to gambling on property, complex derivatives, or any trade assets (Stewart, 2010). Despite an attempt to limit the financial hazards of risk taking, the lobbyists diminished the integrity of the proposed Volcker Rule by watering down its regulatory structures.

Policy Response during the Great Depression

At the height of the Great Depression in 1932, the implementation of financial regulations brought stability to the American economic system. According to "The Political Economy of Regulation" (2002) by MIT, regulations in its broadest sense is a government intervention in market outcomes conducted through regulatory agencies with legislative mandates to oversee specific industries. Senators Carter Glass and Henry Steagall drafted the momentous Banking Act of 1933 that barred commercial banking from underwriting securities (Crawford, 2011). This financial legislation forced the banks to pick between investment banking that conducted securities transactions or commercial banking that holds deposits and loans (Crawford, 2011).

Dr. Edward S. Mead from the Wharton School provided his own analysis of the Glass-Steagall Act in an article titled, "Expert Analyzes Bill" (1932, p. 2):

The Glass-Steagall bill serves to free an amount of gold equal to the government securities held by the Federal Reserve Bank, which gold can be used as a basis for new notes. The method is as follows: A group of member banks, joining together for this purpose, may apply to the Federal

Reserve Bank of their district for loans from the Federal Reserve Bank, secured by municipal bonds, railroad bonds, real estate mortgages or any other collateral, which may be approved by five members of the Federal Reserve Board, and Secured also by the joint liability of the members of the group. After these loans are made, the borrowing banks have a credit with the Federal Reserve Bank for the amount of the loan. They can now turn this credit into Federal Reserve notes to be used to strengthen their cash position to re-establish confidence among their depositors by promptly meeting all demands. Next, the Federal Reserve Bank to obtain from the Federal Reserve agent the amount of notes which it is called upon to furnish to these member bank borrowers. (Expert analyzes bill, 1932, p. 2)

Even Wall Street became intrigued and optimistic on the regulatory act. According to Lockey (1932), the Glass-Steagall Act stirred hope in Wall Street as they appeared:

To be pleased by the fact that the sacrosanct character of the Federal Reserve Act does not prevent its alternation to meet a national emergency. Speedy passage of the Glass-Steagall bill by both the House and Senate was, from Wall Street point of view, the overshadowing event of last week. The central banking system will do more to hasten the economic recovery than anything else that has been attempted. (Lockey, 1932, p. 9-N9)

Prior to Glass-Steagall, the Fed acquired these notes in one of three methods: commercial paper, gold, or fifteen-day notes of the member banks secured by government bonds (Expert analyzes bill, 1932, p. 2). Under the Glass-Steagall Act, the Fed is able to obtain reserve notes with securities along with United States Treasury notes. A year later, the U.S. Congress proposed the second wave of the Glass-Steagall Act that largely dealt with the American banking system.

Initially, the Banking Act faced adversities as members of Congress failed to reach a deal. On May 14, 1933, *The New York Times* published an article titled, “*Glass Bank Bill Ready For Senate*” (1933, p. 6) provided information on the banking legislation put forth by Senator Carter Glass and Representative Henry Steagall:

The House Banking Committee read primary portions of the Steagall and Glass bills today, but reached no decision on any controversial feature. The Glass and Steagall bills differ materially on one point, the proposal of Representative Steagall to allow State banks not members of the Federal Reserve wide opportunity to obtain benefits of the Deposit Insurance Corporation. Mr. Glass wishes to have the State non-member banks ask for membership in the Reserve to qualify for the insurance. (Glass bank bill ready for senate, 1933, p. 6)

To satisfy the controversial demands, Senators Glass and Steagall were forced to make the necessary adjustments to pass the legislation. In an article titled, “Banking Reform Drafted” (1933, p. 1), introduced a compromising bill that satisfied the requirements for the Republicans and the Democrats:

The administration’s banking reform bill, including a bank depositors’ insurance fund corporation. Senator Glass and Representative Steagall, chairman of the House Banking and Currency Committee are jointly sponsoring the bill. The new bill represents a compromise between the views of Senator Glass, a conservative who opposes lessening the restrictions of the Federal Reserve System, and Representative Steagall, an out-and-out advocate of government initiation of guarantees for bank deposits. (Banking reform drafted, 1933, p. 1)

Senator Glass’s banking reform provisions entailed different components:

- a) Divorce of security affiliates within two years.
- b) Prevention of interlocking directorates between investment banking houses and industrial enterprises.
- c) Stopping payment of interest on checking accounts in Federal Reserve member and national banks.
- d) A possible prohibition upon banks lending money to their own officers.
- e) Authorization for State-wide branch banking where State laws permit
- f) Increase of minimum capital for national banks from \$25,000 to \$50,000.
- g) The President favors the plan in principle, leaving the details to be worked out by the two congressional banking experts. The President was represented as gratified by the apparent fact that Mr. Glass and Mr. Steagall have compromised their hitherto divergent views.

(Banking reform drafted, 1933, p. 1)

Glass understood systemic risks that positioned the United States financial system into an extraordinary economic depression, so he had to propose radical solutions by placing restrictions and assembling new financial regulatory agencies in order to revamp the unregulated banking sector. Despite not agreeing to all accounts, Senators Glass and Steagall were determined to pass the regulatory act.

As the banking regulation took its shape, *The New York Times* published an article titled, “Roosevelt Favors Pushing Bank Bill,” (1933, p. 19) stated, President Roosevelt demanded a radical banking transformation that separated the commercial banks from investment banking activities:

More rigid supervision of national banks: discouraging the use of bank deposits for speculation; separation of investment and commercial banking and barring the use of Federal Reserve funds for speculative purposes. Investment banking is a legitimate business. Commercial banking is another wholly separate and distinct business. Their consolidation and mingling is contrary to public policy. I propose their separation. (Roosevelt favors pushing bank bill, 1933, p. 19)

In response to the regulatory demands, *The New York Times* reported the approval of the Glass-Steagall Banking Act. The standing vote in the House overwhelmingly passed 161 to 6 and in the Senate as well (Bank reform bill swiftly approved, 1933, p. 1). The article praised Glass and Steagall for their historic achievement in the approval of the regulatory act.

Senator Glass and Representative Steagall were warmly praised in their respective houses. Senator Walcott declared it was ‘one of the rare privileges’ of his life to have been associated with Senator Glass in the three-year fight for the legislation, while Representative Goldborough asserted that the name of Mr. Steagall should be ‘inscribed’ in an outstanding place. (Bank reform bill swiftly approved, 1933, p. 1)

However, not everyone was on board with Glass and Steagall. The approval of the banking regulation caused a tremendous backlash against the banking hegemony. Initially, the first Glass-Steagall Act was passed in 1932 during the final year of the Hoover Administration. In an article published by *The New York Times* titled, “*Bankers Denounce Glass Bill’s Terms*” (1932, p. 1), individuals who were well entrenched in the financial sector did not hesitate to denigrate the new regulatory law:

Henry J. Haas, president of the American Bankers’ Association, and Allan M. Pope, president of the Investment Banker’s association, emphatically told the Senate Banking and Currency Committee that the Glass banking reform bill is deflationary in character and that it would be a mistake to enact it at this time. Without exception, each of several hundred of our association members with whom I talked opposed the bill at the present time on the ground that we are engaged in attempting to stem the tide of deflation, and have enacted emergency legislation for the purpose. The result of this bill would be diametrically opposed to such movements because of its extremely deflationary provisions. We are of the opinion that it would be a serious mistake to pass a bill at this time having so many provisions of a deflationary and regulatory nature, which would, in our opinion, cause withdrawal of a considerable number of members of the Federal Reserve System. We believe that its effect would be injurious not only to member banks but to the business interest of the country. (Bankers denounce glass bill’s terms, 1932, p. 1)

The approval of Glass-Steagall sparked an outrage, especially from the bankers whose reactions were mainly negative. In an article titled, “*Glass Bill Called Bar to Recovery*” (1932, p. 31), the vice president of the Cleveland Trust Company, Leon P. Ayres testified in court before the Senate Banking and Currency Committee stating his concerns toward the financial legislation.

American banks will suffer severely if the Glass bill is enacted into law. It is not wise to choose the worst period of the worst depression that we have ever experienced as the time to disrupt those parts of our banking machinery on which we most directly rely for the financing of reconstruction. (Glass bill called bar to recovery, 1932, p. 31)

However, Senator Glass countered the criticisms by stating, the purpose of the bill is to prevent a repeat of 1929. Under this bill, a national bank may gamble its head off with its own money, but it cannot recoup at the Federal Reserve Bank (Bankers denounce glass bill's terms, 1932, p. 1).

The conventional criticisms from the bankers condemning the legislation attempted to salvage the old practices that contributed to the financial corruption prior to the Great Depression. Looking back, the 1930s era of regulations provided radical revisions to the American banking system. During the 1930s, Wall Street bankers and politicians sharply disapproved financial regulations (Fosner, 1933). Despite the overall negative sentiment surrounding the act, it did not discourage Senators Glass and Steagall from drafting the bill as Steagall stated:

The bill was not written to please the banker. The bill was written to correct a state of chaos and disorganization in our banking structure which had its inception in the century-old conflict between the States and the national government with forty-nine legislative bodies regulating and granting special privileges to their respective banks." The Result has been a competitive liberalization of bank laws which permitted unsound banks and unsound banking accompanied by losses and tragedies. (Fosner, 1933, p. 3-XX3)

To address the vital principles of this legislation, the author of the article highlighted the central functions proposed by Senator Carter Glass, as he wanted to fortify the Federal Reserve System by circumventing the utilization of Federal Reserve credit for stock-market speculations. The prevention for changes in laws pertained to banking, affiliation, and bank reserves. The other half of the bill drafted by House of Representatives Henry Steagall persistently advocated for a deposit guarantee, a proposal for insurance bank deposits (Fosner 1933). This created an uproar that it became the most debated clause in

the legislation. In a heated battle between the supporters and detractors, “The bankers and other conservatives protested vigorously. The American Bankers Association fought to the bitter end, even urging a Presidential veto to kill the provision in Congress, but it failed” (Fosner, 1933). In a brief explanation in relation to the Federal Reserve Bank and the Glass-Steagall Act:

Bring many non-member banks into the Federal Reserve System. Temporary participation in the deposit insurance pool is permitted to any solvent bank until July 1, 1936, but after that time only member banks of the Federal Reserve System or those banks which have applied for membership may have the insurance benefits. The number of banks outside the Federal Reserve System, which cannot be regulated or aided by the Reserve authorities, has been a significant factor in the number of failures in the crisis of 1920 and 1929. (Fosner, 1933, p. 3-XX3)

On the contrary, some valued the Banking Act in a positive manner praising Glass and Steagall. Prior to the passage of the regulation in 1933, the United States banking system was on the verge of complete collapse. The U.S. government suspended banking activities in majority of the states, barring citizens from banking transactions (Foner, 2008). *The New York Times* published an article titled, “Controller Sees One Bank System” (1933, p. 33), citing financial expert, J. F. T. O’Conner for praising Glass and Steagall at the annual Minnesota Bankers Association.

It was drafted by two of the ablest financial minds in America if not in the world. It will eliminate the disadvantages and expense of having two banking system serving the public. The duplication of bank examination is one item that shows how cumbersome our present system is. With both national and State governments chartering banks, there were certain to be too many banks in the country, and that was one great cause of our banking troubles of the past decade. (Controller sees one bank system, 1933, p. 33)

Within the same article, Minnesota’s banks started to experience its own recovery:

“Twenty-eight of thirty-five banks which were not at first licensed have been reopened.”

To continue, he reminded the readers about the dark days when President Roosevelt declared bank holidays that barred banking activities: “Uncertainty, doubt, bewilderment was written in every face, but confidence and courage came to the rescue” (Controller see one bank system, 1933).

Although the Glass-Steagall Act promoted public interest that aimed to renovate the banking system in response to a near collapse of the American banking industry, the detractors remained persistently critical. Francis Sisson, the president of the American Bankers Association condemned the Banking Act of 1933 by advocating against the act stating he would, “ultimately force its own repeal in amendment” (Banking act condemned, 1933; p. 38).

The one forcing commercial banks to give up investment activities, through bond departments or investment affiliations is a mistaken theories of the originators of the bill. Commercial and investment banking operations under the same organization are incompatible and that the over expansion of investment credit, which was a factor in the ‘new era’ boom preceding the 1929 reaction was mainly blamable upon the investment activities of commercial banks. The most questionable feature of the act is the guaranty or insurance of the deposits. Guaranteeing of deposits, he added, had failed wherever tried in many previous tests, invariably causing weaker instead of stronger banking. The present banking law repeats the old mistakes on a bigger scale. (Banking act condemned, 1933, p. 38)

Due to constant complaints against the Glass-Steagall Act, revisions were inevitable.

Brought forth by one of the Federal Reserve Board member, Marriner S. Eccles, he proposed another Banking Act that was approved and signed by President Roosevelt in 1935. The act changed the structures of the Federal Reserve System to centralize the control of money supply for the entire nation (Banking bill wins favor as revised, 1935). This legislation incorporated changes in the Federal law. First, it created open-market committee devised of seven board members from the Federal Reserve Board and five

representatives of Federal Reserve Banks, warranted to regulate credit fluctuations through the purchase and sales of government securities in the open market by the Reserve banks. Another provision empowers the president to disperse the Federal Reserve Board and reconstitute the board as the “Board of Governors of the Federal Reserve System” (Roosevelt signs new banking law, 1935).

