SNL

Bank, Thrift & Broker/Dealer - Industry News

Bank tax blasted, but Obama says critics use 'twisted logic'

Thursday, January 14, 2010 4:12 PM ET
By Kevin Dobbs

President Barack Obama's plan to levy a special new tax on financial firms to recoup billions of dollars used to bail out banks and other firms was greeted with favor from political allies but disgust from critics.

The president's proposal, announced Jan. 14, seeks to guard taxpayers from up to $117 billion in losses tied to the U.S. Treasury Department's roughly $700 billion Troubled Asset Relief Program. TARP was created in 2008 under the Bush administration and continued under Obama as a way to pump capital into vulnerable financial companies in the wake of the panic that quickly developed after the collapse of Lehman Brothers Holdings Inc. and the near demise of American International Group Inc.

The program, funded with taxpayer money, is credited for propping up Wall Street, but it, along with other government efforts, fell short of preventing the country from plunging into the deepest recession in several generations and one that drove the nation's jobless rate above 10%. The lofty rate has fueled anger among many Americans, a bitterness that politicians have picked up on and directed at the banking industry.

The biggest companies that received the largest share of federal aid have faced the brunt of the backlash, and if Obama has his way, they will pick up the bulk of the cost under his proposed tax. Financial companies with assets of more than $50 billion — including Bank of America Corp., Citigroup Inc., JPMorgan Chase & Co., Wells Fargo & Co., Morgan Stanley and Goldman Sachs Group Inc. — will face a levy on their balance sheets.

The president, in a brief televised speech, emphasized that "only the largest firms … will be affected." Addressing the heads of those firms, he added, "I urge you to cover the costs of the rescue."

About 35 U.S. companies and about 15 U.S. units of foreign firms would be affected. An estimated 60% of the tax revenue will come from the 10 largest companies. Those in favor of the plan agreed with Obama that it is only fair for the largest players to step up to protect taxpayers from losses.

Dominique Strauss-Kahn, the head of the International Monetary Fund, told reporters in Washington that the Obama plan is on the right track and that it could be a model for other countries that had to bail out financial companies. "I really celebrate this proposal … because it shows the political momentum to move in this direction is still there," Strauss-Kahn said.

Obama said he expects the tax to generate about $90 billion over the first 10 years, and $117 billion over 12 years, an amount the administration estimated would ultimately cover all losses on TARP. Each company's tax rate will be based on its liabilities, excluding FDIC-insured deposits and insurance policy reserves.

Critics, however, say the last thing that an industry on the mend from a major downturn needs is another expense. A new tax, the thinking goes, could cut into earnings and, by extension, hinder lending and hiring, a development that could derail the recovery.

"There has to be a return to sanity" in Washington, Donald Musso, president and CEO of FinPro Inc., told SNL. "To get this economy going, we need to jumpstart lending, and you don't do that by adding more and more burdens on the banks."

Moreover, critics say, it appears the Obama administration is most concerned about addressing popular outrage and, additionally, rebuking the nation's largest banks for opposing the president's push for certain broad reforms, such as a new consumer protection agency. Gary Townsend, CEO of Hill-Townsend Capital LLC, emphasized that hundreds of smaller regional and community banks also have received TARP money but will, under the president's plan, escape the new tax.

"This really is dreadful policy," Townsend told SNL. "This is contrived to simply punish the big banks. … I think it is half-baked, not thought through well at all."

A team of analysts at Concept Capital wrote in a report that, "on the plus side … U.S. firms will not be at a competitive disadvantage" because the tax would also be applied to foreign banks' U.S. units. But they called the plan an "overall negative" for large financial firms.

Sam Pappas, president and CEO of Mystic Asset Management Inc., agreed. He noted to SNL that most of the biggest financial companies have already paid off TARP and the majority of the overall rescue funds have been repaid, with interest, giving the government a tidy profit.

"These companies have paid their dues, so I think this thing is just uncalled for," Pappas said. "You're penalizing companies for picking themselves up."

Obama, however, called such criticism "twisted logic." He said big banks and financial companies that failed to effectively manage risk created the need for TARP — a program the president said "was as necessary as it was unfortunate" — and therefore must pick up the tab. Moreover, he said, the new tax will discourage banks from returning to the risky lending and investment practices that led them down a perilous path of steep credit losses over the past two years.

"We cannot go back to business as usual," Obama said.

The tax would go into effect June 30 of this year and be in place for 10 years or until all TARP costs are recovered. The full details of the plan are slated to be delivered along with the president's presentation of his fiscal 2011 budget next month. The plan could then be modified by Congress.

The Democratic-controlled Congress, however, may not ease the terms for big banks. House Speaker Nancy Pelosi and House Financial Services Chairman Barney Frank have endorsed the president's plan, the Capital Concept analysts pointed out, and federal authorities are eager to ensure that big banks in particular atone for their collective role in hastening the nation's descent into recession. "This remains far from a slam dunk, but momentum is building by the day," the analysts said.

Most recently, on Jan. 13, top executives at Goldman, JPMorgan, BofA and Morgan Stanley were called before the Financial Crisis Inquiry Commission and successfully pressed to concede that they contributed to the financial industry's meltdown and the broader economic downturn.

In one candid moment, Goldman CEO Lloyd Blankfein said his firm and the financial industry as a whole made regrettable mistakes. "Anyone who says 'I wouldn't change a thing' I think is crazy," Blankfein told the commission.