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Willful Misconduct

By Richard W. Rahn
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It could probably be shown by facts and figures that there is no distinctly native American criminal class except Congress.

— **Mark Twain (1897).**

Twain's humorous quip, unfortunately, is all too close to the current reality. "Willful misconduct," a criminal offense, is legally defined as "intentionally doing that which should not be done or intentionally failing to do that which should be done, when knowing that injury to a person will probably result, or recklessly disregarding the possibility that injury to a person may result."

Congress, by failing to act in the case of a clear and present danger to parts of the American financial system, could reasonably be considered engaging in "willful misconduct." And here is why.

Decades ago, Congress created two government-sponsored enterprises (GSEs), Fannie Mae and Freddie Mac, to buy mortgages from banks with the goal of increasing the supply of mortgages to enable more Americans to become homeowners. (Fannie Mae was privatized in 1968, and Freddie Mac was created as a private company in 1970.)

It has been known for many years that both organizations were financial time bombs. Peter J. Wallison, former general counsel of the U.S. Treasury Department and now a senior fellow at American Enterprise Institute, wrote a book in 2001 warning of the unfolding disaster we now see, and recommended corrective action by Congress (as did other distinguished financial experts). Nothing was done.

Both GSEs are now in trouble, with Fannie Mae reporting it has $74 billion of subprime and Alt-A mortgage debt but only has about $45 billion in capital. If the GSEs fail, there would be a snowball effect.

In a new AEI report, Mr. Wallison notes: "Thousands of financial institutions hold GSE debt — in amounts that exceed their capital in many cases — and a requirement to write down the value of this debt would weaken the entire financial system as a whole and surely worsen the economic outlook."

If this occurs, Congress would most likely panic and declare the GSEs' mortgage-backed securities are now credit obligations of the U.S. government. The GSEs' combined debt of $4 trillion (yes, trillion) would suddenly be added to the debt of the United States, which would substantially injure the credit position of the U.S. and hurt every American taxpayer, who would ultimately be responsible for its payment. Unfortunately, there is no present alternative to this doomsday scenario because the GSEs are not covered by the normal bankruptcy laws, and Congress has not passed measures for an orderly windup of their businesses — clearly, willful misconduct.

It has been widely recognized in recent years that U.S. financial markets have been losing market share to their foreign competitors — which means both a loss of companies and jobs in the United States.

There have been four major reports on the situation, whose authors included both Democrats and Republicans. All these reports have come to the same conclusions. U.S. regulations have grown rapidly and are now far more burdensome in time and money than those of many responsible foreign competitors — notably the United Kingdom.

Many of the new regulations do not meet even the most basic cost-benefits tests. These regulations are primarily on securities issuers and have had little to do with the problems of the mortgage industry, where the current financial problems lie. The other reason both new and old companies are leaving the U.S. is the high litigation risk associated with private class actions.

A number of responsible proposals are before both the Securities and Exchange Commission and Congress to correct the problems of excessive regulation and tort law abuses, but neither the SEC nor Congress has taken necessary corrective actions. In the meantime, Americans employed in the securities industries unnecessarily lose jobs, and American companies find themselves at an international competitive disadvantage — because, again, Washington officials are engaged in willful misconduct.

Last week, members of Congress hauled up oil company executives to berate and threaten them because of high gasoline prices. As almost everyone knows, prices are set by supply and demand. If increases in supply do not keep up with demand, prices rise. Congress has restricted the supply of oil and oil products by not allowing drilling in the North Slope of Alaska, and in many U.S. offshore coastal and on-shore areas. Politicians have stopped construction of proposed new refineries. These actions have increased the price of gasoline and oil for all, causing increased economic hardship, particularly for the poor.

Those members of Congress who vote for oil drilling and refinery restrictions and then blame others for high oil prices can be accused of willful misconduct.

In 2006, voters turned over the leadership of Congress to the Democrats because the Republicans had overspent and in other ways violated voters' trust.

The Democrats, rather than learn from the Republican mistakes, are now engaged in even more willful misconduct. If they were private corporate executives and acted in such a manner, some might be convicted in a court of law, but members of Congress are protected from the consequences of many of their actions — except the wrath of the voters.

Perhaps if the incumbent party were thrown out every two years, eventually they would get the hint, and willful misconduct would cease.

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