It was officially signed and approved in 1935, but the revision of the Glass-Steagall Act was proposed in 1933 in an article published by *The New York Times* titled, “Saving Banks and The Banking Act” (1933, p. 18):

“The Glass-Steagall Banking Act of June needs ‘thorough overhauling.’ This remark had reference particularly to the deposit-guarantee clauses, which indeed, have already turned out to hasty and imperfect piece of legislation.” (Saving banks and the banking Act, 1933, p. 18)

After the approval of the revisions, the president of the American Bankers Association, Rudolf S. Hecht called the legislation, “sound” as it was published in an article titled, “Roosevelt Signs New Banking Law” (1935, p. 19):

Legislation of this kind is invariably the result of compromises and adjustments. However, the act as finally passed is basically sound and merits the confidence of bankers. We believe the new bill constitutes a forward step in constructive banking legislation and is a decided improvement upon the present system” Marriner Eccles who sponsored the revision praised the act, “In my judgment the Banking Bill now signed by the President marks an important advance in the development of the country’s banking system and the adaptation of monetary administration to present-day conditions and national needs. (Roosevelt signs new banking law, 1935, p. 19)

The advocacy efforts on behalf of the financial sector by the American Bankers Association heavily influenced Glass-Steagall’s revisions as they endorsed the Banking Act of 1935:

Declaring that it is basically sound and merits confidence on the part of banks. The association's approval of the measure was expressed in a statement sent out by its special committee on the act to all banks in the United States. Although many extreme measures pertaining to banking were introduced this session, none of those which threatened serious danger to sound banking prevailed. We believed that, on the whole, the Banking Act of 1935 is an acceptable piece of legislation. (Roosevelt signs new banking law, 1935, p. 19)

Despite the heavy criticisms from the financial sector, the Glass-Steagall Act (1933) downsized the banking sector through the separation of commercial and investment banks that brought stability toward the American financial system. However, at the conclusion of the twentieth century, the legislative branch in 1999 thought they could outwit the congressional members from the 1930s by deregulating the financial sector. This was not only a new era of deregulation, but it set the stage for the contemporary financial crisis. Once the crisis struck on September 15, 2008, instead of looking back in history by reinstalling robust regulations similar to the 1930s, the United States government responded by bailing out the financial institutions by using taxpayers money.

Policy Responses during the Contemporary Era

The second half of this section will primarily deal with the policy responses regarding the contemporary financial crisis. In contrast to the policymakers in the 1930s, the current group of legislators drafted and approved a massive bailout plan for the troubled financial institutions that faced imminent collapse. In other words, congress during the 1930s implemented regulations, while congress today paved over the crisis by bailing out the financial sector. Instead of downsizing the banks, the bailouts allowed large investment banks such as JPMorgan, Bank of American and Wells Fargo to consolidate with weaker banks, thus prolonging the infamous slogan, “too big to fail.” This section will discuss the mergers and bailouts of financial institutions involving the large banks, AIG, Freddie and Fannie along with the creation of the regulatory act call the Volcker Rule.

Prior to the economic doomsday on September 15, 2008, one of the largest investment banks in the United States, Bear Stearns found themselves in deep financial hole that required an intervention from the Fed and JPMorgan Chase (Norris, 2008, p. 1):

Bear Stearns, which boasts that it has never had a losing year in its 85 years, was plagued by rumors that it owned securities it could not sell and that it might be unable to borrow enough money to hold on to the securities. Overnight, the Federal Reserve and JP Morgan Chase arranged to provide the cash Bear Stearns needed. Bear could not borrow directly from the Fed because it is not a commercial bank. The Fed had seen such problems coming, and had announced plans this week to lend money to major dealers in Treasury securities – like Bear – by taking in as collateral mortgage securities that are now hard to sell. The rescue of Bear is not permanent – the loans are for only a month – and there is an expectation that authorities will seek to arrange for Bear to be acquired, perhaps at a low price, or that it will be broken up and sold to more than one buyer. Bear stock fell 47% on Friday; all of the decline came after the rescue was announced. (Norris, 2008, p. 1)

The “robust” bank no longer possessed the financial flexibility to support itself, due to malinvestment of mortgages that severely paralyzed their abilities to perform any type of financial transactions. With Bear Stearns going up in flames, JPMorgan Chase aimed to pillage what was left of the rotting corpse that was Bear Stearns, thus initiating a period of massive banking mergers and financial bailouts. An article written by Eavis and Reilly (2008, p. C.1) titled, “Bear’s Fall Spark Soul Searching; At a Certain Point; Wall Street Firms Are Buys,” broke the news of the acquisition:

The fire sale of Bears Stearns over the weekend highlighted the inherent risks in the business and how quickly a firm can come undone. Bear last reported it had network of about \$11.7 billion and executives on Friday said that figure wasn’t likely to change much when the firm reported first-quarter results. On Sunday, it was sold to J.P. Morgan Chase for \$236 million. (Eavis & Reilly, 2008, p. C.1)

Prior to the JPMorgan Chase-Bear Stearns acquisition, *The New York Times* examined, why go through the trouble of bailing out Bear Stearns? (Morgenson, 2008, p. 1):

But why save bear Stearns? As one of the biggest players in the mortgage securities business on Wall Street, Bear provided munificent lines of credit to public-spirited subprime lenders like New Century (now bankrupt), It is also the owner of EMC Mortgage Servicing, one of the most aggressive subprime mortgage services out there. Let’s not forget that Bear Stearns lost billions for its clients last summer, when two hedge funds investing heavily in mortgage securities collapsed. And the firm tried to dump toxic mortgage securities it held in its own vaults onto the public last summer. Recall, too, that back in 1998, when the Long Term Capital management hedge fund required a Fed-arranged bailout, Bear Stearns refused to join the rescue effort. Jimmy Cayne, then chief executive at the firm, told the Fed to take a hike. (Morgenson, 2008, p. 1)

Poor financial history of toxic mortgage securities and playing financial hardball with hedge fund managers raised legitimate questions to why pump large quantities of capital

into a firm that is on a verge of extinction. In a statement by Bill Fleckenstein of Fleckenstein Capital advocated for the policymakers to let the investment bank perish:

Why not set an example out of Bear Stearns, the guys who have this record of dog-eat-dog, we're brass knuckles, we're tough? This is the perfect timing to set an example, but they are not interested in setting an example. We are Bailout Nation. (Morgenson, 2008, p. 1)

Instead of making a prime example out of Bear Stearns, the Fed opted to aid JPMorgan Chase in the acquisition of the failing investment bank, thus completing the merger in March 2008. Fast forward to September 15, 2008, the fourth largest investment bank, Lehman Brothers officially filed for chapter 11 bankruptcy, thereby triggering a widespread of bank acquisitions and mergers across the board. In an article published by *The Wall Street Journal* titled, "Bank of America to Buy Merrill" (Karnitschnig, Mollenkamp & Fitzpatrick, 2008, p. A.1) detailed Bank of America's merger with Merrill Lynch, despite the dangers of inheriting huge risks:

Merrill Lynch & Co. agreed late Sunday to sell itself to Bank of America Corp. for \$50 billion. The deal, worked out in 48 hours of frenetic negotiating, could instantly reshape the U.S. banking landscape, making the nation's prime behemoth even bigger. In adding Merrill Lynch, it would control the nation's largest force of stockbrokers as well as a well-regarded investment bank. The combination would create a bank of vast reach, involved in nearly every nook and cranny of the financial system, from credit cards and auto loans to bond and stock underwriting, merger advice and wealth management. (Karnitschnig, Mollenkamp & Fitzpatrick, 2008, p. A.1)

Bank of America made a risky purchase by consolidating with Merrill Lynch. Encumbered with more debt by the acquisition, Bank of America eventually begged for more capital from the U.S. government (Bank of America to Receive \$20 Billion More, 2009, p. B1):

Kenneth D. Lewis gambled on bold acquisition to build Bank of America into the nation's largest bank. Two weeks after closing its purchase of Merrill Lynch at the urging of federal regulators, the government cemented a deal at midnight Thursday to supply Bank of America with a fresh \$20 billion capital injection and absorb as much as \$98.2 billion in losses on toxic assets. The Bank had been pressing the government for help after it was surprised to learn that Merrill would be taking a fourth-quarter write-down of \$15 billion to \$20 billion, in addition to Bank of America's rising consumer loan losses. With losses mounting in the financial industry, other banks may eventually feel compelled to turn to the government for assistance, and the program could be used for other big banks. Taxpayers could end up guaranteeing hundreds of billions of dollars of banks' toxic assets. (Bank of America to receive \$20 billion more, 2009, p. B1)

By inheriting substantial quantities of toxic assets, Bank of America had no other options, but to seek for federally funded bailout money from the government, which was mainly derived from the taxpayers. Bank of America and JPMorgan Chase were not alone in acquiring banks as Wells Fargo entered the competition of bank consolidations.

Wachovia, fourth-largest bank holding company in the U.S. was another bank that came under heavy fire during the post-Lehman collapse. *The New York Times* published an article titled, "Wachovia, Looking for Help, Turns to Citigroup" stated (White & Dash, 2008, p. C1):

More banks might run into trouble even with a \$700 billion rescue for the financial system, Wachovia, one of those hardest hit by the housing crisis, became the latest to reach for a lifeline. Weighed down by a huge portfolio of troubled mortgage loans, the nation's fourth-largest bank by assets entered into preliminary deal talks with Citigroup, and extended feelers to Wells Fargo and Banco Santander of Spain. (White & Dash, 2008, p. C1)

Once Wachovia disclosed their books on troubled mortgage loans, it suddenly became a feeding frenzy between Wells Fargo and Citigroup. In an article, "Regulators Push for Sale of Wachovia" (Dash & Ross-Sorkin, 2008, A. 15) discussed the auction between the two banking firms:

A sale of either Wells Fargo or Citigroup would further concentrate Americans' bank deposits in the hands of just three banks: Bank of America, JPMorgan Chase and whichever bank acquired Wachovia would control more than 30 percent of the industry's deposits. Together, those three would be so large that they would dominate the industry, with unrivaled to set prices for their loans and services. Given their size and reach, the institutions would probably come under greater scrutiny from federal regulators. (Dash & Ross-Sorkin, 2008, A. 15)

Dash and Ross-Sorkin (2008) correctly forecasted the mergers that inevitably led to bank consolidations that grew even larger during the financial crisis. Instead of downsizing the banking industry, the opposite effect of banking cannibalism occurred under a lack of regulatory supervision.

Less than a month after the Lehman collapse, *The New York Times* published an article titled, "Wells Fargo Wins the War for Wachovia" (de la Merced, 2008, p. 1) highlighting the winner of the Wachovia sweepstakes:

One of the biggest showdowns on Wall Street ended with a whimper Thursday when Citigroup walked away from efforts to block a deal between Wachovia and Wells Fargo, paving the way for a merger that would concentrate power within the American banking industry to a few firms. Citigroup, which mounted a whirlwind legal battle after Wachovia spurned its \$2.2 billion government-brokered deal last week for a surprise, superior offer by Well Fargo, said it would continue to seek \$60 billion in legal damages. Together, Wells Fargo and Wachovia will have \$1.42 trillion in assets, 48 million customers, and 280,000 employees. The combined bank will be present on both coasts in the fastest-growing markets, playing on the same field as JPMorgan Chase and Bank of America, two of the nation's largest banks. (de la Merced, 2008, p. 1)

The Wall Street Journal broke the same news regarding the banking merger between Wells Fargo and Wachovia reported by Fitzpatrick and Enrich (2008, p. C.1):

Wells Fargo & Co. won the battle for Wachovia Corp. as rival suitor Citigroup Inc. walked away from compromise negotiations because of worries about the quality of some of Wachovia's assets. Unlike Citigroup's original agreement, the Wells Fargo takeover doesn't involve

government financial assistance. A person close to Wachovia said Citigroup officials didn't express serious concerns about the bank's books until talks reached an impasse. (Fitzpatrick & Enrich, 2008, p. C.1).

As mergers became rampant during the financial crisis, the regulators neglected to investigate the acquisitions as they abandoned their duties of overseeing the economic landscape in order to assist for the large banks (LaBaton, 2008, p. C10):

Regulators at four agencies that oversee the nation's banks and saving association on Monday and Tuesday proposed significant changes in accounting rules to bolster banks and encourage widespread industry consolidation by making them more attractive to prospective purchasers. The regulators and Bush Administration have decided to resort to further loosening of the accounting rules to try to get the industry through problems that some experts have attributed in large part to years of deregulation. The Federal Reserve announced that it had eased restrictions that had prevented regulated companies from transferring money to less regulated companies and more risky affiliates. That action would, for instance, enable one arm of a giant financial company, like the commercial banks of Bank of America or Citigroup, to move money to another arm, like their investment units. (LaBaton, 2008, p. C10)

According to an interview on Moyers (2010) MIT economist, Simon Johnson weighed in on his thoughts regarding the outcome of the crisis:

The big banks became stronger as a result of the bailout. That may seem extraordinary, but it's really true. They're turning that increased economic clout into more political power. And they're using that political power to go out and take the same sort of risks that got us into disaster in September 2008. (Moyers, 2010)

Instead of downsizing the biggest investment banks in response to the financial crisis, the opposite effect of bank consolidations occurred involving the largest investment banks.

On the contrary, the banks during the Great Depression were forced to downsize, as they appeared to be "too risky." Instead of reinstating Glass-Steagall or a drafting a similar act that downsized the banking industry, these "too big to fail" banks became more

systemically risky. However, the banking sector was not the only industry susceptible to financial meltdowns as the housing institutions spiraled out of control involving AIG, Freddie Mac, and Fannie Mae.

The American International Group (AIG) is a U.S. based financial services company that was bailed out during the 2008 financial crisis, due to liquidity crisis when their credit rating was slashed from AAA to AA by Standards and Poor's and Moody's. These two credit rating agencies were concerned over the ongoing losses on mortgage-backed securities. In total, it took the U.S. Treasury and the Federal Reserve approximately \$180 billion to bailout AIG's liquidity crisis.

At the end of the 2007, *The Wall Street Journal* published an article titled, "Paulson Urges Congress to Act on Woes" (2007, p. A2), which encouraged the United States Congress to aid the troubled housing market due to subprime loans:

After months of criticism that he hasn't responded aggressively enough, Mr. Paulson implied that the administration was already doing all it could to stem the nation's mortgage woes, which have rolled markets, threatened many homeowners and raised the risk of recession. The administration has repeatedly failed to use the tools at its disposal to protect home buyers from abusive lending, " said Chris Dodd, who himself has been criticized for failing to act on a House-passed bill to expand eligibility for Federal Housing Administration mortgage insurance. Treasury officials are urging the mortgage industry including lenders, loan-servicing companies, and investors who own mortgage-backed securities to finalize a sweeping plan to freeze subprime interest rates. Interest rates on as much as \$362 billion in subprime home mortgage are expected to rise in the coming year, according to Bank of American Securities. Fannie and Freddie said they need to charge extra to reflect higher default risks, caused partly by falling home prices. (Paulson urges congress to act on woes, 2007, p. A2)

According to the reports, Hank Paulson was well aware of the destabilization of the U.S. housing market as he urged the U.S. Congress to immediately respond to the potential crisis.

When Lehman Brother collapsed in 2008, it sent a global shockwave that originated in the United States. In response, the Bush Administration decided to propose an unprecedented \$700 billion bailout package. *The New York Times* published an in-depth article titled, “Administration is Seeking \$700 Billion for Wall St.; Bailout Could Set Record” (Backer, 2008, p. 1), discussed how Ben Bernanke and Hank Paulson assembled the largest financial bailout in the history of the United States:

The plan to buy \$700 billion in troubled assets with taxpayer money was shaped by two men who did not know each other until two years ago and did not travel in the same circles, but now find themselves brought together by history. Mr. Bernanke told Mr. Paulson that it was time to adopt a comprehensive strategy that Congress would have to approve. The former Ivy League Professor, and Mr. Paulson, the hard-charging former Wall Street deal maker, launched what would be the government’s largest economic rescue operation in modern crisis, one that rivals Iraq war cost and at the time many redefined Washington’s role in the marketplace for years. The troubles were only deepening. Lehman Brothers had declared bankruptcy, Merrill Lynch had agreed to be bought by Bank of America and A.I.G. was on the verge of collapse. Mr. Bernanke and Paulson put together an \$85 billion bailout of A.I.G. and presented it to Mr. Bush. (Backer, 2008, p. 1)

Instead of promoting stringent regulations, the policymakers’ response to the financial implosion was to bailout the institutions that were on a verge of complete collapse.

According to Paletta et al. (2008, p. A1), shares of AIG, tumbled more than 30%. The rating agency, Standard & Poor’s threatened to downgrade its credit ratings on AIG due to plummeting share prices and the increasing yield on its debt instruments (Paletta et al., 2008, p. A1).

Roughly, two days after Lehman Brothers filed for Chapter 11 bankruptcy, the U.S. government decided to initiate the first round of bailouts for AIG. An article written

by Karnitschnig et al., (2008, p. A1) titled, “U.S. To Take Over AIG in \$85 Billion Bailout,” explained some of the details behind AIG’s bailout:

This time, the government decided AIG truly was too big to fail. The U.S. government seized control of American International Group Inc. – one of the world’s biggest insurers – in an \$85 billion deal that signaled the intensity of its concerns about the danger a collapse could pose to the financial system. The Fed will lend up to \$85 billion to AIG, and the U.S. government will effectively get a 79.9% equity stake in the insurer in the form of warrants called equity participation notes. Two-year loan will carry an interest rate of Libor plus 8.5 percentage points. The federal government concluded it would be catastrophic to allow the insurer to fail. Banks and mutual funds are major holders of AIGs debt and could take a hit if the insurer were to default. AIG was a major seller of “credit-default swaps,” essentially insurance against default on assets tied to corporate debt and mortgage securities. As the housing market crumbled, the value of those contracts has dropped sharply, driving \$18 billion in losses over the past three quarters and forcing AIG to put up billions of dollars in collateral. (Karnitschnig et al., 2008, p. A1)

The sheer monstrosity of capital that took to bailout AIG using taxpayers’ money exposed the deep-rooted malinvestments and false promises AIG freely loaned out during the economic “boom” prior to the crisis.

With a controversial plan of bailing out these financial institutions like AIG, the opinions across the board were mixed. In an article by *The Wall Street Journal* written by Ng and Plevin (2008, p, c.1) titled, “New AIG Rescue is Bank Blessing,” provided details on the bailout of AIG internationally and domestically:

Banks in the U.S. and abroad are among the biggest winners in the federal government’s revamped \$150 billion bailout of American International Group Inc. Many banks that previously bought protection from the insurer on securities backed by now-troubled mortgage assets stand to recoup the bulk of their investments under a plan by AIG and the Federal Reserve Bank of New York to buy around \$70 billion of those securities via a new company. These securities are collateralized debt obligations backed by subprime-mortgage bonds, commercial-mortgage loans and other assets. Banks in the U.S., Europe, and Canada bought credit-default swaps on these securities from AIG, which in turn promised to compensate them if

the securities defaulted. That enabled the banks to pry roughly \$35 billion in collateral from AIG as a result of those declines and downgrades in AIG's own credit ratings. The banks that have sought and received collateral from AIG include Goldman Sachs, Group Inc., Merrill Lynch & Co., UBS AG, Deutsche Bank AG and others. (Ng & Plevin, 2008, p, c.1)

There were plenty of financial transactions involving the bailout of AIG as the government became the driving force behind the bailouts to “circumvent substantial losses” that potentially “threatened the global financial system.” According to Carlos Mendez, a senior managing director at ICP Capital, “It’s like a home run for some of the banks. They bought insurance from a company that ran into trouble and still managed to get all, or most, of their money back” (Ng and Plevin, 2008, p. c.1).

Regardless of the bailouts, a few people were not afraid to condemn the consequences of governmental bailouts involving large institutions (The bailout of the bailout of 2008, p. A. 16):

The government has put taxpayers at risk for a staggering \$150 billion, the objective should be to see an AIG healthy enough to pay back its government loans without allowing government ownership to further distort the insurance market. This is where the latest version of the bailout needs work. There are two typical outcomes when the government owns a controlling stake in a private business. Either Uncle Sam runs it like a government agency, layers it with lawyers and other process facilitators, and slowly erodes whatever value exists. Or the government runs it like a business and uses its unfair advantage in cost of capital and its ability to regulate to defeat the private competition. (The bailout of the bailout of 2008, p. A. 16)

According to Langley et al. (2008), others have criticized the AIG bailout plan in a different context of too much government intervention: “It’s not the government’s role to buy private companies, said Martin Feldstein, an AIG director and former economic adviser to President Ronald Reagan.” However, the chief executive for AIG, Mr.

Willumstead was only left with two options, file for chapter 11 bankruptcy or accept the

Fed's proposal (Langley et al., 2008). In response, Mr. Willumstead opted to take the Fed's offer. Portrayed as heroes of rescuing the financial sector, particularly AIG, this article frames powerful individuals like Bernanke, Paulson, and Geithner as tireless group of individuals working vigorously to "save" AIG (Langley et al., 2008, p. A1):

Mr. Willumstead placed an urgent call to Tim Geithner, president of the Federal Reserve Bank of New York, which was returned Friday morning. He warned the Fed official of the coming liquidity crunch. Mr. Geithner, was enmeshed in the Lehman crisis, urged Mr. Willumstead to keep him apprised. Paulson and Geithner that evening were in an austere conference room on the first floor of the New York Fed's headquarters, having assembled a meeting of Wall Street's top executives. AIG had a desperate need for fresh capital but no clear way of securing it. At AIG, Mr. Willumstead was working through the night with bankers from J.P. Morgan and private-equity firm Blackstone Group to determine how much money the company would need. By next day, the amount of capital needed had doubled to \$40 billion because of the company's fast-deteriorating real-estate related securities. Mr. Willumstead persisted: "I'm proposing a transaction, not a bailout. If we just get the Fed's backing in exchange for collateral, I give you my work I'll sell every asset needed to pay you back." AIG informed that it needed as \$70 billion to avoid failing. Representatives from J.P. Morgan and Goldman Sachs met all day at the Fed's office, Together with Morgan Stanley, they evaluated AIG's liquidity needs and, separately, the viability of a private-sector solution. Their updated conclusion: AIG needed about \$80 billion. After the AIG board approved the offer, Bernanke and Paulson attended a hastily arranged meeting Tuesday night with top lawmakers, many of whom were stunned by the magnitude of the problem and the response. Mr. Bernanke "spelled out what would happen if AIG failed" and that it would "be felt across America and around the world." (Langley et al., 2008, p. A1)

The summarized exchange between the CEO of AIG and the Federal Reserve provides the audience a perspective of these men working persistently to "save" AIG, as they refused to allow this multinational insurance corporation to file for bankruptcy even at the expense of using enormous amounts of taxpayers' money.

Several months later, the original plan of costing \$70 to \$80 billion of taxpayers' money to bailout AIG insurmountably increased to \$150 billion according to Karnitschnig, Plevan, and Ng (2008, p. A.1):

The U.S. government reached a deal Sunday night to scrap its original \$123 billion bailout of American International Group Inc. and replace it with a new \$150 billion package. It gives the government an unprecedented role as an actor in the financial markets. The government would give AIG more money, including \$40 billion from the U.S. Treasury's \$700 billion Troubled Asset Relief Program. The \$150 billion in government aid consists of a \$60 billion loan, a \$40 billion preferred-stock investment, and \$50 billion in capital largely to purchase distressed assets, which are to be placed into two separate financing entities. The new package is a tacit acknowledgement that the original \$85 billion rescue in September, combined with an additional \$37.5 billion made available to the company last month, together haven't come close to stabilizing AIG. Under the new plan, the government is expected to inject about \$20 billion in to the securities lending vehicle, with AIG providing an additional \$1 billion. The entity would then buy the illiquid securities the AIG unit holds, known as residential mortgage-backed securities, for about 50 cents on the dollar. (Karnitschnig, Plevan, & Ng, 2008, p. A.1)

The early reports indicated that AIG's bailout plan will not consist of taxpayers' money, but those reports were too good to be true as the U.S. government made an exception for AIG at unprecedented levels. The extraordinary efforts to save AIG proved to be costly. Since AIG is a global corporation with millions of clients on the hook, the U.S. government spent at least \$150 billion of taxpayers' money to save AIG from bankruptcy. However, AIG was not the only troubled mortgage institution, as Fannie Mae and Freddie Mac found themselves in deep financial crisis.

In addition to the bailout to save AIG, \$700 billion of TARP bailout money was also allocated to two of the well-known housing institutions that were on the verge of collapse. According to Andrews and LaBaton (2008, p. 1), the rescue package for the Fannie Mae and Freddie Mac could potentially be one of the most expensive financial

bailouts in American history, though it will not involve any immediate taxpayer loans or investment:

Treasury secretary, Henry Paulson, who engineered the plan, would not say how much capital the government might eventually have to provide, or what the ultimate cost to taxpayers might be. Mr. Paulson said it was important to rescue the mortgage giants because a failure of either company would cause turmoil in financial in the United States and around the world. (Andrews & LaBaton, 2008, p. 1)

Notice how Paulson used the rhetoric of threatening the entire global economic system if the policymakers failed to assemble a bailout plan for Freddie and Fannie. Whether Paulson is hyperbolizing the situation or not, it is an attempt to gain a tremendous leverage to force an agenda thought the public sector.

The New York Times published an article written by Ross-Sorkin and LaBaton (2008, p. 1) titled, “U.S. Rescue Seen at Hand for Two Mortgage Giants,” regarding Fannie Mae and Freddie Mac:

The huge potential liabilities of the companies could cost taxpayers tens of billions of dollars and make any rescue among the largest in the nation’s history. Shares of Fannie and Freddie would be reduced to little or nothing, and taxpayers could pay any losses on mortgages they own or guaranteed. Shareholders have already lost billions of dollars as the stocks have plunged more than 80 percent this year. Mr. Paulson had hoped that merely having the authority to bail out the two companies, which Congress provided in its recent housing bill, would be enough to calm the markets. After stock markets closed on Friday, the shares of Fannie and Freddie plummeted. Fannie was trading around \$5.50, down from \$70 a year ago. Freddie was trading at about \$4, down from about \$65 a year ago. With Fannie and Freddie guaranteeing \$5 trillion in mortgage-backed securities, and a big share of those held by central banks and investors around the world, Mr. Paulson appears to have decided that the stakes are too high to take chances. (Ross-Sorkin & LaBaton, 2008, p. 1)

The drastic downturn in mortgages and financial markets ultimately forced the Bush administration’s hand. The Bush administration and the Fed essentially overtook the

mortgage giants, and it placed the two institutions under federal control. An article published by *The New York Times* titled, “A History of Public Aid during Crisis,” by Schwartz (2008, p. 27) briefly discussed past government interventions and compared these with bailouts of Fannie and Freddie:

The effort to save Fannie Mae and Freddie Mac is only the latest in a series of financial maneuvers by the government that stretch back to the rescue of the military contractor Lockheed Aircraft Corporation and the Penn Central Railroad under President Richard M. Nixon, the shoring up of Chrysler in the waning days of the Carter administration and the salvage of the saving and loan system in the late 1980s. The closest historical analogy to the Fannie-Freddie crisis is the rescue of the Farm Credit and saving and loan system in the late 1980s. The savings and loan bailout followed years of high interest rates and risky lending practices and ultimately cost taxpayers roughly \$124 billion, with the banking industry kicking in another \$30 billion. Even if the rescue of Fannie and Freddie ends up costing tens of billions of dollars, the savings and loan collapse is still likely to remain the costliest government bailout to date. The S&L debacle cost upward of \$100 billion, and the economy is more than twice the size today than it was in the late 1980s. (Schwartz, 2008, p. 27)

The Federal government managed “rescue” Fannie Mae and Freddie Mac and it appears that the subprime crisis forced the regulators and policymakers to shove economic ideology aside and indulge these firms and institutions into a business of bailouts.

With history repeating itself in the current state of financial crisis and the increasing rates of inequality, one must ask whether these financial institutions (from micro to macro) are “too big to fail.” An article written by Goodman (2008, p. 1) discussed the current state of our economic landscape:

In the narrative that has governed American commercial life for the last quarter-century, saving companies from their own mistakes was not supposed to be part of the government’s job description. The Bush Administration, which does cast itself in the Reagan mold, hastily prepared a bailout package to offer the government-sponsored mortgage

companies, Fannie Mae and Freddie Mac. The mortgage giants were too big to be allowed to fail. (Goodman, 2008, p. 1)

To justify why the legislators decided to push for a series of bailouts, Goodman (2008)

explained the perpetual global consequences of the mortgage crisis:

Fannie and Freddie own or guarantee nearly half of the nation's \$12 trillion worth of home mortgages, so the whole system of finance for American housing, threatening a most unfortunate string of events: First, an already plummeting real estate market might crater. Then the banks that have sunk capital into American homes would slip deeper into trouble. And the virus might spread globally. The central banks of China and Japan are on the hook for hundreds of billions of dollars worth of Fannie's and Freddie's bonds – debts they took on assuming that the two companies enjoy the backing of the American government. Commercial banks from South Korea to Sweden hold investments linked to American mortgages. Their losses would mount if American homeowners suddenly couldn't borrow. The global financial system could find itself short of capital and paralyzed by fear, hobbling economic growth in many lands. Treasury secretary, Henry Paulson, announced that the government was willing to use taxpayers funds to buy shares in Fannie and Freddie – one that could ultimately cost hundreds of billions of dollars. (Goodman, 2008, p. 1)

In addition, Goodman (2008, p. 1) presented the hazardous act of bailing out these larger than life institutions and the long-term consequences that may prompt complications down the road for Americans:

They are going to raise the cost of living for every American. The government is debasing the value of our money. Freddie and Fannie need to fail. They are too big to save. Using public money to spare Fannie and Freddie would increase the public debt. The United States has been financing itself by leaning heavily on foreigners, particularly China, Japan and the oil-rich nations of the Persian Gulf. Were they to become worried that the United States might not be able to pay up, forcing the Treasury to offer higher interest rates of interest for its next tranche of bonds. And that would increase the interest rates that Americans must pay for houses and cars, putting a drag on economic growth. (Goodman, 2008, p. 1)

As long as the U.S. dollar is the world's reserve currency, the U.S. government will continue to engage in bailouts of larger than life financial institutions such as AIG,

Freddie, Fannie, large banking sectors, etc. The United States financial structure will not be allowed to crumble, just as AIG, Fannie and Freddie were all saved from the recent financial crisis. The reality is that the system has too much riding on the survival of these financial institutions. The policymakers from the 1930s and today vastly differentiated themselves in their response to the economic crisis. The creation of regulatory acts headlined by the Glass-Steagall Act provided economic stability, while the current policymakers today essentially paved over the monetary crisis with bailouts. Some critics argue that this style of crisis management can only result in negative consequences down the road. Although the current set policymakers neglected to pass stringent macro regulations, one man decided to propose an effective solution that would regulate certain banking transactions.

In response to the crisis, former Chairman of the Fed, Paul Volcker created a new banking act that regulates banks proprietary trading, which consists of transaction in securities and other financial tools for the benefit of the bank, rather than on behalf of consumers. The Volcker Rule establishes extra capital requirements on shadow banks participating in proprietary trading, and it limits banks ownership stakes in hedge funds and private equity funds (Mitchell, 2010). Although the regulatory act was proposed in 2009, the financial lobbyist managed to weaken the act by advocating against it. Similar to the Glass-Steagall proposal, the Volcker Rule is facing similar scrutiny of potentially “stunting” the growth of the financial sector.

In early parts of 2009, Joe Nocera of *The New York Times* published an article titled, “The Risk in Money Funds” (2009) advocated for Paul Volcker’s advice of regulating the money market funds similar to bank deposits: “When push came to shove,

they got government support. If they are going to maintain ban like characteristics, they ought to be insured and regulated.” Supported by Senators Jeff Merkley and Carl Levine, the Volcker Rule was drafted to regulate the banking industry: “President Obama proposed the Volcker Rule as the administration sought new ways to crack down on risk and size at financial companies” (Johnson, 2010).

When President Obama officially took over in 2009, his economic staff did not carry the strongest reputation for overseeing the damaged economy with a strong regulatory mindset. A *New York Times* article titled, “Starting the Regulatory Work” (2009, p. A30), it discussed the former Fed chairman as the only trusted regulator:

Will Mr. Obama deliver? Without a clear signal from the President-to-be, the early signs are not terribly encouraging. There are no prominent consumer or investor advocates among his top economic advisors. Except for Paul Volcker, the former Federal Reserve chairman, there are no officials or regulators, past or present, who have distinguished themselves by giving early warning of the impending catastrophe or taking strong action against the excesses that were fueling it. (Starting the regulatory work, 2009, p. A30)

Although the jury is still out on Obama’s economic staff, the author forgot to mention the former Treasury Secretary, Tim Geithner who is essentially Larry Summers 2.0. During the Clinton Administration, Larry Summers heavily advocated for the deregulation of the financial industry and he was one of the main advocates of repealing the Glass-Steagall Act. Perhaps, it may indicate the direction of the U.S. economic policies. Throughout Geithner’s time in office, he never went out of his way to advocate for the Volcker Rule.

The Volcker Rule was an attempt to keep the banks honest from fraudulent dealings that took on too much risk. In an article written by Chan (2010, p. 1) titled, “Bill

Offered to Restrict Big Banks” explained the potential outcomes if the regulatory bill passed in U.S. Congress:

The Legislation would ban banks that take federally insured deposits from investing in hedge funds or private equity funds and from making trades that are the benefit of the banks, not their customers, a practice known as proprietary trading. Goldman Sachs and Morgan Stanley would probably be the Wall Street firms most affected by the ban, known as the Volcker Rule, but they might be able to shed their status as bank holding companies, to avoid some the restrictions. (Chan, 2010, p. 1)

Paul Volcker advocated that the burden would be shifted away from the government, to the banks, using broad bans of classes of behavior:

Implementing the so-called Volcker Rule, regulators should adopt something akin to antimoney-laundering laws, where the federal government bans a particular behavior and then places the onus on banks to screen for red flags and comply with the rules. His suggestion: Bar banks from trading with their own funds if they benefit from any type of government guarantee, such as deposit insurance. Banks would have to police their own activities to make sure they are in compliance, with Federal Reserve examiners ensuring that is the case. Mr. Volcker’s concern is that narrow or prescriptive rules would invite gamesmanship on the part of banks and could allow firms to evade the rule’s intent. Already, some banks and their lobbyists are seeking to sway regulators and encourage them to narrowly define certain types of trading activities. (Volcker on his rule – keep it broad, 2010)

Despite the financial lobbyists that strongly opposed the Volcker Rule, prominent financial figures such as John Reed, William Donaldson, George Soros, and five former treasury secretaries’ strongly support this regulation (Chan, 2010, p. 1). However, every regulatory act will leave a trail of blood for the detractors. Similar to the Glass-Steagall Act that experienced heavy fire for the advocacy efforts of downsizing the banking industry, the Volcker Rule has been subjected to similar scrutiny (Chan, 2010, p. 1):

When Mr. Volcker and the deputy Treasury Secretary, Neal S. Wolin, presented the plan to the Senate last month, they were met with a frosty reception. Senators said, the rule would not have prevented the financial

crisis or saved companies like Bear Stearns, Lehman Brothers, and the American International Group. They said the idea, as outlined by President Obama, was vague and difficult to enforce. And representatives of Goldman Sachs and JPMorgan Chase testified that limits on risk-taking could be achieved by other means. (Chan, 2010, p. 1)

Similar to the criticism of the Glass-Steagall Act, the financial lobbyists have trivialized the regulatory act as an insignificant regulation that fails to prevent catastrophic banking crisis and it would only serve as a barrier to U.S. financial system. Despite criticisms of the Volcker Rule, advocates continued to push for the regulation. One anonymous source called the regulatory act, “common sense” in an article titled, “The Volcker Rule is Just Common Sense” (2010, p. A.18):

There is a direct correlation between the creation of exotic derivatives and the poor judgment that went with it, and allowing banks to trade. Those who complain that the Volcker rule will reach too far into every corner of the economy miss the point that the instability and Goldman-like dishonesty of proprietary trading has already gone there, so the fix must go there too. The Volcker rule simply reinstates time proven common sense to the system. (The Volcker rule is just common sense, 2010, p. A.18)

However, the advocates appear to be irrelevant when Wall Street and large banks feel threatened by any sign of regulations. As several sources from *The Wall Street Journal* and *The New York Times* have reported that, the banks and individuals have persistently lobbied against the Volcker rule, according to Lucchetti and Rappaport (2010, p. C.1) from *The Wall Street Journal*:

Dozens of career regulators at the Federal Reserve, the Securities and Exchange Commission, and the Treasury Department are facing off against bankers, lawyers and other officials at financial firms that want to soften the impact of the rule named after former Fed Chairman Paul Volcker, which outlaws trades that are not designed to meet near-term client demand or as a hedge. Goldman Sachs Group Inc., Credit Suisse Group AG, and Morgan Stanley have argued in meetings with Treasury officials that they should have wide trading flexibility when clients are

involved or when the trades are meant to manage risk. (Lucchetti & Rappaport, 2010, p. C.1)

Goldman Sachs officials and its lobbyists will do whatever it takes in their own power to weaken any financial reforms, even if they make a little impact on the economy

(Lichtblau & Dash, 2010, p. 1):

Goldman and its lobbyists have approached Senate Democrats directly on areas of particular concern, like the so-called Volcker Rule, which would bar institutions like Goldman from buying and selling for their own profit, rather than as a service to its clients. (Lichtblau & Dash, 2010, p. 1)

Despite the conflict between the financial sector and Paul Volcker, some believe that the Volcker Rule will not be fully implemented due to the strenuous process of thoroughly reviewing the legality of the legislation (Why Wall Street May Love a Punishing Election, 2010): “Some Volcker Rule provisions won’t be implemented for 12 years, and it could take 15 months before a study is completed and final rules are issued.”

Unlike Glass-Steagall that was approved on several occasion, the fate of the Volcker Rule seems to be turning its ugly head as the lobbyists completely trivialized the significance of its regulatory powers.

On February 10, 2010, Paul Volcker attended the Senate Banking Committee to discuss his regulatory act, but his ideas were quickly squandered (Weidner, 2010):

It died Tuesday before the Senate Banking Committee from unnatural and illogical causes: the finance lobby, obstruction, fear-mongering and plain ignorance. Too bad for all of us, his prescription for reform will be discarded like loan underwriting standards for a multi-family home near Las Vegas. Mr. Volcker’s testimony was at once a brilliant articulation of the structural dangers of Wall Street as it stands and a forceful warning. He clarified the most controversial part of the rule, the ban on proprietary trading for commercial banks. But given the reaction of committee members, the Volcker Rule appears to be doomed. By the end of his testimony the dais was nearly empty, big bank stocks rallied. The only question now is whether the bill will be gutted or euthanized like failed

investment banks would have been under the Volcker plan. (Weidner, 2010)

Unlike the Great Depression, the half-hearted reaction from the committee truly reveals the lack of interest in passing any forms of financial regulations. Some of those who advocate for financial reform are in full support of implementing the Volcker Rule, while others that are old-fashioned are in support of reviving the Glass-Steagall Act. An article written by Thomas (2010) titled, “Bring Back Glass-Steagall; Banks that Behave Like Hedge Funds Don’t Deserve Guarantees” discussed his advocacy efforts of resurrecting the abolished act:

Senators Maria Cantwell and John McCain proposed a measure that would revive parts of the old Glass-Steagall Act, the 1933 law that separated investment from commercial banking. After having been diluted many times over the years, Glass-Steagall was largely repealed in 1999, permitting a wave of consolidation in the financial industry. Nobel laureate economist Joseph Stiglitz has argued that the repeal of Glass-Steagall had an “especial role” in making the financial calamity of 2008 possible. Former Fed Chairman Paul Volcker, currently the head of the President’s Economic Recovery Advisory Board, has called for a new separation between commercial banking and riskier financial activities. Today, we begin to debate Glass-Steagall all over again.....to re-regulate the financial sector, the answer involves some version of the idea behind Glass-Steagall—drawing a line between banks that the government effectively guarantees and banks that behave like big hedge funds, experimenting with the latest financial toxins. (Thomas, 2010)

However, others believe the current landscape of our financial woes has nothing to do with regulations and de-regulations as noted by Timiraos (2008):

The problem may have more to do with management than regulation – indeed, top executives have been booted from the banks that posted the biggest losses. Banks have struggled to eliminate blind spots for risk, in part because banks have grown so large. It’s so big, the leadership has been finding it hard to keep all of the pieces working together. No matter what any regulator or legislator does, financial markets will create as much risk as they want. (Timiraos, 2008)

Timiros presents a great argument that these larger than life banks must downsize as the banking executives have tough time “keeping all the pieces working together.” Others are reluctant to support the Volcker Rule or restoring Glass-Steagall Act due to skepticisms surrounding the current economic corruptions as noted by Dixon (2009, p. B2):

Glass-Steagall would not have stopped the current crisis. For starters, many institutions that have had trouble were not commercial banks. Lehman Brothers, Bear Stearns, and Merrill Lynch were investment banks; American International Group is an insurance company. All four caused havoc when they teetered or, in Lehman’s case, collapsed, any institutions that is too big to fail, even if it is not in the utility end of banking, requires some of regulation. Of course, lots of commercial banks have also gotten into trouble. Think of Citigroup or, across the Atlantic, the Royal Bank of Scotland or Switzerland’s UBS. One reason was that they invested in troubled securities. So it is appealing to think that they would have been safe if only they had not mingled the casino with utility. The solution is not to pick on one particular banking activity – like proprietary trading – label it as risky and quarantine it in some half-regulated purgatory. The better approach is to improve risk management across the industry. Many changes are required to achieve this, including compensation systems that do not encourage bankers to take excessive risks, but an essential element must be a regulatory system – ideally, a simpler one than what the United States has now – that requires banks to increase their capital buffers as they increase the risk they take. Given that capital is expensive, it will discourage them from taking too many risks, and thus, keep them from collapsing. (Dixon, 2009, p. B2)

Banks and financial firms must be closely monitored from engaging in fraudulent practices and they must be prohibited from taking excessive risks. One of the real dangers is that if one firm experiences termination, it has the potential to drag down the entire financial system. In order to avoid that ominous scenario, the U.S. Congress must devise a plan to end, “too big to fail.”

The economic landscape from the 1930s to 2008 has vastly changed, while other factors have stayed constant. First, we see a commonality of false admirations during both eras for people that are praised such as the bankers that destabilized the financial

system and government officials using taxpayers' money to bailout financial institutions. Second, the legal proceedings during the Great Depression actually pursued the core problems as they confronted banking executives for financial fraud, but the prosecutors during the contemporary crisis failed to criminally prosecute those responsible for their role in the Great Recession. Lastly, the lawmakers during the Great Depression managed to pass financial reforms such the Glass-Steagall Act that downsized the banks; however, the leaders during the contemporary era responded by bailing out the financial institutions, consolidation of banks and lobbyists worked to persistently abolish any forms of financial regulations. The next chapter will discuss the post-recession problems through the analysis of alternative media discourses. These financial practices are deadly as the mainstream press refuse to acknowledge the truth behind these corrupt practices.

CHAPTER FIVE

SUMMARY AND ALTERNATIVE DISCOURSE

Chapter Five concludes this thesis with a summary of the arguments developed in previous chapters and then concludes by providing an alternative approach to viewing the causes, and management of the contemporary financial crisis. Chapter Five starts by reviewing the conclusions and arguments made in previous chapters. This review emphasizes the three critical themes from Chapter Four: (1) High Praises, Heroes and Lies; (2) Financial Criminal Investigations during the Great Depression and the Contemporary Crisis; (3) Policy Responses. The second half of Chapter Five will address the post-recession economic problems and solutions through the analysis of alternative media discourses. This analysis will provide an alternative outlook on the current financial situation, which is readily ignored by the mainstream press. It will be argued that financial “arsenals” such as the unregulated high-frequency trading (HFT), the outstanding derivatives market, and “money printing” (i.e. quantitative easing) are destabilizing the current economic landscape.

Summary of Thesis Arguments

Chapters Two and Three analyzed the historical economic landmarks in chronological order involving governmental regulations beginning with the rise of laissez-faire capitalism starting in the seventeenth century. Prior to the seventeenth century, the standard European economic model primarily operated by the monarchs that established domestic monopolies, while funding colonialism abroad to aggressively seize

precious commodities such as gold and silver. The costs of foreign wars and colonial voyages were not pressing issues as long as the expeditions brought back the maximum amount of wealth at the expense of exploited foreign nations. Considered as the father of economics, Adam Smith criticized the hegemonic system of mercantilism because it mainly benefited the merchant aspirations of extending international commerce. Smith delineated the high cost of tariffs, duties, regulations that restricted trading and prompted higher standard of living. *“The Wealth of Nations”* was not an ordinary book as it radically shifted economic thought. His eloquent advocacy of natural liberty galvanized the minds of a rising generation, arguing that if individuals are left to their own devices, pursuing their own self-interest will generate a self-regulating and highly prosperous society.

Adam Smith published a book titled, *“The Wealth of Nations”* that advocated for the upmost economic independence, and he influenced a series of classical economists in France and England: Jean-Baptiste Say, Frederic Bastiat, Thomas Malthus, David Ricardo, etc. However, these men did not carry on the message of Adam Smith as they developed their own economic perceptions and models. Ricardo’s wealth distribution model is divided amongst the landlords, workers and capitalists. If the capitalists and the landlords are projected to gain majority of the profits, then the workers instantly lose out on equal chance of gaining wealth. Smith, on the other hand, focused on the co-existence that eliminates class conflict between the landlords, capitalists and workers. If the pie expands, all social classes stood to gain. This became a serious problem because the contrasting differences between Ricardo and Smith provided ammunition for the economists in the 1800s that rejected laissez-faire economic policies in favor of colonial

mercantilism. In the 1800s, European workers failed to unionize and colonialism ran rampant in regions that were rich in naturalized resources in the Middle East and Africa. As the powerful European nations embraced colonialism abroad, the United States took a domestic approach in expanding its vast nations thought the expansion of railroads.

During the nineteenth century, the United States experienced substantial economic and corporate expansions. The rise of corporations in the post-Civil War era was mainly modeled after the railroad industry. Although state governments chartered the railroads, they were initially subsidized by local towns to stimulate economic growth. For example, towns created lavish portraits of train stations to entice outsiders as an opportunity for a vacation destination. In 1886, in a case between Santa Clara V. Southern Pacific Railroads, the United States Supreme Court ruled corporations as “persons” under law protected by the fourteenth amendment. In addition, the U.S. government passed the Sherman Anti-Trust Act, which led numerous corporations to consume one another by undercutting competition. Originally, the law intended to sustain free market competition, but the act restructured corporate ownership, thus prompting market consolidations. The public often regarded the newly consolidated corporations during the early twentieth-century as unfavorable greedy monsters of society that hijacked the government and social institutions. To reverse the adverse public perceptions, corporations utilized a public relations (PR) strategy that commenced a new style of advertisement. It promoted the ideals of human understanding, sympathy, contacts, and relationships that convinced the public to immerse themselves in the modern company. The humanitarian public relations campaign efforts established the blueprint for the rest of the mega-corporations to renew their relationship with the public. The rise of

corporations during the early twentieth century propelled the U.S. economic system toward new heights, especially during the era of “Roaring Twenties.”

The post WWI decade of the “Roaring Twenties” was characterized by economic prosperity that financially propelled the American business industry to all time highs. However, economic opulence dose not last forever, as prosperity often ends. Speedy financial growth and the rapid increase of consumption came to a screeching halt due to threats of overproduction and financial fraud, which inevitably led to the stock market crash of 1929. Presumably, the United States failed to comprehend the boom-bust business cycles of capitalism as the deregulated market and unsound governmental policies led to the outcome of substantial economic and social fragility. By 1932, the world manufacturing sharply plummeted by two-thirds (67%) and unemployment sharply escalated to over 13 million people in the United States (Chambers et al., 1983). The situation became dire as quarter of the working population was unemployed and the banking system was facing utter collapse.

Although it is typical for markets to fluctuate, the Great Depression of 1929 did not occur by accident. The crisis was an accumulation of massive fraud that went unnoticed over the years, but there was one brave soul that volunteered to expose the individuals responsible by conducting an investigation of the financial industry. Known as the Pecora Commission, the inquiry commenced on March 4, 1932 by the United States Senate Committee on Banking and Currency to investigate the root causes of the Stock Market Crash. The Congressional hearings led by Ferdinand Pecora, a Manhattan prosecutor, famously interrogated Charles Mitchell, the CEO of National City Bank for promoting risky securities and fraudulent financial activities. In facing humiliation, the

financial sector squandered the public's trust as their reputation imploded throughout the Pecora Commission. The Pecora hearings not only revealed the fraudulent financial practices, but the revelation of fraud forced the U.S. Congress to assemble strict financial restrictions.

In response, President Roosevelt and two members of Congress, Carter Glass and Henry Steagall, drafted the Glass-Steagall Act in 1933 that separated investment and commercial banking activities because commercial banks absorbed too much risk with depositors' money. In addition, the act prohibited bank holding companies from owning financial companies. Glass-Steagall Act ended the inherent conflict of interest between the commercial banks (lending) and the investment banks (ownership) by separating the two entities; therefore, the law allows both investment banks and commercial banks as long as they are separated entirely. For instance, a stock brokerage firm could not own an insurance company or a bank and vice versa. Large financial firms, such as JP Morgan, were seen as part of the problem and were directly targeted and forced to cut their services. By allowing FDR's New Deal program to integrate with the United States political and economic system, the era of regulated capitalism predicated on infrastructure boosted the U.S.'s global dominance at the forefront of the world.

However, capitalist productivity slowed as industry matured across the twentieth century. The United States experienced a stage of stagflation in the 1970s, which is defined as low economic growth and high inflation. In response, policymakers decided to abandon infrastructure-based economy in favor of a market-based economy. As a result, the United States experienced another round of deregulation. In order to repeal the Glass-Steagall Act of 1933, the policymakers took several initiatives, such as reinterpretation of

the Glass-Steagall Act in 1998 when Citicorp and Travelers Insurance Company merged to form Citigroup. Under Glass-Steagall, this transaction was illegal, but the Federal Reserve's reinterpretation of the banking regulation assisted the completion of the merger (PBS Frontline, 2003).

During the Clinton Administration (1993-2001), the Legislative Branch and the Federal Reserve gave the green light to banks to get deeply involved in investment banking, which welcomed the conflict of interest in these banks by pushing shady financial investments on investors who were oblivious to the consequences (Gupta, 2008). The final blow that completely abolished the Glass-Steagall Act occurred in 1999, when Congress decided to pass the Gramm-Leach-Bliley Act. By passing this bill, it gave control to bank's securities firms and insurance companies under the common ownership. By abolishing the banking firewall that is the Glass-Steagall Act, the financial sector experienced a serious round of consolidation throughout the American economic system. The global economy grew at unprecedented rates, while the thought of an economic downturn seemed preposterous. However, this debt-fueled growth came to a crashing halt as the world experienced the second worst economic crisis in history on September 15, 2008, when the fourth largest investment bank in the United States, Lehman Brothers filed for bankruptcy. This triggered a ripple effect on the system as Lehman acted as a financial anchor that dragged the entire system down into the abyss.

Prior to the crisis of 2008, the subsequent boom in the sub-prime mortgage market allowed numerous unqualified individuals to become homeowners saddled with outlandish loans made available by the aggressive financial institutions in order to line their own pockets. The government and the bankers created an illusion that housing

prices always rise. Meanwhile, consumer defaults on high interest loans seemed improbable because the loans could be forever refinanced (Galbraith, 2009).

Unfortunately, numerous subprime borrowers defaulted when they were unable to pay higher rates required by re-sets on mortgage arms. Home prices began to fall with cascading foreclosures.

Homeowner defaults threatened vast amounts of mortgage-backed securities. The collapse of mortgage-backed securities ultimately caused massive derivative defaults. AIG, a global insurance institution sold a kind of derivative called a credit default swap, which insured against defaults in mortgage back securities. AIG neglected to back these derivatives with adequate capital reserves. When the subprime meltdown occurred AIG was unable to pay out credit default swaps to their counterparties until the New York Fed lent AIG over \$182 billion in bailout money (Nadesan, n.d.; Teitelbaum & Son, 2009).

Using taxpayers' money, the United States government drafted and signed into law by President George W. Bush on October 3, 2008, a \$700 billion bailout emergency package called Troubled Asset Relief Program (TARP) that bailed out multiple financial and housing institutions facing heavy liquidity crisis, such as AIG, Freddie Mac, Fannie Mae, and large banks. Unlike the Great Depression, the current crisis profoundly failed to discipline, let alone even attempt to prosecute, central figures involved in today's financial crisis. Instead of prosecuting guilty individuals, the government created moral hazards for the financial institutions by using taxpayers' money to bailout the financial sector. Despite the United States remarkably paving over the worst financial crisis since the Great Depression, our nation is still facing a daunting task of stabilizing the national economy. The state of our economy is highly volatile as post-recession problems still

linger today, from the flash crash in 2010 to the Libor scandal that manipulated the interest rates involving the mega banks around the world.

Summary of Comparative Analysis of Press Coverage

Chapter Four analyzed the discourses found in mainstream press covering two historic economic eras, the Great Depression (1929) and the Great Recession (2008). The articles from *The New York Times* and *The Wall Street Journal* were mainly derived from an academic database called ProQuest. The first major theme identified across the articles was titled, “High Praises, Heroes, and Lies.” This theme revealed media discourses that indicated a journalistic search for “heroes” during the dismal times of economic instability in the 1930s. Prior to the Pecora investigation, *The New York Times* provided headlines regarding the substantial losses around the time of “Black Tuesday.” To temper the negative press reports of the time, *The New York Times* framed the bankers as a voice of reason that encouraged audiences to remain optimistic. However, these headlines can also be construed as a discursive deception, which distracted the public from the hardships of the financial depression by encouraging them to believe that the system was being saved by prosecuting wrongdoers. The press has also manufactured heroes during the contemporary crisis. Three notorious bankers stood out in press accounts as the “saviors” of the financial system: Tim Geithner, Ben Bernanke, and Hank Paulson. According to mainstream media accounts, their persistence and expertise remedied the global economic crisis, thus avoiding an economic doomsday.

The media discourses of heroic figures saving the system may be propagandistic in that they offer reassurances to the public during tumultuous times, thereby facilitating audience disengagement. For instance, during the Great Depression, the stock market suffered a series of devastating blows, but the mainstream press greatly suppressed the scale of the economic impacts. During the 2008 crisis, the media discourses designated Ben Bernanke, Tim Geithner, and Hank Paulson as the individuals capable of stabilizing the economic crisis. Public accolades for Geithner and Bernanke's "heroic" efforts extended their financial careers within the new Obama presidential administration. Yet, these so-called heroes may have actually undermined the scale of response required to re-regulate capitalism.

The second theme identified in media accounts contrasted the nature of criminality involving the Great Depression (1929) and the contemporary crisis (2008). During the 1930s, the U.S. Senate Banking Committee assembled a legal team led by Ferdinand Pecora to investigate criminal transactions involving the financiers. During the investigations the media discourse shifted in an unfavorable manner for the bankers. *The New York Times* extensively covered the case of Charles Mitchell of National City Bank for financial fraud, speculation, and reckless securities. The publication's extensive coverage made an example out of Charles Mitchell for committing financial fraud. During the Great Depression, the press called for and documented prosecutions. For example, the press covered banking titan in Charles Mitchell of National City Bank public interrogation for financial fraud; thereby, triggering a compelling message stating, 'no individual is above the law.'

In contrast, the newspaper publications during the current 2007-2009 crisis were reluctant to mention the high-level banking executives that may have been responsible for the crisis. No calls were made for assembly of a team of federal prosecutors similar to the Pecora Commission. Rather, it can be argued that contemporary articles communicated a series of stories that rationalized the lack of systemic investigation and prosecution by federal authorities. Stories focused on the lack of resources and employees to properly investigate and prosecute the individuals believed responsible for the crisis. It was demonstrated that the culture and the discourse of criminal prosecutions shifted during the crisis of 2008 when the CEO of late Lehman Brothers, Rich Fuld was able to escape criminal charges for financial fraud. High-level bank officials escaped unscathed, rather than serving as examples of the universality of justice. Only lesser-known individuals, who were often women or minorities, were prosecuted and sent to prison.

The last theme detected in the media and examined in this project compared the policy responses during the Great Depression and the present crisis. The Pecora commission led to a series of regulatory acts in reaction to the rapid bank failures and corruptions. By drafting and advocating for regulations in the banking sector, individuals like Carter Glass and Henry Steagall faced intense backlash from Wall Street and their colleagues. The heavy criticisms did not deter them from regulatory actions; instead, President Roosevelt signed the legislation and their efforts were rewarded once the banking sector stabilized. In contrast, during the current crisis, policymakers heavily lobbied for the Troubled Asset Relief Program (TARP), which bailed out the large financial institutions, such as banking and insurance for sub-prime loans and investments. The current group of lawmakers abandoned the philosophy of universal justice and

advocated for something completely different. This thesis suggests legislators have failed to address the core issues pertaining to financial frauds, deregulation, mismanagement of corporations, and accountability for the mishandlings large sums of capital.

Although little has been done, many critics of the crisis have proposed solutions. Some have advocated reviving the Glass-Steagall Act, while others disapprove of the idea because the financial landscape has vastly changed since 1933. In 2009, the former Chairman of the Fed, Paul Volcker attempted to install a new regulatory act that bans proprietary ('prop') trading. Prior to Paul Volcker's regulatory proposal on proprietary trading, mega banks such as JP Morgan Chase and Goldman Sachs utilized "trading desks" to engage in financial transactions for buying and selling securities with their own capital to generate profits. The key element for the trader is to generate the most amount of profit by buying low and selling high. Whether the trader trades for commodities, options, shares, currencies, derivatives or bonds, they have the option to cover right away or later (Das, 2010, p. 60). Proprietary trading may lead to gambling on property, complex derivatives, or any trade assets (Stewart, 2010). On a broad level, the "trader desk" sold collateralized debt obligations (CDOs) based in debt-bonds to the customer desk; yet, the banks placed bets against their own clients with credit default swaps (CDS), predicting that these clients would default on their loans. In the critically claimed documentary, *Inside Job* (2010), Allan Sloan of *Fortune Magazine* described how he first experienced the world of subprime mortgages through a trading desk that revealed horrendous number of securities issued by Goldman Sachs:

Borrowers had borrowed, on average, 99.3 percent of the prices of the house. Which means they have no money in the house. If anything goes wrong, they're gonna walk away from the mortgage. Two-thirds of the

loans were rated AAA, which meant they were rated as safe as government securities. (Ferguson et al., 2010)

During the peak of the economic “boom,” during the first half of 2006, Goldman Sachs sold over \$3.1 billion of these toxic CDOs (Ferguson et al., 2010). This is one of the major reasons why the United States government decided to ban ‘prop’ trading. Under the Volcker Rule, banks are prohibited from trading their own accounts, but they are still allowed to hold securities on a short-term basis in relation to risk-mitigating hedging activities. In addition, banks are not prohibited from trading on behalf of the customer and government obligations (Volcker Rule as of July 10, 2012, 2012). In 2010, JP Morgan Chase and Goldman Sachs announced their decisions to shut down proprietary trading desks in compliance with the Volcker Rule. The elimination of proprietary trading comes at a heavy price as these two mega banks estimated losses of billions of dollars in annual profits (Kopecki & Chanjaroen, 2010). The original intent for the Volcker Rule was to prevent the mega banks from undertaking excessive funds with firms’ own capital, but Paul Volcker underestimated the power of financial lobbyists that weakened the integrity of the regulatory act.

Despite the attempts to limit the power of “too big to fail” banks, the financial lobbyists persistently diminished the integrity of the proposed Volcker Rule. Paul Volcker even advocated the benefits of the act in front of the Senate Banking Committee in 2010, but the committee did not budge. Several articles framed the Volcker Rule as an enemy to the banks because the rule sought to limit banking powers. In an attempt to water down the regulatory act, large banks such as Goldman Sachs and individual lobbyists, persistently visited the policymakers in D.C. to weaken the Volcker Rule. The

current state of the Volcker Rule fails to possess its original regulatory powers as it has been redrafted numerous times since its original proposal back in early 2010. The Great Depression (1929) and the Great Recession (2008) made it critical to implement a system of regulatory acts in order to protect the populace from financial frauds and blind speculative bets. Despite getting over the last recession from 2007 to 2009, the system is still impacted by high rates of volatility and fragility as regulators and policymakers continue to neglect the complex, risk-based financial transactions that are running rampant at Wall Street.

Chapter Four briefly analyzed the discourses of historic economic events using two of the most mainstream newspapers: *The New York Times* and *The Wall Street Journal*. The next section will shift focus toward the discussion of post-recession problems through the lens of alternative media discourses. Mainly derived from the World Wide Web, the rise of Internet amongst the populace provides nuanced information to individuals all over the globe. The alternative press offers additional news frames, shaping in alternative ways how audiences view and analyze information about the economy and government policy, among other issues. This next section will shortly examine the popular phenomenon of alternative media in relation to their coverage of the current financial crisis.

Alternative Views and the Alternative Media

The concept of the alternative press is not merely a contemporary phenomenon amongst our society. It can be argued that the alternative presses have existed as long as

the mainstream press, due to dissenting views on social hegemony. For example, Johann Gutenberg's famous printing press in the fifteenth century radically changed how the commonwealth practiced Christianity, as prior to his printing press the *Bible* was only available to the clergy (Karat, no date). The printing press was able to break the institutional hegemonic rule over the populace deriving from the priests' exclusive access to information. Therefore, the alternative media enabled by the print press and more recently by the Internet help to empower people by providing information previously available to a selected few.

Alternative media outlets perform similar duties of disseminating information through the internet, magazines, newspaper, radio, television, etc. However, in comparison to the mainstream press, the alternative media do not command the same amount of prestige and reputation in the eyes of the populace. Unlike the mainstream press, alternative media are less likely to be owned by large corporations and agencies, such as GE and Comcast. Currently, the multinational mega corporations owning the mainstream media are perceived as the main drivers for biased and/or selective reporting. Let's take a look at the past and present corporate affiliations of one of the most "revered" publications, *The New York Times*. Corporate affiliations include Schering-Plough International (pharmaceuticals), the John D. and Catherine T. MacArthur Foundation, Chevron Corporation, Wesco Financial Corporation, Kohlberg & Company, The Charles Schwab Corporation, eBay Inc., Xerox, IBM, Ford Motor Company, Eli Lilly & Company, etc. (Global Research, 2012). It is critical for the audience to understand the strong alliance between mega corporations and the mainstream press. Corporate

ownership of major mass media organizations can shape journalist discourses, especially when economics are concerned.

The alternative press is heterogeneous in viewpoints and typically is not owned by a mega corporation. One of the biggest alternative news sites, *Global Research Centre for Research on Globalization* has been actively informing the audience on a wide range of issues ranging from geopolitics, foreign wars, and global economic calamities without accepting private foundations (Global Research, 2013).

One of the critical functions of the alternative press is to shed more light on dire situations that are neglected from the mainstream press. The people of the United States and other nations with free speech rights possess the luxury and the freedom to advocate for social change through alternative media. In contrast, some countries have implemented censorship that prevents certain types of media from being available for public viewing. Although under-utilized, the alternative media promote free exchange of ideas and viewpoints.

According to Lee (2007), alternative media can be interpreted from the viewpoint of Marxism to “serve the public interest of the working class.” Lee (2007) goes further by stating, “It is media that play a central role in production, and distribution of a ruling class’s hegemony and that is this way the media become primary center of capitalist values, primary weapons of social control.” Instead of promoting a one-way communication discourse, the concept of a global public sphere utilizing alternative media enables individuals across the globe to communicate without the burden of censorship and corporate and commercial interest (Ramirez Pinzon, Sanchez de Sales & Winzer Ruiz, no date).

The digital revolution in the last 25 years has increased the popularity of alternative media discourses, which are mainly driven by the expansion of Internet technology. Over the years, the mainstream press became more concentrated than ever (Waltz, 2006). Some have claimed that governments, special interest groups, and corporations have compromised the integrity of journalism to the extent that the mainstream press is now associated with the term, “propaganda machine.” In response, people are increasingly turning to alternative media as a default option for news coverage. The main source of alternative press lies in the World Wide Web, where it is easy, affordable, and accessible for people to produce in an uncontrolled nature, without the constraints of the government or corporate interests. Importantly, the internet’s capability to contact vast amount of people all over the globe makes online sources of alternative media extraordinarily popular (Karat, no date). The next section examines the post-recession problem using alternative discourses from various sources. Some alternative media sites were clear in revealing their authors’ identities, while others like *Zerohedge.com* opted to cover their identities by substituting their real identities with pseudonyms (a fictitious name), such as Tyler Durden from the film *Fight Club*.

Post-Recession Problems: HFT and Dark Pools

Although, a large portion of the populace relies on the mainstream press for news, the alternative framework provides the readers with a detailed and investigative outlook on particular cases. The mainstream press has the most readers and publications such as *The New York Times* and *The Wall Street Journal* are viewed as highly reputable. In

contrast, the alternative press is growing rapidly, but still has relatively few readers and its heterogeneous constituent writers rarely have the same status as the mainstream publications. The alternative press often appears more willing than mainstream media to value transparency and to interrogate critical details. In addition, whistleblowers that expose critical information are often interviewed by alternative media sources for valuable insights. Unlike the mainstream press that commands a powerful reputation, the alternative press does not possess much social standing. However, the alternative press has built an incredible momentum over the years, mainly derived from the expansion of the Internet. Generally, alternative discourses found in the alternative media provide new viewpoints on the global economic crisis by giving voice to marginalized experts and by critically addressing issues mainstream media may have incentives for evading.

This section will draw on the alternative media to address some of the disregarded consequences of financial practices that contributed to the 2007 financial crisis, such as high frequency trading, the unregulated derivatives market, and the negative consequences of Large-Scale Asset Purchase (LSAP) or Quantitative Easing (QE). These issues are addressed in the alternative press in great detail, but not typically examined beyond a few token stories in the mainstream news accounts.

Technological innovations have opened new opportunities for investors and financial firms using automated trading systems based on algorithms that are physically situated close (co-location) to the stock exchanges (NYSE, NASDAQ, etc.). As the U.S. economy transitioned from industrial production to a market-based economy, financial profits became the cornerstone of the global economy. The introduction of the digital age in the 1970s and its rapid development since the 1980s sparked the financial sector to

another level of growth. The utilization of computers at the exchanges allows for more capital accumulation across cities, nations, and continents. Over the decades, the sophisticated development of processors and communication links have enhanced the traders' abilities to outwit the financial capitals around the world, from Wall-Street titans to London, and other well-known trading destinations (Essential Intelligence, 2012).

According to Brown (2010), high-frequency trading (HFT) operates automatically using high-speed processors that are controlled by intricate algorithms that process orders, analyze stocks, and accumulate large sums of profit at an unimaginable speed. The two key factors of speed and proximity executed in HFT generate considerable advantages to the sellers and buyers. To give the audience a better understanding of HFT and its advantages, Brown (2010) states:

Like the poker player peeking in a mirror to see his opponent's cards, HFT allows the program trader to peek at major income orders and jump in front of them to skim profits off the top. And these large institutional orders are our money – our pension funds, mutual funds, and 401Ks. (Brown, 2010).

In the recent years, the mechanization of HFT is dominating the stock exchanges: “As of 2010, 50 to 70% of all stock trades were done by high frequency trading computer algorithms. Morgan Stanley has shown that the percentage of HFT in the stock market has skyrocketed to 84%” (Washington's Blog, 2012b). Thus, the new culture of computerized trading system is part of the process of eliminating flesh-and-blood on the exchange floors.

Paul Wilmott's describes HFT as a dangerous tool in today's market:

The problem with the sudden popularity of high-frequency trading is that it many increasingly destabilize the market. Hedge funds won't necessarily care whether the increased volatility causes stocks to rise or

fall, as long as they can get in and out quickly with a profit. But the rest of the economy will care. (Durden, 2009b).

In an interview with Joe Saluzzi, Wilmott explains that computer-trading programs dominate the stock markets and also make large sums of capital, regardless of whether the stocks shift up or down (Washington's Blog, 2009):

Specifically, the program traders collect an average of quarter of a penny per share every time they buy. Even if they sell it at same price of fraction of a second later, they make another quarter of a penny when they sell... Program traders claim that they are providing liquidity for the markets. But they aren't. They're simply providing volume (remember 70% of the volume in the stock markets are from computer program trading). This distorts basic information about the markets, and confuses real investors' view of what is going on. (Washington's Blog, 2009a).

The manipulation and distortion of market numbers through high-frequency trading illustrate the illegality of routine market operations.

Considered one of the prominent participants in the world of high-frequency trading, Goldman Sachs went on a financial accumulative rampage in 2009 by earning over \$100 million per day on 116 out of 194 trading days by utilizing the method of HFT at the Alternative Trading System (ATS) (Brown, 2010). Over the years, high-frequency trading has arguably become the largest source of income for Wall Street banks.

According to Zero Hedge's Durden (2009b), Goldman Sachs accumulated \$11.6 billion in revenue and they are continuing the tradition of obtaining large wins and minimal losses. Although Goldman is making lucrative profits from HFT, Durden (2009b) begs the question, is this Ponzi scheme?

HFT's merely perpetuate the same Ponzi market mythology last seen in the Madoff case, but on a massively larger scale. When it all blows up, the question is whether the SEC will go after the perpetrators of this pyramid with the same zeal that it pursued Madoff himself. We think not. (Durden,

2009c)

Since there is very little faith in the SEC's ability to regulate high-frequency trading, some have offered potential regulatory suggestions to prevent the distorting of market prices:

Saluzzi says that one way to curb this manipulation and distortion of the markets is to force program traders to wait 1 second between buying and selling a stock. In their make-believe world, a second is an eternity....so forcing a 1-second delay would reduce the attraction and profitability of program trading. (Washington's Blog, 2009b).

Another proposed check on HFT is a Tobin tax – a very small tax on every financial trade. Proposals for the tax range from .005% to 1%, so small that it would hardly be felt by legitimate “buy and hold” investors, but high enough to kill HFT, which skims a very tiny profit from huge number of trades. (Brown, 2010)

There is very little faith in the United States government willingness to propose those solutions listed above to remedy the dangers of high-frequency trading because Wall Street banks and firms will heavily lobby to nullify any forms of regulatory acts, similar to what transpired with the Volcker Rule.

Recently, two government regulatory agencies, the Securities Exchange Commission (SEC) and the Commodity Futures Trading Commission (CFTX), have investigated the hazards of the high-frequency trading market:

The Securities and Exchange Commission and Commodity Futures trading Commission have sharpened their focus on high-frequency and algorithmic trading since May 6, 2010, when about \$862 billion was erased from stock values in 20 minutes before share prices recovered from the plunge.

The CFTC has been considering issuing a so-called concept release, a step prior to formal rulemaking, which could lead to new testing, supervision and oversight requirements for high frequency and automated trading. (Krieger, 2010)

Two major themes stand out in this passage: “sharpening their focus” and “considering a concept release.” It sounds as if these two financial regulatory agencies are always late to the step or ten behind. Monitoring HFT is already considered a daunting task for the regulators because many of the financial transactions occur in “dark pools” away from the traditional exchanges, such as the NYSE. ‘Stealth Trading,’ as it is known, enables high-frequency traders to perform financial transactions unmonitored in secrecy.

In an interview, Scott Patterson shared his thoughts on the lack of regulatory actions by the SEC concerning high-frequency trading and dark pools:

Mary Schapiro as much as admitted to Congress last year that she and her agency can’t surveil the market. That really is worrisome for obvious reasons. So what are they waiting for? It’s true that recently the SEC approved the so-called consolidation audit trail, or the CAT, which is billed as a giant eye in the sky for the market. But it’s still in the planning stages and who knows when it will actually be implemented-or whether it will actually be able to capture what’s going on. (Smith, 2012)

This is just a small sample of the regulatory incompetence and the lack of control, which allow Wall Street traders the freedom to accumulate profits in the most corrupt ways. Recently, the flash crash (see chapter 2) that occurred on May 2010 prompted the SEC to “sharpen their focus” as Dow Jones nearly lost 1000 point within a matter of minutes, but no regulatory acts concerning HFT has been passed since. If these regulatory agencies fail to take charge in regulating the HFT market, constant flash crashes may become prevalent in the near future, thereby devastating the global stock markets. Now, discussion turns to briefly discuss the unregulated market of financial derivatives, which acts very similar to options and futures.

Unregulated Market of Financial Derivatives

Financial derivatives pose major systemic risks to the global economy, yet the US government and the policymakers have failed to develop new derivatives rules.

According to Charles Morris, derivatives “derive their value from other instruments. An option is the right, but not the obligation to buy or sell a stock at a specific price within a specific time” (Morris, 2008). When describing the world of financial derivatives,

Warren Buffet coined the term, “financial weapons of mass destruction” (Das, 2010).

When we hear the word “derivatives,” it may resurrect cruel memories of calculus, but a financial derivative is a legal contract that derives its value from another asset, such as current or future valuation of commodities, government bonds, stocks, currencies or change of interest rates (Phillips, 2009). In addition, derivatives are used as insurance, hedging a bet that a loan may or may not default prior to its expiration date

(Demonocracy.info, 2012). Essentially, the unregulated derivatives market operates similar to a gigantic casino, but with future values; therefore, a trader is not prohibited from purchasing a derivative on an existing derivative (Demonocracy.info, 2012).

Janet Tavakoli, an expert on derivatives, stated in an interview conducted by Chris Martenson that the derivatives market played a critical role during the financial crisis in 2008. Tavakoli claims the main problem is controlled fraud by the Wall Street Bankers (Taggart, 2012):

The root causes is control fraud – people in the financial system being able to do whatever they want and remain unchecked. Where you have a group of individuals who are well rewarded for this kind of behavior and yet there is no punishment for fraud. As long as we keep that in place, you will see more of the same. The way the Fed and regulators have chosen to deal with it is to pretend it’s not happening and just continue to print money. And, as I say, it acts as a neurotoxin in the financial system.

(Taggart, 2012)

Tavakoli's description of derivatives as neurotoxins highlights the danger they pose to the American financial system.

Tarpley argues in the alternative media that the lack of management and regulations of financial derivatives have caused a pivotal downturn in the contemporary crisis (Tarpley, 2010):

Financial derivatives have come to represent the principal business of the financier oligarchy in Wall Street, the City of London, Frankfurt, and other money centers. Politicians and the news media to hide and camouflage the central role played by derivative speculation in the economic disasters of recent years have made a concerted effort. Journalists and public relations types have done everything possible to avoid even mentioning derivatives, coining phrases like "toxic assets," "exotic instruments," and – most notably- "troubled assets," as in TARP. (Tarpley, 2010)

This is an interesting observation by Tarpley because the mainstream media failed to focus in great detail the risk posed by the overblown derivatives market. During the 1990s, Clinton's financial advisors, Greenspan, Summers, and Rubin deliberately ignored and shutout Brooksley Born of the CFTC in her attempt to warn the Clinton administration of the systemic risks involving over-the-counter (OTC) derivatives. The mainstream media failed to give voice to Born's concerns. Had Greenspan, Summers, and Rubin decided to act upon her warnings regarding the OTC derivatives market, the severity of the 2008 financial crisis may have been subdued. Instead, the consequences of ignoring the monstrosity of the outstanding derivatives market will continue to be at the heart of the next financial crisis.

The derivative market has triggered a downfall involving the large banking institutions worldwide. An article written by Actindependent.org (2009), decodes some of the communication messages during the time when Bear Stearns filed for bankruptcy:

Bernanke warned against ‘chaotic unwinding.’ All these code words are signals that derivatives are being talked about including speculative instruments as options and futures. Derivatives also include the credit default swaps so prominent in the fall of AIG, collateralized debt obligations, structured investment vehicles, asset-backed securities, mortgage backed securities, auction rate securities, and a myriad of other toxic variations. (Actindependent.org, 2009)

The mainstream press’s mystification of financial “terms” such as credit default swaps and collateralized debt obligations impedes the dissemination and public understanding of vital information about the causes, consequences, and continued risks posed to the global economy by the unregulated and largely dark derivatives markets.

Since the implementation of the Commodities Future Modernization Act (2000), America’s top banks have spiraled out of control with respect to the value of outstanding derivatives. The accounting valuation of derivatives has increased the size and riskiness of America’s largest banks. Back in the early 2000s, the 10 largest banks authorized about 55% of all U.S. banking assets; however, the top 10 banks today control about 77% of all U.S. banking assets (Snyder, 2011). As explained by *Zero Hedge*, four U.S. banks now account for 95.9% of total derivative exposures: JP Morgan Chase with \$78.1 trillion, Citi with \$56 trillion, Bank of America with \$53 trillion and Goldman Sachs with \$48 trillion (Durden, 2011). Unfortunately, many of the biggest banks primary assets are composed of derivatives. These large banks are not only growing, but also their risk exposure hit an all-time high. The “too big to fail” banks in the United States have accumulated more than 200 trillion dollars of exposure to derivatives, which is equivalent

to three times the size of the entire global economic system (Snyder, 2012). Unlike previous times, if the derivative bubble pops in the near future, there is no government or a central bank in this world possessing enough bailout money to save the financial sector without wildly inflating money supply by rapid and massive money printing. One essential point people must understand is that a sovereign nation such as the United States possesses the luxury to always 'print' money from its central bank; therefore, it can never become insolvent as long as the debts and liabilities are denominated in U.S. dollars. However, rapid money printing can cause massive inflationary pressure and de-stabilize domestic and international trade and financial transactions.

According to Michael Snyder, the derivative market was formed to hedge risks, but the market spiraled out of control with speculative bets, drastically increasing the market size from \$600 trillion to roughly \$1.5 quadrillion (Snyder, 2011). To help the readers understand the notional figures, Graham Summers of Capital Research provided the readers with a better understanding of outstanding derivatives:

If you add up the value of every stock on the planet, the entire market capitalization would be about \$36 trillion. If you do the same process for bonds, you'd get a market capitalization of roughly \$72 trillion. The notional value of the derivative market is roughly \$1.4 quadrillion. I realize that number sounds like something out of Looney tunes, so I'll try to put it into perspective.

\$1.4 Quadrillion is roughly:

- 40 TIMES THE WORLD'S STOCK MARKET

- 10 TIMES the value of EVERY STOCK & EVERY BOND ON THE
PLANET.

- 23 TIMES WORLD GDP

It is nearly impossible to conceive a trillion dollars, but to break thought the threshold of “quadrillion” points to the madness that is associated with Wall Street. Even though the Great Recession (2007-2009) concluded, it is only a matter of time before the global economy experiences another reckoning crash of the derivatives market. There is not enough money to go around without unprecedented money printing for a series of global bailouts as the central banks around the world will be forced to swallow the bitter pill they avoided back in 2008. The sheer size of the derivatives market is a critical threat to the world’s economy. Since the system has become more intricate over the past several decades, some believe that the derivative contracts are nearly impossible to comprehend and as long as they stay unregulated, the assessment of financial risks will be tough to gauge (Washington’s Blog, 2012). The next theme found in the alternative media is the Federal Reserve’s actions of purchasing United States treasury bonds and mortgage-backed securities by printing obscene amounts of money from the United States Treasury.

Quantitative Easing (QE)

To escape from the financial agony of debt at unprecedented levels, there are three different methods:

1. Create GDP growth to grow out of debt
2. Increase taxes
3. Inflate out of debt.

The method adopted by the Federal Reserve to keep the interest rates capped at extremely low levels attacks the value of the U.S. dollar. After the collapse of Lehman Brothers in

2008 and the TARP bailouts, the United States Treasury and the Federal Reserve have engaged in historic levels of purchasing treasury bonds and mortgage-backed securities known as “money printing,” “Quantitative Easing (QE), or Large-Scale Asset Purchases” (LSAP). These actions have been covered most extensively in the alternative press, particularly by alternative financial news sites, such as Zerohedge.

In this process of “quantitative easing,” the Fed purchases financial assets (usually treasury securities) from banks and other financial institutions (FI). This adds capital to the FI balance sheets (hence the term money printing). When the Fed purchases the securities, the security asset is transferred to the Fed’s balance sheet, and the FI gets “virtual” money on its balance sheet (Swann, 2012). Many experts and financial observers covered by the alternative press are opposed to this method of monetary stimulus due to its inflationary tendencies and consider the policy to be the “last resort.” Previously, QE method was utilized by the Japanese Central Bank in the 1990s, but was ineffectively as they have engaged in nine more QE’s.

Going back to the Keynesian theory of government intervention, one method of stimulating a stagnant economy is to suppress interest rates for money that banks lend to one another. The Federal Reserve slashed interest rates from 5.25 percent to 0.00 percent and initiated large sums of printing money (Das, 2011, p. 340). In a simple scenario, if Well Fargo has excess capital (cash) and they decide to lend that extra money to JP Morgan Chase at a suppressed interest rate then everyone begins to borrow and spend, resulting in a stimulated economy. However, this method has not worked and it is not presently working to stabilize the current state of the U.S. economy as will be explained below.

To give the audience a brief background there has been three separate instance of LSAP in the past. The Federal Reserve's first round of LSAP commenced in 2008 with the aim of devaluing the strength of the U.S. Dollar on foreign exchange markets (Rickards, 2011, p. 33). In 2008, the Fed initiated a mass purchase of \$500 billion in mortgage-backed securities or toxic mortgages that destroyed the system under President George W. Bush. A year later, the Fed announced it would purchase another \$750 billion in mortgage-backed securities (Swann, 2012). However, the monetary easing did not end with LSAP from 2008-2009. A year later, the Fed decided to proceed with another round of LSAP. This second round of LSAP amplified the cost structure of the majority of the exporting countries and of the rapidly growing economies around the globe (Rickards, 2011). From November 2010 to June 2011, the Fed purchased approximately \$600-\$800 billion in U.S. Treasury Bonds by printing nearly \$75 billion per month. It also had another effect as it deposited additional cash reserves in the European Central Bank (ECB) (Swann, 2012). To continue, during this phase of LSAP 2 funding period, cash reserve of foreign banks increased from \$308 billion to \$940 billion (Swann, 2012). However, is the third time the charm?

The Fed is set to significantly purchase two of the most historic investments in the United States, mortgage-backed securities, and treasury bonds for an unlimited duration. By implementing QE, the Fed is forcing investors money into risky Wall Street investments because of the suppressed interest rates (0%) available to savers and investors. The Fed purchases the safe bets, which would lower their return making corporate bonds and dividend paying stocks more appealing (Swann, 2012). Projected to print 85 billion dollars a month starting in January 2013, the Fed is set to purchase \$40

billion a month in mortgage-backed securities and \$45 billion in 10 to 30 year U.S. treasury bonds (Zero Hedge, 2012; Miller, 2013). By the end of 2013, the Federal Reserve's balance sheet will be roughly four trillion dollars. The practice of "money printing" produces inflation, which even venture into hyperinflation; however, one major reason why the U.S. economy is not experiencing dangerous levels of hot inflation is due to the Shadow Banking System. The shadow banking is essentially a system of non-financial establishments that borrow capital in the short-run to invest in long-term assets. According to Das (2011), as the shadow banking system expands, risks are transferred from unregulated banks to unregulated vehicles, making the risks difficult to represent and calculate. This particular system generates credit-money designed by the banks and does not participate in the real economy (Demonocracy.info, 2012). Since the crisis of 2008, The Shadow Banking System has been deleveraged and it must sell assets to acquire new capital, which is derived from the Fed in order to pay back others (Demonocracy.info, 2012). Overall, the Federal Reserve must pump at the minimum of \$3.9 trillion to stabilize the Shadow Banking System.

In an interview with *The Real News Network*, economist Michael Hudson stated LSAP or QE has never proven to work. He stated this latest round of QE3 is a program for the Fed to supply money to the Wall Street banks until Beethoven writes his 10th Symphony. There has never been a correlation between QE and employment whatsoever (Jay, 2012). Hudson further added, "The crooks have taken over the economy and are trying to bail themselves out of the mess that they are in, so that they can somehow re-bid up real estate prices to restore the happy bubble economy that led to all these problems to begin with. Of course, the end of this will be yet another bailout in QE4 and QE5" (Jay,

2012).

Unfortunately, this is the state of the global economy moving forward. The unregulated derivatives market significantly exceeds the global GDP. The dangerous cyber game of high-frequency trading (HFT), which is capable of severely destabilizing the market, escalates. The Federal Reserve and Treasury's engagement in unlimited rounds of LSAP/QE to "maintain" price stability and "lower unemployment" exacerbates instability and does not stimulate the real economy. Five years after the Lehman crisis, volatility in the market remains high despite the Dow Jones Industrial hitting record levels by surpassing over 14,000 points in March 2013 because high unemployment and underemployment persist, causing further debt defaults and putting downward pressure on corporate profits. Uncertainty and angst among the populace remain as society progresses into the future. There is a clear distinction between the mainstream and alternative press' style of framing news. While, both remain factual in their reports, alternative press digs a bit deeper by revealing information that the mainstream press dares not to touch such as the Shadow Banking System, the sheer amount of unregulated derivatives, and the dangerous world of high-frequency trading (HFT). As long as the mainstream press prolongs dishonesty and trivialization of economic fraud in this "Alice in Wonderland" economy, the advocacy movement within the alternative media will continue to increase amongst the populace.

Conclusion

Although the alternative media outlets tend to carry a smaller group of followers in comparison to the mainstream press, the alternative media discourses framed the severity of the global economic crisis in a grim manner. Unlike the mainstream media's tactic of ignoring or trivializing the core issues such as high frequency trading and the derivatives market, the mainstream press offers a narrow range of analysis and perspectives on the magnitude of fraud. In contrast, the alternative discourses found across the Internet often provided in-depth analysis from a range of perspectives not widely represented in the mainstream news outlets. *Zero Hedge*, for example, specifically targeted Goldman Sachs by unraveling some of their fraudulent strategic trading tactics to the readers (Zero Hedge, 2009b). By sharing data on the staggering earnings, profits, and manipulative schemes, the alternative press is able to foster a critical look at those corporations and individuals involved in questionable or outright corrupt financial practices. The audience is able to gain further insight by stories that unpack the culture of afterhours trading and the mysterious world of dark pools where the atmosphere is unregulated and manipulated for profiteering. In some instances, these alternative websites operate like whistle blowers because they are sharing sensitive information regarding the financial firms.

Other alternative sites utilized the discourse of sarcasm and mockery to communicate to the readers. Financial blogger named, Michael Krieger facetiously states:

Wow, that makes me feel a lot better. Two years sharpening their focus. They are considering a concept release! Must be busy working on the Jon Corzine case right? Which beach is he laying out on this week? (Krieger, 2012)

Krieger is mocking these soft regulatory agencies for failing to supervise properly. In another account, Webster Tarpley slammed the mainstream press for misinforming the public by failing to associate derivatives with credit default swaps, collateralized debt obligations, etc. Tarpley states the mainstream media refuse to associate the term, “derivatives” in relation to the collapse of 2008. Janet Tavakoli claims derivatives were at the center of the crash. Overall, the bluntness, transparency, in-depth analysis, and humor of the alternative press facilitate a view of the crisis from more critical perspectives.

In times of economic turbulence, financial transactions involving high-frequency trading and derivatives will most likely cause the next economic collapse. Thriving under an unregulated market system, high-frequency trading is capable of triggering flash crashes similar to the May 2010 fiasco that devastated the NYSE. An implosion of the derivatives bubble will make the Great Depression look like child’s play. The central banks around the world cannot continuously bailout the financial institutions, such as the banking industry, auto industry, and insurance firms, in the aftermaths of repeated economic recessions without eventually sparking destabilizing inflation. How will the policymakers respond when the \$1.4 quadrillion derivative bubble burst? The regulatory agencies are always a step, or ten, behind as they fail to adjust, giving Wall Street the freedom to set their own rules. As each crash is more severe than the previous, it is only a matter of time until our society faces another economic meltdown. The consequences of ignoring the actual problems, such as outstanding derivatives, high-frequency trading and continuous creation of financial bubbles that distorts the market such as education and mortgages, will be at the heart of the next crisis.

On July 26, 2012, in a shocking statement, Sanford Weill expressed a change of heart stating the banks have grown too large and to counter this problem, downsizing the banks is a necessary process. *The New York Times* published an article covering a story on Sanford Weill, who led the advocacy movement in repealing the Glass-Steagall Act of 1933. During the late 90s, Sanford Weill of Citigroup benefited from the repeal of the banking act by consolidating commercial lending and investment banks under one entity. This initiated the rise of mega banks and monetary transactions, thus ushering in a new era of deregulated finance (de la Merced, 2012). Driven by extreme accumulations of capital, risks, bets, and bonuses, the financial opulence was short-lived when Lehman Brothers filed for bankruptcy in 2008. Although he does not regret his advocacy efforts during the late 90s, Weill is currently advocating for a sensible banking regulation. I commend Sanford Weill's for his encouragement for a sensible regulatory act that downsizes the banks in the first place.

However, is reviving the Glass-Steagall Act still relevant for fixing the current financial crisis? We must understand that the Glass-Steagall Act was drafted in 1933. The United States financial system has evolved tremendously, especially since the 1980s. Downsizing the banking industry is one of the issues at the center of the table, but why go through all that effort if the banking regulation is incapable of monitoring the contemporary problems, such as high frequency trading and dark pools? Carter Glass and Henry Steagall did not account for technological advancements and computerized banking transactions at the stock exchanges. It would be meaningless to reinstate the Glass-Steagall in its original form. Instead, Sanford Weill should have advocated for a new and improved version of the Glass-Steagall Act that oversees the current landscape

of the market system, such as high-frequency trading, the derivatives market, naked short selling, re-hypothecation, and other contemporary practices that heavily distort the market.

It is easy for Sanford Weill to appear on national TV and repair his public image by atoning for his financial sins, so the public can embrace him once more. However, why can't our society embrace a figure like Brooksley Born? She warned Clinton's financial advisors and Alan Greenspan of the OTC derivatives posed the ability to demolish the entire global economy. What about Byron Dorgan? During the repeal process of the Glass-Steagall Act, he warned the United States Congress of financial repercussions (Crawford, 2011, p. 129):

I think we will look back in 10 years' time and say we shouldn't have done this, but we did because we forgot the lessons of the past and that what was true in the 1930's is true in 2010. I wasn't around during the 1930's or the debate over Glass-Steagall... We has now decided in the name of modernization to forget the lessons of the past of safety and soundness. (p. 129)

In a similar stance with Byron Dorgan, Senator Paul Wellstone advocated against the repeal of Glass-Steagall (Crawford, 2011, p. 130):

I rise in strong opposition to S. 900, the Financial Services Modernization Act of 1999. S. 900 would aggravate a trend toward economic concentration that endangers not only our economy, but also our democracy. S. 900 would make it easier for banks, securities firms and insurance companies to merge into gigantic new conglomerates that would dominate the U.S. financial industry and the U.S. economy. This is the wrong kind of modernization because it fails to put in place adequate regulatory safeguards for these new financial giants, the failure of which could jeopardize the entire economy. It's the wrong kind of modernization because taxpayers could be stuck with the bill if these conglomerates become too big to fail. (p. 130)

Wellstone's concerns were not widely publicized.

The three individuals listed above accurately predicted the crisis of 2008 during the late 1990s; yet, their advocacy efforts went up in flames because our policymakers in Washington ignored their warnings and the public failed to encourage action because they lacked adequate knowledge about the real risks posed by de-regulation. The prosecutors during the Great Depression made a decision to prosecute the high-level banking executives that abused the stock market. It was a bold move to prosecute the high level banking officials during a time when bankers were embraced as celebrities, but Pecora took a stance by advocating for the greater good of the public. As well as hammering economic corruption, Pecora paved a path for a series of regulations starting with the Glass-Steagall Act in 1933. In contrast, our society is now stuck in the eye of a financial F5 hurricane. Our methods of paving over problems using bailouts, deregulation, quantitative easing (QE), and the lack of prosecutions will eventually backfire. With the derivatives market exceeding over a quadrillion and the unregulated high frequency trading running rampant in many parts of this world, something must give. No one knows exactly when that day will arrive, but I promise, this next financial crisis will have everyone trembling for their financial security.

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